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Ms. Ann E. Misback
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November 30, 2023

RE: Proposed Rule for Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions (Docket IDs OCC-2023-0011, FRS-2023-0226, and FDIC-2023-0062)

Dear Mr. McDonough, Ms. Misback, and Mr. Sheesley:

Americans for Financial Reform Education Fund (AFREF) appreciates the opportunity to comment on the Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve (Fed), and the Federal Deposit Insurance Corporation's (FDIC) interagency proposal for Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions.[1] AFREF is a nonpartisan and nonprofit coalition of more than 200 civil rights, consumer, labor, business, investor, faith-based, and civic and community

[1] Office of the Comptroller of the Currency, Federal Reserve System, and the Federal Deposit Insurance Corporation. Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions. 88 Fed. Reg. 180. September 19, 2023 at 64524 et seq.

groups dedicated to advocating for policies that shape a financial sector that serves workers, communities and the real economy, and provides a foundation for advancing economic and racial justice.

The proposed long-term debt rule is an important complement to the agencies' efforts to enhance financial stability and banking sector resilience — most importantly the pending Basel III endgame proposal.[2] The long-term debt proposal would extend the long-term debt requirements to more organizations (they already apply to the largest and most complex firms) to increase the resolution options for failed institutions. The 2023 cascading failures of Silicon Valley Bank, Signature Bank, and First Republic Bank highlighted the importance of additional capital guardrails for a wider array of financial institutions.

AFREF supports the agencies' goal of applying a long term debt requirement to banking organizations in categories II, III, and IV of the Fed's large banking organization tailoring framework and to large depository institutions.[3] The proposal would strengthen the liability structures of firms covered by the proposed rule and provide an added cushion in the event of failure.[4] As a group, banking organizations in category IV in particular, with total assets between $100 billion and $250 billion, have become overly reliant on uninsured deposits, and the long-term debt requirement would reduce the concentration of this unstable deposit base by adding more stable long-term debt to their capital structure. The eligible debt for this requirement is structured to be available in a resolution scenario to absorb losses after insolvency. This would expand the resources available to the FDIC to resolve a large bank without accessing the federal Deposit Insurance Fund or would reduce the costs to the Deposit Insurance Fund.

The proposal would require supervised banking organizations to maintain a more stable liability base and maintain a cushion in the form of long-term debt to absorb financial losses in a resolution scenario. The proposal would work in concert with the pending resolution planning proposals and pending resolution guidance (introduced in parallel in August 2023) that require certain depository institutions and consolidated banking organizations to file resolution plans and provide clarity on the expectations for strengthening these resolution plans.[5] Together, the proposals would provide the FDIC and the other agencies with better resolution roadmaps and the proposed long-term capital rule would undergird capital resources post insolvency to carry out an orderly resolution. A key objective is for the FDIC to have

[2] Proposed Rule by the Office of the Comptroller of the Currency, the Federal Reserve System, and the Federal Deposit Insurance Corporation. Regulatory Capital Rule: Large Banking Organizations and Banking Organizations with Significant Trading Activity. 88 Fed. Reg. 179. September 18, 2023 64028 et seq.

[3] Category II is defined as firms with ≥ $700 billion Total Assets or ≥ $75 billion in cross jurisdictional activity according to the Fed tailoring framework. Category III is defined as firms with ≥ $250 billion total assets or ≥ $75 billion in nonbank assets, with short term wholesale funds, or off-balance sheet exposure. Category IV is defined as other firms with $100 to $250 billion total assets. Source: Requirements for Domestic and Foreign Banking Organizations, Tailoring Rule visual.

[4] This includes large bank holding companies, certain large foreign-owned intermediate holding companies and large depository institutions.

[5] These proposals include: 1) FDIC Resolution Plans Required for Insured Depository Institutions With $100 Billion or More in Total Assets; Informational Filings Required for Insured Depository Institutions With at Least $50 Billion But Less Than $100 Billion in Total Assets (FDIC-2023-0060-0001); 2) Guidance for Resolution Plan Submissions of Domestic Triennial Full Filers; and 3) Guidance for Resolution Plan Submissions of Foreign Triennial Full Filers.

the tools and resources to oversee a large bank's resolution without disrupting the financial system and needing to access the Deposit Insurance Fund.

Many large banks, particularly the category IV firms with total assets from $100 to $250 billion, are over reliant on uninsured deposits that can present liquidity risks for troubled or distressed institutions. The 2023 bank failures demonstrated that banks in this asset band can not only collapse but also transmit contagion to other firms. As the proposal notes, "in recent years, certain banks that are not global systemically important banking organizations (GSIBs) have grown in size and complexity, and new vulnerabilities have emerged, such as increased reliance on uninsured deposits."[6] These large banks' risk profiles grew at the same time as the prior administration's deregulatory agenda rolled back key safety and soundness guardrails for large banks, including regulatory capital, liquidity, stress-testing, and eliminating the resolution planning requirements for banks with total assets from $50 to $100 billion.

The large banks' increasing risk profiles and reduced guardrails set the stage for the financial crisis of 2023 and the failures of Silicon Valley Bank, Signature Bank, and First Republic Bank. All three banks were insured depository institutions of non-GSIB banking organizations with consolidated assets of over $100 billion. All three experienced rapid and significant withdrawals of uninsured deposits that drew depositor and investor attention to the underlying weaknesses in the banks' financial positions and prompted deposit runs and counterparty flight. These bank failures, the 2nd, 3rd and 4th largest in America's history, further highlighted the risk that one bank failure can transmit panic and lead to the failure of another firm, creating broader systemic risk across financial markets. The losses from these failures were not on the same scale as the widespread losses to Americans from the 2008 financial crisis, but the 2023 bank failures did result in costs to the FDIC's Deposit Insurance Fund of $34 billion.[7]

AFREF is generally supportive of the proposed long-term debt rule and offers observations and modest suggested improvements on some specific elements of the proposal most relevant to us and our coalition members. The proposed long-term debt requirement does promote safety and soundness, but it can only complement the more essential efforts to raise regulatory capital requirements for large banking organizations. As a result, while we support the proposal, we also highlight in our comments the ways in which a long-term debt solution on its own has not been successful historically and remains more valuable as an additive measure after substantially raising equity levels.

***Systemically important banks require guardrails to maintain sufficiently stable liabilities as a going concern and to cushion losses in the event of a failure:*** The proposed long-term capital rule extends appropriate safeguards to more financial firms. Category IV firms are systemically important and have demonstrated that they are ill prepared for an orderly resolution. The largest category I GSIBs are already subject to a long-term debt requirement and total loss absorption capacity (TLAC) based on the TLAC Rule

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[6] 88 Fed. Reg. 180 at 64525

[7] Gruenberg, Martin J. Chairman FDIC. "Oversight of Financial Regulators: Financial Stability, Supervision, and Consumer Protection in the Wake of Recent Bank Failures." Remarks before the Committee on Banking, Housing, and Urban Affairs. U.S. Senate. May 18, 2023.

of 2020.[8] Foreign-owned category II and III firms, while not subject to the U.S. TLAC rule, are subject to the global GSIB TLAC requirements imposed on their parents. Category IV firms, on the other hand, along with their subsidiary depository institutions, are not currently subject to any form of long-term debt or TLAC requirement.[9] The 2023 bank failures underline the importance of the regulators' proposed requirements for loss absorbing long-term debt resources to resolve category II, III and IV banking organizations and large depositories in a way that reduces costs and risk of disruption to the banking system.

AFREF supports the proposal's goals of diversifying large bank liabilities away from uninsured deposits and strengthening their resolvability. The long-term debt requirement would reduce the risk that uninsured depositors face losses, lower the potential for runs on uninsured deposits, and should contribute to preventing contagion and financial system instability that would result from a large bank's failure. Banks would be required to maintain a form of debt capital with which to "absorb losses and create equity in resolution."[10] The FDIC would be able to use the proceeds of the debt issued by the failed bank in resolution to absorb losses by leaving it behind in the receivership estate of the failed entity. In this manner, the proposal would mitigate the risk that any depositor would take losses in the resolution. This proposal follows an advance notice of proposed rulemaking released by the Fed and the FDIC in October 2022 that looked at several possible changes, including a long-term debt requirement, to promote more orderly resolutions for large banks.[11]

AFREF supports the features of the rule that would prohibit large banks from engaging in certain activities that could complicate their resolution and also disincentivize these banks from holding the eligible long-term debt issued by other banks. These measures would reduce large banks' interconnectedness and the likelihood of spreading contagion among these banks during periods of financial market stress. The proposal would provide a three-year phase-in period and also allow certain outstanding long-term debt to count toward the minimum requirements to provide banks with a reasonable transition period to fulfill the required characteristics of eligible long-term debt instruments.

***Long-term debt proposal complements but cannot replace stronger capital standards:*** Notwithstanding AFREF's overall support, the long-term debt proposal should not distract from the critical importance of strengthening equity capital requirements to increase banks' safety and soundness and bolster financial system resiliency. The pending proposal to require that large banks hold more capital that stabilizes banks' balance sheets should be the primary focus of the agencies' efforts to strengthen the financial system and reduce systemic risk. The long-term debt proposal complements the efforts to strengthen bank capital,

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[8] Comptroller of the Currency, Federal Reserve, Federal Deposit Insurance Corporation. Total Loss-Absorbing Capacity, Long-Term Debt, and Clean Holding Company Requirements for Systemically Important U.S. Bank Holding Companies and Intermediate Holding Companies of Systemically Important Foreign Banking Organizations: Eligible Retained Income. 85 Fed. Reg. 59 Thursday, March 26, 2020, 17003 et seq.

[9] Board of Governors of the Federal Reserve Tailoring Requirements for Domestic and Foreign Banking Organizations, 2019.

[10] 88 Fed. Reg. 180 at 64527.

[11] FDIC. Resolution-Related Resource Requirements for Large Banking Organizations: Extension of Comment Period. 87 Fed. Reg. 242. December 19, 2022 at 77529 et seq.

but the long-term debt proposed rule cannot ameliorate systemic risk or reduce the risk of failure, it can only improve the resolution of banks that have already failed. As leading banking expert Anat Admati has reminded us, “by far the most important approach to enhancing financial stability and increasing loss absorbing capacity is a dramatic increase in equity requirements for banks and other financial institutions. Genuine, reliable, credible and cost-effective loss absorption *cannot* be achieved by any of the other means.”[12]

The long-term debt proposal can improve resolution optionality, but complex financial institutions may still be difficult to resolve even with long-term debt levels envisioned in the proposed rule. Further, Arthur Wilmarth, Professor Emeritus of George Washington University Law School, suggested in 2020, the long-term debt requirement, together with single point of entry resolution strategy and a total loss absorption capacity, may not guarantee seamless resolution of failed banks that are subsidiaries of financial holding companies: “It is also far from clear, based on historical evidence, whether the parent holding company of a failed systemically important institution can be placed in an OLA resolution without triggering contagious runs by the creditors of its subsidiaries.”[13]

Practically speaking, while resolution plans and long-term debt provide a regulatory strategy and a source of capital post resolution, they do not fully account for the need for a surviving bridge bank to have access to other resources beyond capital in resolution, such as sufficient liquidity to support an orderly resolution.

***Proposed long-term debt rule complements other pending safety and soundness, systemic risk, and resolution planning proposals — but capital standards essential first principle (Question 1):*** The long-term debt proposal complements existing and proposed rules to strengthen safety and soundness of the firms and increase financial system resiliency. The proposal establishes long-term debt requirements based on firms’ regulatory capital requirements to establish minimum percentages of long-term debt to deliver enough capital to the entity in the event of failure to meet the minimum capital ratios in the existing Basel III capital accord as a going concern in resolution. Consistent with the GSIB TLAC rule, the proposed long-term debt requirement would be calculated as the amount of capital necessary for a surviving bridge company in resolution to meet ongoing capital requirements. The proposal pegs the needed capital in resolution as equivalent to 7 percent of risk weighted assets, 4.5 percent of average total consolidated assets, or 3.5 percent of total leverage exposure. The size of the long-term debt requirement in the proposal would be based on the higher of 6 percent of the firm’s risk-weighted assets, 3.5 percent of its average total consolidated assets, or 2.5 percent of its total leverage exposure.

The long-term debt proposal would work in concert with the pending regulatory capital to strengthen a bank’s capital structure. Increasing equity capital can absorb losses and reduce the potential impact from a firm’s failure without the burden of debt service managing through periods of stress. The long-term debt

[12] Admati, Anat R. Stanford University School of Business. “The Missed Opportunity and Challenge of Capital Regulations.” December 2015 at 11.

[13] Wilmarth, Arthur E. “SPOE Plus TLAC = More Bailouts for Wall Street.” *35 Banking & Financial Services Policy Report No. 3*. March 2016 at 1 to 14.

proposal notes that regulatory capital is likely to be significantly or completely depleted in the lead up to a failure, which is why having long-term debt capital that can be deployed in the surviving bridge bank is a significant benefit to the FDIC in carrying out an orderly resolution. But increasing large banks' equity capital requirements would be more effective in reducing the risk of failure and reducing systemic risk that can better maintain depositors' and other counterparties' confidence in the banking system and making the financial system more resilient. Anat Admati of Stanford Business School observed:

> Increasing equity requirements substantially brings about numerous benefits beyond increasing loss absorption capacity that allows banks to continue making loans after incurring losses without needing support. With more equity, liquidity problems, runs and all forms of contagion are less likely. Moreover, any loss in the value of the assets is a smaller fraction of the equity, thus fewer assets must be sold under distressed conditions to 'delever.' Better yet, distortions in banks' lending and funding decisions due to overhanging debt are alleviated. As another bonus, more equity is the best way to reduce the implicit guarantees subsidy that distorts markets and rewards recklessness.[14]

The pending Basel III Endgame and GSIB surcharge proposals are essential to strengthen regulatory capital to prevent runs on banks' liabilities, support orderly resolutions, and strengthen the financial system. Banks' safety and soundness would benefit from equity capital levels substantially above and beyond the current Basel capital framework.

The long-term debt proposal is one of several proposals since the banking crisis of 2023 that would increase the safety and soundness of non-GSIB large banks and improve their capacity to be resolved in an orderly manner in the event of failure. We support both objectives of large banks being safe and sound and the FDIC having the resources and tools to oversee orderly resolutions of big banks in the event of their failure. Long-term debt requirements in isolation are unlikely to provide sufficient backstops. As Admati noted, "In the past, the inclusion of debt as part of capital regulation has not worked. Tier 2 capital included only debt-like securities and even Tier 1 capital allowed many non-equity claims that were held by investors expecting specific returns. Yet, holders of such claims did not suffer losses even when banks ran into trouble and received government bailouts."[15] Regulators must ultimately recognize from experience that equity is the only form of non-runnable capital, and increasing banks' equity capital by finalizing the proposed capital rules is paramount to preventing further bank failures and contagion and avoiding bank bailouts.

***Proposed long-term debt rule appropriately extends requirements to more institutions (Question 2 and 3):*** The long-term debt proposal applies to non-GSIB large banks, including categories II, III and IV of the Fed's tailoring framework,[16] in order to subject these firms to a long term debt requirement consistent

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[14] Admati, Anat R. Stanford University School of Business. "The Missed Opportunity and Challenge of Capital Regulations." December 2015 at 8.

[15] Admati, Anat R. Stanford University School of Business. "The Missed Opportunity and Challenge of Capital Regulations." December 2015 at 11.

[16] Fed Tailoring Visual.

with the GSIBs' requirement in the TLAC Rule of 2020.[17] The agencies propose to require bank holding companies and other holding companies in these categories, as well as large depository institutions with total assets of over $100 billion, to hold an amount of long term debt on their balance sheet.

The proposal also appropriately covers savings and loan holding companies. These entities are similar to large banks, with the financial scale, complexity, and other risk factors with the potential to disrupt financial markets. These institutions take deposits and make loans — including mortgages and credit cards — but also engage in margin lending and other complex nonbanking activities that pose higher levels of risk. SLHCs also have higher concentrations of deposits than banks, less diverse liability structures, and are more vulnerable to structural interest rate risk due to concentrations of longer duration home mortgages.

The proposal addresses the risks of deposit runs at large firms based on their concentrations of long-term deposits and other less stable liabilities. The Spring of 2023 failures of category IV institutions Signature Bank, Silicon Valley Bank, and First Republic Bank prompted depositor outflows at other similarly-sized banks and contributed to the market turbulence and the failure of Credit Suisse. At the time of its failure, Credit Suisse had a category III intermediate holding company and category II U.S. operations. The failure of covered holding companies or covered insured depository institutions could potentially have a negative impact on U.S. financial markets and the economy. These failures can spread panic that prompts debt and equity holders to withdraw from financially vulnerable firms and markets and to shy away from opaque assets with uncertain risk. The proposed rule creates a parallel requirement at the insured depository institution level, which improves resolution for the bank in addition to the parent company, and the long-term debt would be more directly available to absorb losses in each entity in the event of a failure and resolution.

***Higher concentrations and over-reliance on uninsured deposits should be considered in the criteria for the long-term debt requirements (Question 4):*** A bank's overreliance on uninsured deposits should be an additional characteristic in determining the coverage of the proposed rule. Firms that are overly concentrated in uninsured deposits should be subject to a requirement to diversify their funding into longer-term liabilities, which would reduce banks' reliance on uninsured deposits, irrespective of institutional size. The criteria could address both the scale and concentration of uninsured deposits. For example, a firm could be considered over-reliant on uninsured deposits if over 40 percent of total deposits were uninsured, and the volume of uninsured deposits exceeded $20 billion.

***Long-term debt proposal strikes right balance to cushion against potential failure (Question 5):*** The agencies' approach to sizing the long-term debt keyed to existing regulatory capital requirements, referred to as the capital refill framework, tailors the debt requirement to what the surviving entity would need to meet capital requirements during and after resolution. Each covered entity would be required to hold a minimum amount of eligible long-term debt that could fully recapitalize and replenish its going-

[17] 85 Fed. Reg. 59. March 26, 2020 at 17003 et seq.

concern capital to meet minimum Tier 1 leverage capital requirements if the entity's going-concern capital was depleted and it entered resolution.

The proposal details the calculation that requires entities to have an external long-term debt requirement equal to 7 percent of risk-weighted assets that matches the combination of tier one capital (4.5 percent of risk-weighted assets) and capital conservation buffer (2.5 percent). The proposal further reduces the long-term capital by 1 percentage point to allow for balance sheet depletion that brings the net requirement to 6 percent of risk-weighted assets. The capital refill theory suggests that losses leading to failure would deplete risk-weighted assets and capital, justifying the balance sheet depletion allowance.[18]

The regulators must continue to evaluate the long-term debt requirement by considering any changes in capital requirements over time, as the proposal notes. This is especially true of any increases in the minimum required capital ratios currently being considered. If the going-concern capital requirements increase, the percentage of long-term debt required in insolvency according to the capital refill framework for both the holding company and any affiliated depository institutions would also need to increase.

AFREF emphasizes, as did many commenters on the original 2022 ANPR that is refined in this proposed rule,[19] that substantially increasing bank regulatory capital levels would be the most effective policy to improve the resiliency of covered entities and covered depository institutions and avoiding disorderly resolutions. Additional capital would proactively reduce the probability of large banking organizations' failing in the first place and increase the chance that a covered entity or depository institution would have remaining equity in the less likely event of a failure. While regulatory capital is likely to be significantly or more completely depleted in the lead up to a resolution, focusing on much higher capital levels would nonetheless provide a stronger bulwark against depositor runs, contagion, and disorderly resolutions and contribute to a more resilient financial system.

***Regulators should retain discretion to raise long-term capital requirements to address emerging concerns (Question 6):*** The calibration of the required amount need not be impacted by other factors, such as the level of uninsured deposits at depository subsidiaries, but the agencies must maintain language in the proposal that reserves the right of supervisors to require a firm to hold amounts greater than the proposed calibration would dictate. This discretionary authority would allow the supervisors to raise long-term debt requirements to address emerging issues, such as high concentrations of uninsured deposits or interest rate risks related to liquidity that became prominent in the 2023 failures.

***Long-term debt instrument eligibility should be limited to those securities that further the purpose of strengthening entities in resolution (Question 25):*** The regulators should limit the types of eligible instruments for long-term debt so that the resulting securities will more reliably meet the objectives of diversifying the liabilities away from uninsured deposits and making available long-term debt that can

[18] 88 Fed. Reg. 180 at 64530.

[19] *See* Board of Governors, Federal Reserve System and FDIC. Resolution-Related Resource Requirements for Large Banking Organizations. 87 Fed. Reg. 204 at 64170 et seq.

convert to necessary capital in a resolution scenario to absorb losses. The proposal recommends features that will increase balance sheet stability, will reliably be available to absorb losses in resolution, and will not include characteristics typically appealing to retail investors.

Eligible securities should be externally sourced, unsecured, with minimum remaining security but not in minimum denominations, and established under U.S. governing law. Further, the securities should have a plain vanilla structure (without links to other assets, indices, or benchmarks, and without contractual conversions or credit sensitive features, such as those that trigger accelerated payments). These features promote simplicity of structure and clarity about the risk. The plain vanilla features allow market participants to more easily monitor and interpret the subordinated securities and impose market discipline on the firm.

Precluding securities that are not in minimum denominations limits retail investor interest in purchasing the eligible long-term debt. A central purpose of the securities is to absorb losses in a failure scenario. Retail investors should not be the buyers of these securities, as they may not fully appreciate the deep subordination. These long-term debt instruments are positioned by design to absorb losses from more senior creditors. Retail investors should not be directly exposed to the eligible securities. The agencies should consider additional steps to further prevent the promotion of these securities to retail investors or to funds that invest on behalf of retail investors.

***Proceeds from the long-term debt should be invested in highly liquid capital securities (Question 34):*** The goal of the capital refill framework is to establish an appropriately-sized source of capital in the event of insolvency and failure so that all of the long-term debt can be allowed to default and the principal be converted to equity capital. However, the proposal does not account for other needs of the surviving, recapitalized company, notably whether the long-term debt will provide sufficient liquidity to achieve its resolution strategy. Particularly in a single point of entry resolution strategy, the going concern after failure would require a certain amount of liquid assets to maintain operations. Investing the proceeds of the long-term issuance in high quality liquid assets would further allow for the surviving entity to have sufficient liquidity in insolvency, in addition to conforming to minimum Basel III capital ratios.

***Proposal should strengthen "clean holding company" requirements (Question 40):*** The ''clean holding company'' requirements would improve the resolvability of covered entities and their operating subsidiaries. In particular, the proposal would prohibit covered entities from issuing short-term debt instruments to third parties, entering into qualified financial contracts with third parties, and having liabilities that are subject to ''upstream guarantees'' or that are subject to contractual offset against amounts owed to subsidiaries of the covered entity. The proposed "clean holding company" provisions should be strengthened to provide additional supervisory vigilance and resources to monitor financial relationships throughout the legal entity structure where affiliates rely on guarantees from depositories. Maintaining a clean holding company concept requires extra supervisory vigilance and resources to monitor financial interrelationships up and down the legal entity structure where an affiliate is relying on guarantees from a depository.

**Agencies should prohibit the issuance of more junior securities instead of a 5 percent cap to avoid any confusion about the role of the eligible long-term debt to absorb losses (Question 41):** The proposal would cap the amount of a covered entity's liabilities that rank at either the same priority as or junior to its eligible external long-term debt at 5 percent of the sum of the covered entity's common equity tier 1 capital, additional tier 1 capital, and eligible long-term amount. The regulation notes that "The proposed prohibitions and cap would apply only to the corporate practices and liabilities of the covered entity itself. They would not directly restrict the corporate practices and liabilities of the subsidiaries of the covered entity."[20] The agencies should consider instead prohibiting securities holders to be junior to the eligible securities in its liability stack, as the existence of more junior securities could undermine the clarity of the purpose of the eligible debt to be available to absorb losses in a resolution scenario. Since their inherent purpose is to absorb losses in resolution, the required features should establish that eligible securities must be deeply subordinated to all other creditors.

***Proposal appropriately expands the capital deduction framework for GSIBs and intermediate holding companies of foreign GSIBs (Question 50):*** The capital deduction framework must discourage banks from buying each other's long-term debt. The proposed rule would expand the existing capital deduction framework for long term-debt issued by the U.S. GSIBs and the intermediate holding companies of foreign GSIBs to include external long-term debt issued by covered entities and external long-term debt issued by covered insured depository institutions. The agencies included these requirements to provide comparable capital deductions to covered companies now that category II, III and IV firms are subject to long-term debt requirements:

> Requiring that U.S. GSIBs, U.S. GSIB subsidiaries, and Category II banking organizations apply the deduction framework to the LTD of a covered entity or IDI that issues externally would discourage these banking organizations from investing in such instruments, and would thereby help to reduce both interconnectedness within the financial system and systemic risk. Therefore, the proposal would expand the current deduction framework in the capital rule for U.S. GSIBs, U.S. GSIB subsidiaries, and Category II banking organizations to also apply to eligible external LTD issued by covered entities and mandatory or permitted externally issuing IDIs to meet the minimum LTD requirement set forth in this proposal by amending the capital rule's definition of covered debt instrument."
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> Notably, however, the recently released Basel III reforms proposal would subject Category III and IV banking organizations to the LTD deduction framework that currently only applies to U.S. GSIBs, U.S. GSIB subsidiaries, and Category II banking organizations and would apply a heightened risk weight to investments in LTD that are not deducted. Thus, if both this proposal and the Basel III reforms proposal are adopted as proposed, Category III and IV banking organizations will newly become subject to the capital rule's deduction framework for investments in LTD and the deduction framework would be expanded to apply to eligible LTD issued by covered entities and mandatory and permitted externally issuing IDIs.[21]

[20] 88 Fed. Reg. 180 at 64541.

[21] 88 Fed. Reg. 180 at 64545.

***Technical changes harmonize the proposal with existing TLAC rule for U.S. GSIBs and U.S. IHCs of foreign GSIBs (Question 63):*** The proposal includes technical changes to improve upon and align the proposal with comparable requirements in the GSIBs' TLAC rule of 2020. Most notably, this includes applying a 50 percent haircut to long-term debt meeting the TLAC requirement if the debt is greater than one year old but less than two years to maturity, which would improve the companies' management of the tenor of their eligible long-term debt. The proposed change would incentivize firms to reduce reliance on eligible long-term debt with maturities of less than two years and increase the loss absorption requirement for firms that rely heavily on eligible long-term debt with maturities of less than two years. These changes would harmonize provisions within the TLAC rule and address administrative concerns about the TLAC rule including the haircut for long-term debt used to meet TLAC requirements, minimum denominations for long-term debt used to satisfy TLAC requirements, and the treatment of certain transactions for clean holding company requirements.

***The agencies should prevent retail investors from buying the proposed long-term debt instruments, but if permitted must make the disclosure robust to avoid confusion about the purpose of the securities (Question 64):*** The subordinated nature of this long-term debt must be accompanied by robust disclosures about its purpose. The proposed disclosure includes clarifying that the purpose of the debt securities is to absorb losses associated with other creditors in resolution. In a failure scenario, these bondholders should therefore expect to lose 100 percent of their bondholder investment. These securities should not be offered to retail investors because of the potential for total investment losses in the case of a firm's default that makes them unsuitable for retail investors. However, if the agencies insist upon allowing these high-risk instruments to be sold to retail investors or to funds that make investments on behalf of retail investors, these securities should be clearly disclosed as deeply subordinate to other debt securities in the firm's liability structure. They are designed for the very purpose of absorbing losses subordinate to other creditors in the event of default.

Americans for Financial Reform Education Fund commends the OCC, Federal Reserve, and FDIC for promulgating robust rules to establish necessary long-term debt requirements that would provide additional asset cushions to promote orderly resolution for entities in the event of default and failure. The proposed long-term debt requirements can be an important complement — but not substitute — to rigorous capital standards currently being considered. More robust capital standards provide the best regimen to strengthen safety and soundness and provide resiliency against systemic risk. Thank you for the opportunity to comment and for the consideration of these recommendations in the development of a final rule on long-term debt.

Sincerely,
Americans for Financial Reform Education Fund