April 11, 2011

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Docket No. R-1401
RIN 7100-AD61

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, DC 20219
Docket No. OCC-2010-0003

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Attention: Comments/Legal ESS
RIN 3064-AD70

Re: Risk-Based Capital Guidelines: Market Risk

Dear Sir or Madam:

The Clearing House Association L.L.C. ("**TCH**"), the American Bankers Association ("**ABA**"), the Institute of International Finance ("**IIF**"), the International Swaps and Derivatives Association, Inc. ("**ISDA**") and the Securities Industry and Financial Markets Association ("**SIFMA**" and, together with TCH, the ABA, IIF and ISDA, the "**Associations**")[1] appreciate the opportunity to comment on the joint notice of

[1] See Annex 1 for a description of the Associations.

proposed rulemaking (the "**NPR**")[2] issued by the Board of Governors of the Federal Reserve System (the "**Federal Reserve**"), the Office of the Comptroller of the Currency ("**OCC**") and the Federal Deposit Insurance Corporation (together, the "**Agencies**") to revise their market risk capital rules (the "**MRC Rules**" and, as proposed to be revised by the NPR, the "**Proposed MRC Rules**"), generally aligning them with Basel II.5.[3] The need for revisions to and enhancements of the MRC Rules was apparent before the onset of the financial crisis, which all too clearly exposed deficiencies in the MRC Rules – most importantly, the need for higher standards of risk control to address stressed and illiquid markets, particularly for non-correlation trading desk securitization positions.

Those of our members that are subject to the MRC Rules generally have revised their internal models to address those deficiencies, apart from the formal requirements of the MRC Rules, and have enhanced their due diligence practices surrounding trading decisions, particularly with respect to securities arising out of securitizations. We endorse amending the MRC Rules to enhance their measurement of market risk and bring the MRC Rules into alignment with Basel II.5. However, we have a number of concerns with the approach taken in the NPR, some of which go to deficiencies that, although not practical to address in the short term, we expect will be addressed in the fundamental review being undertaken by the BCBS's Trading Book Group (the "**Trading Book Group**"), and some of which go to substance or the need for clarification as Basel II.5 is implemented in the United States. Part I of this letter summarizes our comments; Part II addresses several over-arching concerns not addressed by the specific questions posed by the Agencies in the NPR; and Part III sets forth our responses to certain of the specific questions posed in the NPR.

I. Executive Summary

As discussed in Part II.A, the Associations believe that the redundancy in Basel II.5's market risk calculations is one of the principal areas requiring a fundamental review by the Trading Book Group. Our concern with this redundancy is not only that it

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[2] 76 Fed. Reg. 1890 (Jan. 11, 2011).

[3] "**Basel II**," as used in this letter, refers to the capital framework set forth in the Basel Committee on Banking Supervision's ("**BCBS**") June 2006 publication, *International Convergence of Capital Measurement and Capital Standards – A Revised Framework*. "**Basel II.5**," as used in this letter, refers to that publication as revised and updated to include the revisions to the market risk provisions in Part VI of that publication set forth in the BCBS's June 2009 publication, *Revisions to the Basel II Market Risk Framework* and *Guidelines for Computing Capital for Incremental Risk in the Trading Book*, in its July 2009 publication, *Enhancements to the Basel II Framework* (the "**July 2009 Enhancements**"), and in its February 2011 publication, *Revisions to the Basel II Market Risk Framework – Updated as of 31 December 2010* (the "**February 2011 Revisions**").

requires too much capital for some positions but, even more important, that it distorts the link between the degree of economic risk inherent in a position and the related capital requirement, affecting decision-making. In the short term and in the absence of agreement on a better approach, some redundancy may be unavoidable. However, on a longer-term basis, we believe that banks,[4] the Agencies, the BCBS and the Trading Book Group must work together to develop a coherent, integrated framework that captures all important general market, idiosyncratic, basis and default risks and eliminates redundant capital charges.

As discussed in Part II.B, in the Associations' view it is very important that the Agencies be direct and transparent in identifying the areas where the Proposed MRC Rules differ from Basel II.5 and explain the reasons for the differences. We are concerned that, in many areas, the Proposed MRC Rules go beyond Basel II.5, adding a number of provisions that increase the conservatism of the U.S. approach and, in doing so, creating competitive equality concerns for U.S. banks. We do not believe that the comparable provisions in Basel II.5 are unduly lax and we thus urge the Agencies to follow the global approach except where unique U.S. circumstances (for example, variations in accounting treatment) warrant national discretion.

The Associations' responses to certain of the questions posed in the NPR are provided in Part III of this letter. They include the following:

- Given the level of double- and triple-counting in the Proposed MRC Rules, the 15% surcharge in paragraph (a)(2)(i)(B) of Section 9,[5] included in the comprehensive risk measure for correlation trading positions, is unnecessary, even on a temporary basis (Question 1).

- The Associations urge the Agencies to clarify that the requirement for a "two-way market" applies only to correlation trading positions and other trading positions that are subject to restrictive covenants and to conform the definition of "two-way market" to international standards (Question 1).

- The Associations believe that a "pay as you go credit default swap" ("**PYG CDS**") should receive the same full hedge recognition

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[4] We are using the term "**bank**" in this letter to include any banking organization subject to the MRC Rules as in effect from time-to-time, including bank holding companies and depository institutions.

[5] Unless otherwise noted, "**Section**" references in this letter are to sections of the Proposed MRC Rules.

as a total return swap for purposes of the standardized measurement method for specific risk under paragraphs (a)(4) and (5) of Section 10. Further, the Associations believe that, in the circumstances discussed in Part III.A.3, transactions should receive the 80% hedge recognition treatment provided for in paragraph (a)(5) of Section 10 notwithstanding the absence of an "exact match" between the reference obligation of the hedge and the debt or securitization position (Question 1).

- The liquidity horizon in Section 8(b)(1)(i) for determining the incremental risk measure is excessively long for certain highly liquid exposures – for example, G10 rates and currencies (Question 1).

- The definition of "securitization" should be aligned with Basel II.5 and, in particular, should not encompass, as a default rule, exposures to investment firms that do not resemble what is customarily thought of as a securitization (Question 1).

- When calculating the specific risk add-on for securitization-type products under the standardized measurement method of Section 10, banks should be permitted to de-construct the components of indexed and securitization-type products in order to give effect to the netting of long and short positions and hedges (Question 1).

- Banks should not be required to maintain capital against covered positions in an amount that exceeds the maximum loss that the bank could suffer with respect to the position (Question 1).

- The Associations urge the Agencies to consider, as an alternative to the ten-business day requirement of Section 5(b) in the VaR calculation, continuing to permit banks to use a calculation based on one-day VaR multiplied by the square root of time, using a scaling factor as necessary (Question 1).

- The requirement in Section 3(a)(2) to consider future administrative costs in a bank's valuation process is impractical, is inconsistent with U.S. GAAP and should be removed (Question 1).

- The Associations generally support the NPR's closer alignment of the definition of covered position with paragraphs 685 and 687 of Basel II.5. However, we believe there are a number of respects in which clarification or modification is needed, including the time

horizon over which determinations of intent and of the existence of a two-way market are applied, the exclusion of hedges outside the bank's hedging strategy, the treatment of hedges of securitization exposures and the extent to which internal hedges will be eligible for trading book capital treatment (Question 3).

- The Associations urge the Agencies not to address model deficiencies with a formal model-specific capital supplement requirement but instead to address model deficiencies discretionarily on a bank-specific basis (Question 4).

- Banks should be permitted, during the two years after the Proposed MRC Rules become effective, to calculate trading losses for back-testing purposes under Section 4(b) by including or excluding fees, commissions, reserves, net interest income and intra-day trading, as long as this is done consistently (Question 5).

- We urge the Agencies to afford banks substantial discretion and flexibility in identifying "significant sub-portfolios" for purposes of Section 5(c) (Question 6).

- The Associations appreciate the Agencies' continuing efforts to establish standards of creditworthiness for capital and other purposes that are consistent with Dodd-Frank Section 939A. However, we are concerned that it may not be possible to develop a satisfactory alternative meeting the criteria set forth in the NPR in the near term and, accordingly, urge the Agencies to work with Congress to modify Section 939A to the extent necessary to permit credit ratings to be used in bank capital regulations (including the MRC Rules) to the extent doing so is required for consistency with international standards, pending development of an appropriate alternative measure of credit risk (Question 7).

- The proposed due diligence requirements – particularly that the documentation of due diligence be completed before acquiring a security – are impractical. We urge the Agencies to conform the Proposed MRC's due diligence requirements with international standards, including by permitting documentation requirements to be satisfied after a security is acquired (Question 8).

- The Associations believe that banks should have the flexibility to (i) define or identify what a "portfolio" is for disclosure purposes,

taking into account the bank's judgment as to the meaningfulness and materiality of the disclosure, and (ii) determine and disclose risk measures that are the most meaningful to their portfolios. Further, the Associations view stress testing scenarios as proprietary and do not support their detailed disclosure (Question 12).

II. Over-Arching Concerns

A. The Associations place great importance on the Trading Book Group's fundamental review, including the need to address the redundancy in the components of the market risk capital measures.

The Trading Book Group has acknowledged that aspects of Basel II.5 require substantial attention and change and, accordingly, is revisiting Basel II.5. Among the areas most requiring a fundamental review is Basel II.5's redundancy in measuring risks, and the related distortion in capital charges for different portfolios and activities. The redundancy in Basel II.5's market risk calculations – double- and triple-counting risks in numerous respects, resulting in a layering of capital charges – has been commented on at length in submissions to the BCBS[6] and has been a major focus of the Trading Book Group's discussions. For example:

- The stressed VaR-based measure is definitionally – and apparently by design – duplicative of the VaR-based measure, with the calculations being the same and capturing the same risks but with stressed VaR using model inputs from a period of significant financial stress.

- The incremental risk measure, applicable to debt positions (and, if the applicable Agency approves, equity positions) for which specific risk is calculated using a model approach under Section 7(b), is additional to that specific risk calculation. The relationship between incremental risk and specific risk is analogous to the relationship between stressed VaR and VaR, except that the additional factor for incremental risk purposes is the imposition of the constant level of risk assumption instead of model inputs from a stressed period.

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[6] See, for example, the joint letter, dated March 13, 2009, of ISDA, IIF, the London Investment Banking Association and the International Banking Federation addressed to the co-chairs of the Trade Input Group concerning BCBS Nos. 148 and 149.

- The comprehensive risk measure for correlation trading positions – specified to measure "all price risk" – is duplicative of the VaR-based measure and stress VaR-measure and the modeled specific risk calculations (the latter as part of the VaR and stressed VaR calculations). Those measures also encompass price risk of correlation trading positions, covering "losses on a position that could result from movements in market prices." The use of this measure is, however, seriously undermined by the regulatory floor in Section 9(a)(2)(i), as well as the 15% surcharge in sub-clause (B) of Section 9(a)(2)(i), which may dominate in some portfolios for the period of at least one year during which it will apply. Moreover, the surcharge is not a component of or required by Basel II.5 and, in our view, is both unnecessary and risk-insensitive.

- Conceptually, the VaR, stressed VaR and comprehensive risk measures capture spread risk, downgrade risk and default risk across markets, where the specific risk measure captures spread risk, downgrade risk and default risk idiosyncratically (that is, for particular issuers or portfolios). There is, of course, a correlation between market-wide and idiosyncratic changes in these risks and between systemic spread widening and an increase in systemic default rates. The incremental risk measure captures default risk and credit migration risk related to both market and idiosyncratic factors. Separately capitalizing jump-to-default risk under the incremental risk measure and stressed spread changes under stressed VaR therefore results in double counting.

Were the Agencies to recognize a model-specific capital supplement, doing so may add yet another layer of redundancy. We strongly urge the Agencies not to take that approach. See our more detailed comments in Part III.C, below, responding to Question 4.

As a short-term measure and in the absence of agreement on a better approach, some redundancy may be unavoidable. Over the longer term, however, we believe that banks and the Agencies, along with the BCBS and the Trading Book Group, must work together to refine the components of market risk capital and eliminate the layering of duplicative capital charges. The Basel II.5 standards (including their proposed incorporation into the Proposed MRC Rules) take a "patchwork" approach that lacks coherence. Our concern with this redundancy is not only that it requires too much capital for some positions, but, even more important, that it distorts the link between the degree of economic risk inherent in a position and the related capital requirement, affecting decision-making. While substantial work needs to be done to

develop an alternative and better approach, we believe that banks and their regulators should agree on the objective: a coherent, unified framework that captures all important general market, idiosyncratic, basis and default risks and is coherent across the trading and banking book continuum. We expect such a model would require a large set of historical and prudential inputs that would create a single P&L distribution across multiple liquidity horizons (and hence avoid the need for multipliers) that could be examined at different times and across different confidence levels.

Although we believe the initial deliberations of the Trading Book Group show promise, we also recognize that creating a more coherent approach and eliminating the redundancies of the Basel II.5 patchwork approach will take time. Accordingly, subject to our specific comments in Part III below, we endorse the Agencies' proposal to move ahead with the Proposed MRC Rules, incorporating Basel II.5 into the Agencies' approach for U.S. banks. It is important to note, however, that creating the infrastructure changes to accommodate Basel II.5 requires substantial expense and effort by those banks that are subject to the MRC Rules. Those banks have, of course, been working on the infrastructure required by Basel II.5 for some time, in anticipation of amendments to the MRC Rules; however, remaining uncertainties and the scope of these changes make this a formidable undertaking. Although we are confident that the Trading Book Group's fundamental review ultimately will result in a more coherent approach to measuring market risk and believe it essential that the Trading Book Group proceed with its fundamental review (notwithstanding new infrastructure expenses that changes arising out of the review may entail), as of today the timing and content resulting from its review are not known. We encourage the Trading Book Group to complete its fundamental review as quickly as possible. When the Trading Book Group's review is completed and its recommendations adopted as revisions to Basel II.5, we urge the Agencies to work with their counterparts from other countries at the BCBS to arrive at an implementation schedule for revisions (which we expect will be extensive) that gives banks the flexibility to spread the costs of additional major infrastructure changes over a reasonable period.

B. The Proposed MRC Rules differ from Basel II.5 in a number of respects. We believe it very important that the Agencies identify where they have chosen to diverge from Basel II.5 and explain their reasoning.

Although the NPR does not identify differences between the Proposed MRC Rules and Basel II.5, it became apparent during the Associations' review that there are a number of differences. We have commented on some of these elsewhere in this letter. They include:

- the regulatory floor, as well as the 15% surcharge in Section 9(a)(2)(i)(B), provided for in Section 9(a)(2)(i) of the Proposed

MRC Rules, which we believe is unnecessary, inconsistent with Basel II.5 and risk-insensitive (Part II.A);

- a more restrictive definition of "two-way market" in the Proposed MRC Rules than in Basel II.5 (Part III.A.2);
- a broader definition of the term "securitization" that, among other things, brings within its scope exposures to investment firms (Part III.A.5);
- the failure to limit the specific risk capital requirement for securitization tranches to the maximum possible loss of such exposures (Part III.A.8);
- the exclusion from the definition of covered position of hedges that are outside the scope of a bank's hedging strategy (Part III.B); and
- the strictness as to the timing and other application of due diligence requirements for securitizations (Part III.G).

We recognize that differences among markets and legal regimes in some circumstances require differences in regulatory approach. However, the items identified above do not seem to result from differences in U.S. markets or circumstances as compared to markets or circumstances abroad but, instead, reflect regulatory decisions made by the Agencies. For the reasons set forth elsewhere in this letter, we urge the Agencies to conform these aspects of the Proposed MRC Rules to Basel II.5.

More generally, we urge the Agencies to be direct and transparent in identifying the areas where they chose Proposed MRC Rules that differ from Basel II.5, in each case explaining the reason for the difference. The Associations believe that it is essential that Basel II.5 be consistently implemented across jurisdictions. We are concerned that, by adding to the Proposed MRC Rules a number of provisions that cause the U.S. rules to require more capital, particularly for credit correlation trading portfolios, than Basel II.5-based rules in other jurisdictions, the outcome will exacerbate international disparities, with potential competitive consequences for U.S. banks.

III. Responses to Certain Specific Questions

A. Question 1. The Agencies request comment on all aspects of the proposed rule and specifically on whether and for what reasons certain aspects of the proposed rule present particular implementation challenges. Responses should be detailed as to the nature and impact of such challenges. What, if any, specific approaches (for example,

transitional arrangements) should the Agencies consider to address such challenges and why?

Our comments in response to Question 1 address concerns that are not encompassed in responses to the other specific questions set forth below.

1. Although the Associations generally support the NPR's comprehensive risk measurement approach to correlation trading positions, we believe it has significant deficiencies and should be viewed as a temporary measure.

The Associations appreciate that the approach to measuring the comprehensive risk of correlation trading positions in Section 9 is substantially similar to the approach in Basel II.5. However, we have several important concerns with the approach.

First, the Associations recognize that modeling of tranched credit products prior to the crisis fell short in some respects, but also believe that events have borne out that modeling of products with corporate credit underlying fared relatively better than those with asset-backed securities ("**ABS**") underlying. Accordingly, the Associations believe that the rigorous standards required for comprehensive risk measurement approval, including multiple weekly stress tests, as well as supervisory efforts to benchmark and cross-validate comprehensive risk measurement implementation across firms, should be sufficient to ensure an appropriate capture of the relevant risks, making the add-on to the comprehensive risk measure unnecessary. Should the proposed approach be retained indefinitely, it will limit the ability of banks to participate effectively in the development of markets for trading corporate credit correlation. While some observers may wish to eliminate such markets entirely, the Associations do not believe this is a sensible objective. Banks by the nature of their participation in lending markets inevitably take on positions that expose them to the correlation of credit risks. Limits on the ability of banks to hedge such risks and trade more actively in such markets will ultimately have detrimental prudential effects. Moreover, systemic risk likely will increase if such activities were to leave the regulated financial system and move to unregulated "shadow" entities.

Second, as discussed in the third bullet of the first paragraph in Part II, the most important components of price risk covered by the approach are also captured in the VaR and stressed VaR measures and in the modeled specific risk calculations. Although redundancy is an area that needs to be addressed more broadly by the Trading Book Group in its fundamental review, we believe that this is especially the case with respect to the comprehensive risk measure.

Third, similar concerns apply to the proposed application of an additional 15% comprehensive risk surcharge in paragraph (a)(2)(i)(B) of Section 9. As noted

above, price risk is already triple-counted. The Associations cannot support the application of a largely arbitrary calculation that is not materially responsive to the underlying risk and, furthermore, is unnecessary given the level of double- and triple-counting in the Proposed MRC rules as discussed in Part II.A.

2. We urge the Agencies to clarify that the requirement for a "two-way market" applies only to correlation trading positions and other trading positions that are subject to restrictive covenants. We also urge the Agencies to conform the definition of this term to international standards.

The Proposed MRC Rules:

- define the term "two-way market" in a manner that is different from Basel II.5 and international standards,[7] most importantly by requiring that the position "can be . . . settled at that price within five business days";

- consistent with Basel II.5 and international standards, define the term "correlation trading position" to mean one for which, among other things, a two-way market exists for the exposures on which all or substantially all of the value of the underlying exposures is based;

- unlike Basel II.5, specify (in paragraph (1)(ii) of the definition of covered position) that a covered position must be free of restrictive covenants on its tradability or the bank "is able to hedge the material risk elements of the position in a two-way market"; and

- in paragraph (a)(1)(i) of Section 3, specify that a bank must have clearly defined policies and procedures for determining which trading assets and liabilities are trading positions or correlation trading positions and that those policies and procedures "must take into account . . . (i) [t]he extent to which a position, or a hedge of its material risks, can be marked-to-market daily by reference to a two-way market."

Basel II.5 does not require that there be a two-way market for every covered position. The Associations are concerned that the provisions of the Proposed MRC Rules referenced above, read together, could be construed to require that there be

[7] See paragraph 689(iv) of Basel II.5, as added by the February 2011 Revisions.

a two-way market for every covered position. We urge the Agencies to confirm that that is not the intended reading of the provisions and that they should be read literally – that is, a two-way market must exist for the exposures on which all or substantially all of the value of the exposures underlying a correlation trading position is based; other covered positions that are not freely tradable must be able to be hedged in a two-way market; and the requirements of Section 3(a) with respect to the bank's policies and procedures are intended only to support those determinations. If the two-way market test were to be applied more broadly as a requirement for all covered positions, it would result in a significant number of positions (indeed whole businesses) no longer being eligible for the trading book. In many cases, positions that were acquired through market-making activities and held on active trading desks would fail such a test, even though they are best risk-managed and analyzed for capital purposes within the trading book. Additionally, applying the two-way market test in the most stringent manner could result in short derivative positions failing the test; if failing the test means that they are not evaluated for capital purposes under the MRC Rules as revised, inasmuch as they also are not covered by the banking book credit-risk rules, they simply would not be captured for risk-based capital purposes.

We also urge the Agencies to clarify that the phrase "restrictive covenants on its tradability" in paragraph (1)(ii) of the definition of the term "covered position" does not encompass securities transferable only to qualified institutional buyers in reliance upon Rule 144A under the Securities Act of 1933 merely because of the Rule 144A requirements. The Rule 144A market is a deep institutional market, and the liquidity of securities that trade in that market have been recognized for other regulatory purposes, including by the OCC for purposes of determining when an investment security is "marketable" under the OCC's investment securities regulations, 12 C.F.R. Part 1.

Finally, we do not understand the need to restrict the term "two-way market" to those where positions can be settled within five business days, since this would automatically exclude a number of markets where settlement periods are longer than five business days (for example, liquid mortgage pass-through securities). Moreover, as noted above, Basel II.5 does not include this restriction. Under the current rules, trades that settle over a longer timeframe attract market risk capital requirements from trade-date onwards, as well as additional credit risk requirements to capture the extended settlement risk. This approach provides appropriate capital requirements for each type of risk. Under the Agencies' proposal, all such positions subject to the two-way market requirement would be dealt with only under the credit risk rules, and this could in fact understate the market risks inherent in the positions. Given therefore that extended settlement risk is explicitly addressed elsewhere within the credit risk capital rules, we believe that this requirement should be removed from the two-way market definition.

We believe that international consistency is particularly important in an area such as the definition of trading position or book in order to remove the possibility of arbitrage between different countries' rules. Additionally, absent international consistency, U.S. banks operating overseas could face situations where the same position is treated inconsistently for capital purposes in its consolidated capital requirements and in its overseas entities' capital requirements. Such an inconsistent treatment would not only raise level playing field issues but would also create significant operational challenges for these banks – which in turn would cause these banks to incur additional costs – as systems, policies and procedures would need to be adjusted to account for the disparate treatment of exposures across jurisdictions.

3. A PYG CDS should receive the same full hedge recognition as a total return swap for purposes of the standardized measurement method for specific risk under paragraphs (a)(4) and (5) of Section 10. In addition, some transactions should receive the 80% hedge recognition treatment provided for in paragraph (a)(5) of Section 10 notwithstanding the absence of an "exact match" between the reference obligation of the hedge and the debt or securitization position.

PYG CDSs are credit derivatives where the credit protection seller, in consideration of a fee paid by the credit protection buyer for the credit protection, makes a payment to the credit protection buyer only if and when the underlying issuer/obligor defaults in making a payment on the underlying security. A PYG CDS differs from a total return swap ("**TRS**"). Under a TRS, the credit protection seller customarily makes all payments as and when due and the credit protection buyer, in addition to paying a fee for the credit protection, customarily pays to the credit protection seller payments received on the underlying security as and when received. PYG CDSs are the most common form of credit derivative hedges for asset-based securities.

Paragraphs (a)(4) and (5) of Section 10 appear to draw a distinction between TRS – for which paragraph (a)(4) provides full hedge recognition if there is an exact match (which customarily would mean an exact CUSIP match) between the reference obligation and the TRS – and other types of derivatives, including PYG CDSs, for which paragraph (a)(5) provides only 80% hedge recognition even if there is an exact match. We do not believe that there is a substantive difference in protection warranting different treatment of a PYG CDS that is an exact match and a TRS that is an exact match. Accordingly, we urge the Agencies to clarify in paragraph (a)(4) that a PYG CDS that is an exact match is accorded full hedge recognition.

Further, the hedge recognition treatment in paragraph (a)(5) of Section 10 only extends to a CDS to the extent there is an exact match between the reference

obligation of the CDS and the debt or securitization position. We understand the reference to "exact match" to mean a match not only as to the obligor but also as to the specific security or obligation. The Associations believe that paragraph (a)(5)'s treatment should extend to a CDS that fully hedges the credit risk of the applicable debt or securitization position where there is an exact match as to the obligor or issuer but not necessarily an exact match as to the specific security or obligation. CDSs typically do not name specific obligations but rather reference particular entities. To the extent a CDS fully hedges all of the credit risk of a position, it should not matter whether the credit risk of the position has been hedged by a CDS referencing an entity or one referencing the specific debt or securitization position. Requiring an exact match as to the specific security or obligation in order to qualify for the treatment in paragraph (a)(5) would fail to recognize the real scope of risk reduction.

Finally, credit derivatives, especially CDSs, are traded on market conventions based on standard maturity dates, whereas debt or securitization instruments may not be. We believe that for a CDS hedging a debt or securitization position where the hedge maturity extends beyond the maturity of the debt or securitization position (or is the nearest standard maturity date to the maturity date of the debt or securitization position) should still be eligible for the 80% hedge recognition. Providing such recognition would afford trading desks additional flexibility in implementing hedging strategies, thereby allowing them to hedge more efficiently and encouraging them to prudently manage trading book risk.

4. The liquidity horizon for determining the incremental risk measure is excessively long for certain highly liquid exposures – for example, G10 rates and currencies.

The Associations believe that the incremental risk measure's floor on liquidity horizons in Section 8(b)(1)(i) of the lower of three months and the contractual maturity of the position is excessively long for certain highly liquid exposures – for example, high-grade G10 rates and currencies (for example, local currency sovereign debt or spot exchange rates). The NPR defines a liquidity horizon as the time required for a bank to reduce its exposure to, or hedge all of its material risks of, the position in a stressed market. As demonstrated in the recent financial crisis, liquid markets for such highly liquid exposures exist even in times of significant financial stress, making a three-month floor excessively conservative.

5. The definition of "securitization" in the Proposed MRC Rules should be aligned with Basel II.5 and, in particular, should not encompass, as a default rule, exposures to investment firms that do not resemble what is customarily thought of as a securitization.

The definition of the term "securitization" in the Proposed MRC Rules (i) does not follow Basel II.5, (ii) if adopted would be unique to the United States, and (iii) we believe is inappropriately broad so as to encompass exposures to investment firms that do not resemble what is customarily thought of as a securitization. The definition of securitization set forth in paragraph 539 of Basel II.5 provides:

> . . . a structure where the cash flow from an underlying pool of exposures is used to service at least two different stratified risk positions or tranches reflecting different degrees of credit risk. Payments to the investors depend upon the performance of the specified underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures. The stratified/tranched structures that characterise securitisations differ from ordinary senior/subordinated debt instruments in that junior securitisation tranches can absorb losses without interrupting contractual payments to more senior tranches, whereas subordination in a senior/subordinated debt structure is a matter of priority of rights to the proceeds of liquidation.

The definition of "securitization" in the NPR moves away from the Basel II and II.5 definition of that term, which recognizes the fundamental difference between securitizations and ordinary senior and subordinated debt instruments – namely, junior tranches of securitizations can absorb losses without interrupting contractual payments to more senior tranches, whereas the "subordination" of a debt instrument is a matter of priority of right to the proceeds of liquidation. In addition, the NPR's definition of "securitization" is sufficiently broad that, absent an exclusion, it would encompass exposures to investment firms that issue debt as well as equity or more than one class of equity.

The key distinction in paragraph 539 of Basel II.5 – that junior tranches of a securitization can absorb losses without interrupting contractual payments – is wholly absent from typical exposures to investment firms and, thus, it would be inappropriate to treat such exposures as securitizations as a default rule. Moreover, we note that requiring all exposures to investment firms to be treated as securitizations, subject to

applications for exclusion, would result in banks filing thousands of applications for exceptions, and result in punitive capital charges when exceptions are not granted.[8]

Many regulated financial institutions include exposures to investment firms in their trading book, using the net asset value of the investment firm to determine the fair value of the exposure. Banks manage these positions similarly to other trading book positions – that is, they actively manage these exposures, with the intent to trade for short-term profit or to hedge these exposures. The investment firm's net asset value represents the mark-to-market values of the underlying traded fund positions and is considered in the calculation of general market risk capital. The modeling of market risk capital also takes into consideration the overall leverage within the investment firm. Specific risk capital is based on the extent to which the investment firm holds covered debt or equity positions that are subject to specific risk capital. Hedges to such positions are derived based on publicly traded debt or equity positions that reflect the market values of underlying securities or positions owned by the investment firm. The purpose of holding these positions on the trading book is not to invest in the capital structure of the investment firm.

For all of the foregoing reasons, we believe that exposures to investment firms should not be treated, as a default, as securitizations. Rather, the default rule should be that exposures to investment firms are not deemed to be "securitizations" unless a bank's supervisor or examiner determines that the exposure is in fact a securitization in accordance with paragraph (9) of the definition of "securitization." To accomplish this change we suggest deleting paragraph (8) from the definition of "securitization" in its entirety and appending "or investment firm" to the end of paragraph (5) of that definition. Moreover, because the definition of "securitization" in the NPR mirrors the definition of that term in the U.S. version of Basel II,[9] we urge the Agencies to make equivalent edits to that definition as well for the reasons discussed above.[10]

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[8] Paragraph (8) of the definition specifies that the applicable Agency may grant an exemption from securitization status for an exposure to an investment firm that exercises "substantially unfettered control" over, among other things, the size and composition of its assets, liabilities and off-balance sheet exposures.

[9] See, for example, the definition of "securitization" in Section 2 of Part 225 of 12 C.F.R., Appendix G.

[10] For more information, please see the ABA's letter, dated February 15, 2011, to the Federal Reserve regarding *Treatment of Exposures to Investment Funds as Securitization Exposures under the Basel II Advanced Capital Adequacy Framework*.

6. When calculating the specific risk add-on for securitization-type products under the standardized measurement method of Section 10, banks should be permitted to (i) de-construct the components of tranched securitization-type products and positions in an index, and (ii) "look through" to the underlying exposures of funds, in each case, in order to give effect to the netting of long and short positions and hedges.

The standardized measurement method for specific risk in Section 10 is straight-forward and well-defined as applied to non-tranched debt exposures: (i) the bank nets long and short positions; (ii) to the extent possible, after giving effect to its netting of long and short positions, the bank may recognize hedges, subject to criteria specified in Section 10; and (iii) the bank then applies the appropriate risk-weighting factor to the result of the foregoing calculation.

Section 10 and commentary in the NPR text concerning the standardized measurement method for specific risk do not address whether or how netting long and short positions or application of hedges applies to tranched securitization products or position in an index. The Associations strongly believe that banks should be able to de-construct tranches of securitizations or the names underlying an index and, in either case, associated hedges to net long and short positions and recognize hedges associated with a component of the tranched securitization product (for example, a bank is short an index but long all of the underlying names in the index, or a bank is short the 0%-10% tranche, and long the 0%-5% and 5%-10% tranches of the same structure). Permitting de-construction provides the right incentive for banks to fully hedge their risks; not permitting de-construction encourages banks not to hedge the underlying risks because the hedges attract additional capital requirements. Moreover, apart from correlation trading where basis risk is accounted for in the comprehensive risk measure, where there is a degree of basis risk between a position and its hedge(s), index and tranche de-construction should be permitted to recognize some netting benefit, but not the benefit accorded identical netting.

If the Agencies are not prepared to allow de-construction of all positions, we urge them to at least allow for:

- index de-construction since basis risk for a long index position hedged against single names should be zero or minimal (and any mismatch in the names or amounts between the single name hedges and index position would attract specific risk capital requirements); and

- tranche de-construction in a scenario where a bank has "completed the capital structure" – that is, the bank (i) holds all

> tranches of a structure and (ii) is fully hedged with CDSs on the underlying portfolio. This approach would encourage banks to reduce risks by appropriately hedging positions, without such hedges attracting additional capital requirements. In this scenario, even if the Agencies are not prepared to allow for identical matching, hedge recognition could be restricted to the 80% specific risk offset treatment prescribed in Section 10(a)(5), in order to provide some capital requirement against any residual basis risk.

Some of the Associations' members have been informally advised by the Agencies in the past that hedges of indexed and tranched products, when de-constructed, will only be recognized if all of the constituents of the index or tranche are rated investment grade. That creates a perverse incentive to not hedge the higher-risk non-investment grade exposures because capital requirements on the hedges become additive. It is also risk insensitive in circumstances where, notwithstanding the capital disincentives to hedging, the credit risk of the position is fully hedged. We understand that the investment grade requirement is not an international standard that has been applied elsewhere and, accordingly, it raises competitive equality issues. The focus of this requirement is also misplaced. The method used to de-construct the applicable exposure and how the banks hedges its components should be the focus, rather than the credit ratings of the underlying components, which by themselves are not indicative of the soundness of the de-construction process or the effectiveness of the hedges. Moreover, in light of Dodd-Frank Section 939A, the application of this approach going forward is uncertain. For these reasons, we urge the Agencies to permit the de-construction of tranched and indexed products and recognition of hedges as described above, but without imposing the investment grade requirement that has informally been imposed in the past.

For similar reasons, including that doing so would encourage banks to fully hedge their risks and promote competitive equality and consistent international standards, we urge the regulators to adopt an approach similar to the "CIU Look Through Method" contained in Chapter 7.7 of the Financial Services Authority's Prudential sourcebook for Banks, Building Societies and Investment Firms ("**BIPRU**") and to allow banks to look through to the underlying exposures in funds such as mutual and money market funds (for example, sovereign bond funds) when calculating market risk charges. BIPRU permits banks to look through to the underlying holdings of a fund and on a proportional basis to compute market risk capital charges under the standardized method, thereby allowing banks to give effect to the netting of short and long positions and hedges of the underlying exposures of a fund.

7. We urge the Agencies to provide additional clarity on the types of events that are meant to be captured by the definition of "event risk."

The Proposed MRC Rules provide that specific risk includes "event risk, default risk, and idiosyncratic," and define the term "event risk" to mean "the risk of loss on a position that could result from sudden and expected large charges in market prices or specific events other than default and credit migration of the issuer." Default risk and credit migration risk are captured by the new incremental risk charge in Section 8 and related definitions.

We urge the Agencies to consider providing guidance or examples as to the types of events they anticipate may be captured by the definition of "event risk." They could do this either in an expanded definition of the term "event risk" in the final version of the revised MRC Rules or in the accompanying text. Without more clarity, banks are left with substantial uncertainty as to what is encompassed and how event risk as a component of the specific risk measure may relate to other components of the market-risk capital requirements and potentially duplicative capital charges. We are also concerned that, without a common understanding as to the types of events that models addressing event risks should capture, comparability of VaR data among institutions will be reduced.

8. Banks should not be required to maintain capital against covered positions in an amount that exceeds the maximum loss that the bank could suffer with respect to the position.

In Part II.A, we commented on our concern with respect to the redundancy in Basel II.5 and the Proposed MRC Rules, double- and triple-counting risks in numerous respects. Pending the Trading Book Group addressing that issue as part of its fundamental review, we urge the Agencies to include in the final revised MRC Rules a provision stating that, if a bank can demonstrate to the satisfaction of the applicable Agency that the amount of capital required by the final revised MRC Rules to be maintained by the bank with respect to a covered position or positions exceeds the maximum loss the bank could occur with respect to the covered position or positions, then the amount of required capital will be limited to this maximum loss exposure.

Conceptually, this principle is similar to the low level exposure rule in the Agencies' Basel I guidelines. In addition, this principle was incorporated into Basel II.5 in the BCBS publication *Annex – Changes to the Revisions to the Basel II Market Risk Conceptually* (the "**2010 Annex**"), which provides, "[b]anks may limit the capital charge for an individual position in a credit derivative or securitisation instrument to the

maximum possible loss."[11] And Section 10(a)(1) of the Proposed MRC Rules includes a similar cap, but limited to the specific risk add-on for an individual debt or securitization position that represents purchased credit protection, with the specific risk add-on being "capped at the market value of the protection,"[12] but with no corresponding cap on a sold credit protection position.

We recognize, of course, that the burden will be on the bank requesting relief to demonstrate that the MRC Rules require more capital than the maximum loss exposure, but we do expect that banks will be able to make that showing when it is in fact the case.[13]

9. The Associations urge the Agencies to consider, as an alternative to the ten-business day requirement of Section 5(b) in the VaR calculation, continuing to permit banks to use a calculation based on one-day VaR multiplied by the square root of time using a scaling factor as necessary.

Section 5(b) provides that the VaR-based measure must be based on a holding period equivalent to a ten-business day movement in underlying risk factors. Implementing a sound ten-day VaR calculation assuming constant positions presents several significant challenges, including the simulation of ten-day shocks, the full repricing of positions ten days out, historical time series data availability for newer markets and risk factors, how to treat positions which are due to expire during the ten-day period, and significant challenges in back-testing a ten-day P&L (because positions are not actually held constant over the ten days, which is inconsistent with the required assumption for the ten-day VaR calculations) as well as requiring ten years worth of data to back-test a ten-day 99% VaR measure. We acknowledge that, under stressed marked conditions, using the square root of time may be less appropriate because portfolio returns tend to correlate. However, in light of the significant challenges to implementing

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[11] See paragraph 3 of the 2010 Annex adding a new paragraph titled "Limitation of the specific risk capital charge to the maximum possible loss."

[12] There is some inconsistency between the manner of the calculation under Section 10(a)(1), which looks at the "snap shot value" of the protection, and the Basel II.5 approach, which measures the maximum loss by reference to the change in value. Additionally, the Proposed MRC Rules effectively apply the specific risk cap to a short risk position and are silent on the treatment of a long risk position.

[13] We note that this principle will also be an issue under Basel III, under which securitization positions that are not rated or have a rating below BB- are assigned a risk weight of 1250%. When minimum Tier 1 Capital ratios are over 8% (as they will be), a bank will effectively be required to hold more capital for such positions than its maximum potential loss.

a ten-day VaR highlighted above, we urge the Agencies to consider, as an alternative, allowing banks to continue to use the square root of time calculation to convert one-day VaR measures to the equivalent of a 10-business-day holding period, using a scaling factor as necessary to mitigate concerns regarding the appropriateness of using the square root of time under stressed market conditions. Also, the comparability of VaR among different banks will be significantly reduced by requiring a complete ten-day VaR, rather than a uniform, conservative scale-up of a one-day 99% VaR, given the range of assumptions that have to be made and the likelihood of a variety of different approaches among banks.

10. The definitions of "qualifying" and "other" following Table 2 in Section 10 should be clarified to include securitization positions.

Table 2 in Section 10(b) provides the risk-weighting factors for specific risk measures of debt and securitization positions in three categories – government, qualifying and other. However, the definitions of those categories in clauses (i), (ii) and (iii) of Section 10(b) only refer to debt instruments in the three categories. Those definitions should be expanded to include securitizations as well. We anticipate that this is merely a drafting correction.

11. We urge the Agencies to permit banks the option of using, or not using, as the case may be, a derivative's delta as currently required by Section 10(a)(2).

The Proposed MRC Rules require, in Section 10(a)(2)'s provisions dealing with the standardized measurement method for specific risk, that

> [f]or debt, equity or securitization positions that are derivatives with nonlinear payoffs, a [banking organization] must risk weight the market value of the effective notional amount of the underlying instrument or portfolio multiplied by the derivative's delta.

While we agree that applying delta to the effective notional amount of a non-linear derivative is theoretically correct, implementing this in regulatory capital calculations will require a very significant amount of work for banks. If the specific risk rules for correlation and securitization positions are quickly replaced by the securitization framework once the issues regarding Section 939A of Dodd-Frank concerning the use of external ratings are resolved, this work would be useful for a period that potentially is quite short. Further, in certain instances, multiplying by delta will be preferable to not doing so because using delta results in lower risk-weighted assets. As a result, the Associations believe that the Agencies should provide banks with the option of risk weighting using delta, rather than requiring it. The change could be implemented by changing the word "must" in the above-quoted text to "may."

In addition, the Associations request that the Agencies clarify whether regulators would need to approve the models used to generate delta values.

12. The requirement in Section 3(a)(2) that a bank's valuation process consider future administrative costs is problematic and should be removed.

Although conceptually understandable, the requirement to quantify future administrative costs presents several issues. First, the administrative costs of executing transactions in liquid markets (for instance, plain vanilla swaps) are close to zero and thus immaterial, calling into question the need for a requirement to quantify these costs at all. Second, allocating administrative costs to individual transactions in the trading book is difficult because of the large number of services provided or relied on when executing trades (for example, market research, execution and information technology services). These allocations will inevitably be arbitrary and thus not meaningful or indicative of actual administrative costs. Estimating the administrative costs of less liquid portfolios is even more problematic. Sales in these portfolios occur far less frequently than in more liquid portfolios, making estimating administrative costs less precise and, in many instances, arbitrary. Finally, banks will often establish a concentration reserve to cover the increase in transaction costs that results from holding a large and, as a result, less liquid position. Determining and then allocating the marginal future administrative costs over those already accounted for in the concentration reserve is difficult to do in a meaningful way and as a result estimates of these costs are likely to be arbitrary and unhelpful. For all of the foregoing reasons, the Associations urge the Agencies to eliminate the requirement in Section 3(a)(2) to consider future administrative costs in a bank's valuation process.

In addition, given the inconsistency between the valuation provisions in Section 3(a)(2) and valuation standards under U.S. generally accepted accounting principles ("**U.S. GAAP"**) creating parallel valuation frameworks, we urge the Agencies, in developing and implementing the valuation standards for purposes of the MRC Rules, to work closely and collaboratively with accounting standards setters in order to achieve a consistent valuation mechanic.

13. The Associations are concerned that issues related to calculating stressed VaR will hinder the model approval process.

Although the goal of the stressed VaR measure is clear, we believe that as implemented in Section 6(b)(1) – which requires application of the model used to calculate VaR but with a stressed parameter set[14] – the NPR has oversimplified the

[14] Under Section 6 (b)(1), "a bank must calculate a stressed VaR-based measure for its covered positions using the same model(s) used to calculate the VaR-based measure, . . . but with model inputs calibrated to historical data from a continuous 12-month period

process necessary to calculate stressed VaR properly. If done properly, calculating a stressed VaR measure could be prohibitively complicated for many portfolios. A robust calculation of stressed VaR necessarily faces a number of practical challenges and requires additional modeling choices over and above those made when calculating VaR. For example, identifying the "stressed" period requires some degree of reduction of the scope of portfolio risk factors. In addition, it is likely that the proxies or benchmarks used in the stressed VaR calculation will differ from those used in VaR, given limits on the availability of accurate historical data and because the universe of traded instruments and indices evolves over time. Importantly, calibrating a risk model across significantly different market environments requires different distributional assumptions – for example, the modeling of the distribution of interest rates should specify how historical returns observed in a high interest rate environment can be applied to the current environment where interest rates are low.

The recent BCBS publication *Interpretive Issues with Respect to the Revisions to the Market Risk Framework* (Feb. 2011) ("**February Interpretive Issues**") notes that stressed VaR is subject to a use test because the VaR engine used to generate stressed VaR is subject to a use test through the use of the current VaR calculated using the same engine.[15] We are concerned that the additional modeling constraints described above have not been sufficiently recognized and that this will hinder the model approval process. We therefore urge the Agencies to be sensitive to the concerns outlined above when approving models.

B. Question 3: The Agencies request comment on all aspects of the proposed definition of covered position.

The Associations generally support the NPR's movement away from looking to accounting rules (that is, the characterization of an asset or liability as "trading" under U.S. GAAP) for purposes of defining what is a covered position[16] and a closer alignment to paragraph 685 and 687 of Basel II.5. However, we urge the Agencies

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that reflects a period of significant financial stress appropriate to the bank's current portfolio."

15 See the response to question 10 of Section 1 of February Interpretive Issues.

16 The Financial Accounting Standards Board's ASC 320-10-00, formerly known as Financial Accounting Statement No. 115, "Accounting for Certain Investments in Debt and Equity Securities"), and related accounting guidance, defines "**trading securities**" as securities that the bank bought and holds principally for the purpose of selling them in the near term, "**held-to-maturity securities**" as securities that the bank has a positive intent and ability to hold to maturity, and "**available for sale securities**" as securities that are neither trading securities nor held-to-maturity securities.

to clarify or modify the scope of covered positions,[17] taking into account related definitions, that are subject to the Proposed MRC Rules in nine respects, as follows:

First, we are concerned that a narrow reading of the definitions of trading position and covered position would result in banks being required to move positions back and forth between the trading book and banking book (and, accordingly, back and forth between evaluation under the MRC Rules as in effect from time to time and the basic standards in Basel I or Basel II, as applicable) during periods of market stress and volatility. The particular language we are concerned with is: (a) in the definition of "trading position," the phrase "held . . . for the purpose of short-term resale or of the intent of benefitting from actual or expected short-term price movements"; (b) in paragraph 1(ii) of the definition of "covered position," the phrase "is able to hedge the material risk elements of the position in a two-way market" as applied to securities subject to trading restrictions; and (c) in Section 3(b)(1), the phrase "policies and procedures must require . . . (ii) [d]aily assessment of the [banking organization]'s ability to hedge position and portfolio risks, and of the extent of market liquidity."

Requiring banks to immediately remove from MRC Rule treatment securities that were initially acquired within these standards but no longer meet these standards (and may fail to meet them only temporarily) because of a change in the bank's short-term intent during periods of market distress or the absence of a liquid two-way market, and then reverse the treatment when conditions change, will introduce substantial volatility into capital calculations. The Associations strongly believe that that would be the wrong result. We encourage the Agencies to clarify that a bank would be able to continue to treat a position as a covered position notwithstanding market changes that bear on the bank's short-term intent and hedging strategies if the bank, in consultation with the relevant Agency, determines that the bank has the ability over the intermediate term to manage the position as a trading position notwithstanding market disruptions. We urge the Agencies to address this concern by adding the following sentence at the end of the definition of covered

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[17] The NPR defines the term "**covered position**" as a trading asset or trading liability that "is a trading position or hedges another covered position" as to which the bank "is able to hedge the material risk elements of the position in a two-way market," and then defines the term "**trading position**" as a position held by the bank

> for the purpose of short-term resale or with the intent of benefitting from actual expected short-term price movements, or to lock in arbitrage profits.

It goes on to specify that a hedge "must be within the scope of the bank's hedging strategy" as described in Section 3(a)(2) in order for the hedge to fall within the Rules. The NPR's definition of trading position is similar to the standards included in paragraphs 685 and 687 of Basel II.

position: "The **[**banking organization**]** may continue to treat a position that was a covered position when established as a covered position subject to these rules, notwithstanding the **[**banking organization's**]** change in its expectations as to the time horizon over which it will sell or terminate the position or the depth of the market for hedging the material risk elements of the position, if the bank reasonably concludes that the bank has the ability to hold the position in a manner that is consistent with the **[**banking organization's**]** trading strategy through a current period of market disruption or volatility."

Second, we ask the Agencies to clarify that securities held as available for sale under U.S. GAAP[18] may be covered positions under the Proposed MRC Rules. We assume that that is a consequence of moving away from the U.S. GAAP trading characterization as the test and that available for sale securities may be covered positions, depending on the nature of the bank's intent. Under U.S. GAAP, banks may move securities between available for sale status and trading securities status, particularly during periods of market distress. The "positive intent" standard for trading securities status under U.S. GAAP is not the same as the "intent of benefitting from actual expected short-term price movements" in the proposed definition of trading position. We believe banks should be permitted discretion in determining the application of the two intent standards and that there should not be a presumption that a security held as available for sale may not be a trading position under the MRC Rules. We urge the Agencies to confirm that our understanding is correct in their final adoption of revised rules.

Third, we ask that the Agencies confirm our understanding that Level 3 securities that are not subject to restrictive covenants on their tradability and for which by definition there is not observability on all valuation inputs, but that otherwise meet the requirements for a covered position, may be treated as covered positions analyzed for capital purposes under the Proposed MRC Rules. Some Level 3 securities historically, and we believe properly, have been included in trading books and analyzed under the MRC Rules. Assuming that the Proposed MRC Rules as outlined in the NPR do not require that a two-way market exist for every covered position (discussed in Part III.A.2 of this letter), our understanding would be correct.

Fourth, the proposed revisions to the definition of a covered position include a number of tests, some of which are to be applied at the "position" level (for example, certain types of positions are specifically excluded from the trading book) and some of which are to be applied at the "portfolio" level (for example, the trading and hedging strategies must cover "each portfolio of covered positions"). This is confusing

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[18] As U.S. GAAP and International Financial Reporting Standards converge, banks and the Agencies will need to revisit this issue along with the interplay between capital requirements and accounting standards more generally.

and operationally challenging to meet. Many of the tests required are most suited to an assessment of the overall portfolio rather than of each and every position in isolation, since groups of positions are risk-managed on a "portfolio" basis. We encourage the Agencies to clarify that a bank may make the determination of the eligibility of positions for the trading book at the "portfolio" level, but subject to the bank being able to demonstrate a sufficiently robust process, with supporting policies and procedures, to do so.

Fifth, we urge the Agencies to delete the language in paragraph (3)(ii) of the definition of covered position that excludes hedges that are outside the scope of the bank's hedging strategy. Basel II.5 does not include this exclusion. Hedges of trading positions should be included in the trading book whether or not they are within the scope of a bank's hedging strategy. Decoupling the hedge from the position hedged would exaggerate actual risk by failing to recognize the offsetting behavior of the trading position and the hedge, and thus increase required capital unnecessarily. We note the Agencies' concern that banks may craft hedging strategies in order to bring non-trading positions that are more appropriately treated under the credit risk capital rules into the bank's covered positions. However, we believe that the substantially higher amount of capital required by Basel II.5 and the Proposed MRC Rules addresses that concern. It is simply no longer the case that evaluating a position as part of the trading book under the revised MRC Rules requires less capital than banking book treatment. In many cases, the opposite will occur – that is, a particular position will require more capital if treated as part of the trading book than the banking book.

Sixth, we believe that banks should be permitted to calculate the amount of capital needed for hedges to securitization exposures where the hedges themselves are not securitization exposures under the internal models approaches in the Proposed MRC Rules and should not be required, with respect to those hedges, to calculate capital under the standardized approach to specific risk in Section 10. The Proposed MRC Rules define the term "debt position" to exclude "a securitization position or a correlation trading position." Similarly, the definition of "correlation trading position" includes a hedge to what is otherwise a correlation trading position. The definition of "securitization position" does not specifically reference a hedge to what is otherwise a securitization position, but does specifically include "an exposure that directly or indirectly references" what is otherwise a securitization exposure.

We are uncertain as to the Agencies' intent with respect to whether hedges to securitization positions and correlation trading positions should be evaluated for market risk purposes along with those positions or separately. In general, we believe that hedges to cover securitization positions and correlation trading positions should, if the hedge itself is not otherwise a securitization position or correlation trading position, be analyzed for specific risk under the standards applicable to debt positions more broadly, which may include an internal models approach, because we believe those

standards more accurately measure risk. We see no prudential reason for these hedges to attract higher capital requirements than under the Existing MRC Rules.

Seventh, we request that the Agencies clarify whether an exposure and its hedge – if entered into at or around the same time, with no change in the exposure and its hedge anticipated until the maturity of both transactions and assuming the hedge is within the scope of a bank's hedging strategy – will qualify for inclusion in the scope of "covered position." In addition, the Associations seek to confirm that hedge fund exposures that hedge a position in the trading book and are within the scope of a bank's hedging strategy qualify for inclusion in the definition of "covered position."

Eighth, we ask the Agencies to confirm that, similar to the European Union's Capital Requirement Directive (2006-49-EC, Annex VII, Part C) and the U.K.'s Prudential Sourcebook for Banks, Building Societies and Investment Firms (1.2.14), an internal hedge[19] will be allowed if it materially or completely offsets the component risk element of a non-trading book position or a set of positions. Positions arising out of internal hedges are eligible for trading book capital treatment, provided they meet the covered position definition and the following criteria:

- internal hedges must not be primarily intended to avoid or reduce capital requirements;
- internal hedges must be properly documented and subject to particular internal approval and audit procedures;
- the internal transaction must be dealt with at market conditions;
- the bulk of the market risk that is generated by the internal hedge must be dynamically managed in the trading book within the authorized limits; and
- internal transactions must be carefully monitored.

For example, the treatment above is applicable for interest rate risk hedges of banking book positions. In the United States, it would apply to interest rate risk hedges of mortgage servicing rights that, as intangible assets under U.S. GAAP, are not covered positions.

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[19] By "**internal hedge**," we mean a transaction between a bank's trading book desk and banking book desk whereby risk is transferred from the banking book to the trading book and subsequently hedged in the external market.

Ninth, the definition of covered position excludes any "direct real estate holding" (in paragraph (3)(vii) of the definition), consistent with the existing MRC Rules. The text of the NPR discussing that exclusion[20] comments that "[i]ndirect investments in real estate, such as through real estate investment trusts or special purpose vehicles, must meet the definition of a trading position in order to be a covered position."

We read this language to mean that, if the security in or exposure to a REIT or special purpose vehicle held by a bank meets the requirements for a covered position, even though the REIT or special purpose vehicle may represent a structured financing of a single or small number of commercial or residential real estate assets or mortgage positions, that the treatment of the position as a covered position is proper, and that the purpose of the above-quoted language is simply to caution banks that re-packaging otherwise directly held non-qualifying securities or exposures within a REIT or special purpose vehicle will not in itself support market risk treatment. We would appreciate the Agencies clarifying that our understanding is correct.

C. Question 4: Under what circumstances should the Agencies require a model-specific capital supplement? What criteria could the Agencies use to apply capital supplements consistently across banks? Aside from a capital supplement or withdrawal of model approval, how else could the Agencies address concerns about outdated models?

The Associations urge the Agencies not to address model shortcomings with a formal model-specific capital supplement requirement but instead to address shortcomings on a bank-specific basis, fashioning a remedy or consequence that is appropriate to the circumstances. We very much agree with the Proposed MRC Rules' requirement that a bank review its internal models no less frequently than annually, in light of, among other things, developments in financial markets and modeling technologies, and more generally we agree with the NPR text accompanying Question 4. However, we do not believe that model shortcomings are likely to be best addressed in a standardized manner, including a model risk multiplier similar to the back-testing multiplier as suggested in the NPR. The amount and manner of calculation of the additional capital that is needed will most certainly depend on the circumstances, especially on the nature and details of the shortcomings in the relevant bank's models. If any supplement is to be applied on a bank-specific basis instead of uniformly across banks, the Agencies do not need any additional authority for requiring that a particular

[20] 76 Fed. Reg. at 1895 (2nd column).

bank satisfy higher than minimum capital requirements. The existing regulations already provide that authority.

Finally, we note that an automatic and formulaic capital supplement would be procyclical, with the deficiencies more likely to be recognized during periods of market distress than periods of financial stability.

D. Question 5: The Agencies request comment on any challenges banks may face in formulating the measure of trading loss as proposed, particularly for smaller portfolios. More specifically, which, if any, of the items to be excluded from a bank's measure of trading loss (fees, commissions, reserves, intra-day trading, or net interest income) present difficulties and what is the nature of such difficulties?

Challenges with respect to the exclusions from the proposed measure of trading loss mostly arise from a lack of historical data. In order to allow banks time to create the necessary data base, under Section 4(b), banks should be permitted, during the two years after the Proposed MRC Rules become effective, to calculate trading losses for back-testing purposes by including or excluding fees, commissions, reserves, net interest income and, subject to the comment below, intra-day trading, as long as this is done consistently. Many banks currently maintain data with respect to trading losses and gains only on a basis that includes these elements. It may not be possible to create historical information that excludes these elements. Moreover, because banks are not required to capture intra-day gains and losses for purposes of financial reporting, many banks will need time to design the systems necessary to capture changes in revenue resulting from intra-day gains and losses. Although we agree that the MRC Rules ultimately should move to back-testing calculations that exclude these elements, the Agencies should permit banks time to come into compliance.

E. Question 6: The Agencies request comment on what, if any, challenges exist with the proposed subportfolio backtesting requirements described above. How might banks determine significant subportfolios of covered positions that would be subject to these requirements? What basis could be used to determine an appropriate number of subportfolios? Is the p-value a useful statistic for evaluating the efficacy of a bank's VaR model in gauging market risk? What, if any, other statistics should the Agencies consider and why?

We generally support the requirement in Section 5(c) that a bank divide its portfolio into significant sub-portfolios for purposes of VaR calculations, as well as the refinements to the back-testing process set forth in the Section 4(b). However, we urge the Agencies to permit substantial discretion and flexibility in identifying "significant sub-portfolios" for purposes of Section 5(c). Generally speaking, we believe

banks should be permitted to identify sub-portfolios based upon the internal management structure of the bank. To do otherwise would create two sets of books with cumbersome parallel systems, and would impede the practical use of back-testing results. Sub-portfolio categorization is likely to vary significantly across banks. We do not believe that is problematic. In general, the Agencies might expect similar sub-portfolio differentiation along broad product lines – for example, grouping together desks that are primarily sensitive to interest rates, foreign exchange, equities, municipal securities, credit products (bonds, loans and derivatives) or mortgage products (residential or commercial). However, requiring a strict division along product lines would itself be problematic. Some desks are designated to focus on a particular client base with a variety of products. We are concerned that further differentiation by the factors identified in the NPR – trading volume, product type and number of distinct traded products, business lines or number of traders or trading desks – would misrepresent the bank's risk by giving undue weight to excessively granular portfolios, introducing a degree of "statistical noise," and removing diversification benefits.

In addition, we urge the Agencies to be sensitive to the operational challenges banks will face complying with the subportfolio backtesting requirements. Organizational changes and model enhancements can affect the availability of the time series data for subportfolio backtesting and raise complicated operational issues. For example, occasionally portfolios are re-aligned to reflect new organizational hierarchies for various business reasons. When this occurs, it may not be operationally feasible to reconstruct the historical time series under the new hierarchy. Similarly, when models are enhanced, it may not be operationally feasible to reconstruct two years of model results.

We do not believe that p-values add sufficiently explanatory power to warrant the additional effort of calculating p-values. Banks generally already have in place band breaks to flag inadequate modeling. Band breaks may be a crude tool, but so is general VaR. That is why other market risk elements have been added in the Proposed MRC Rules. The p-value metric ascribes more precision to the tail probability assessment of general VaR than is warranted. To fairly reflect the adequacy of market risk calculations under the Proposed MRC Rules, the p-value would need to be stated in terms of the full market risk amount, not just the general VaR term. In particular, the stressed VaR element captures losses that, over a long enough time horizon, are expected to go beyond the level represented by data in the general VaR timeframe.

F. Question 7: What specific standards of creditworthiness that meet the Agencies' suggested criteria for a creditworthiness standard outlined above should the Agencies consider for these positions?

The Associations appreciate the Agencies' continuing efforts to establish standards of creditworthiness for capital and other purposes that are consistent with

Dodd-Frank Section 939A. We recognize that inadequacies in the issuance and use of credit ratings contributed to the financial crisis, but we believe a complete abandonment of ratings is ill advised and an over-reaction. While Section 939A makes it necessary to develop alternatives to credit ratings for purposes of capital regulations, any alternative requires careful scrutiny to ensure that it can be verified by regulators, used by all banking organizations (including those without a sophisticated modeling capacity), and reflected in U.S. implementation of global prudential and regulatory standards. We are very concerned that an alternative approach to Basel II.5's use of ratings will not be developed (and evaluated by the Agencies and banks alike with the care that is necessary for its implementation as a fundamental component of the Agencies' capital regulations) in a sufficiently timely manner to permit its use in the final revised MRC Rules. Accordingly, we urge the Agencies to work with Congress to amend Dodd-Frank Section 939A, at least to the extent necessary to enable the Proposed MRC Rules to incorporate the more risk-sensitive treatment of debt, securitization and re-securitization positions provided for in the Basel II.5 market risk rules for a period that permits development of an appropriate alternative measure of credit risk. We appreciate, however, that statutory relief may not be forthcoming and, accordingly, will continue to work with the Agencies to develop solutions.

TCH, IIF, SIFMA and ABA commented on the Agencies' advanced notice of proposed rulemaking (the "**Section 939A ANPR**"), the comment period for which expired on October 12, 2010, to revise their risk-based guidelines and regulations to remove any reference to, or requirement of reliance on, credit ratings and to substitute other standards of creditworthiness.[21] The Associations adhere to the views expressed in those letters.

The criteria in the text accompanying Question 7 of the NPR (which are the same criteria as those set forth in the Section 939A ANPR) that are the most challenging in this context include:

- Be sufficiently transparent . . . replicable, and defined to allow banking organizations of varying size and complexity to arrive at the same assessment of creditworthiness for similar exposures . . .;

• • •

- Be reasonably simple to implement and not add undue burden on banking organizations . . . .

[21] 75 Fed. Reg. 52283 (August 25, 2010).

Larger banks – for the most part, the internationally active banking organization subject to the U.S. version of Basel II – have well-developed internal modeling capabilities for many exposures. Smaller banks generally do not. Moreover, even for the larger banks, issues of transparency, replicability and simplicity are significant.

Although Section 939A of Dodd-Frank prohibits the Agencies from referring to or requiring the use of credit ratings, it does not prohibit a bank from considering such ratings in analyzing credit quality or modeling risk. We believe Section 939A allows the Agencies to adopt standards of creditworthiness that permit the consideration of ratings without expressly referencing them or mandating their use. That flexibility, however, will not lend itself to development of alternative standards in the near term that meet the specified criteria, particularly the two referenced above.

Accordingly, as set forth above, we urge the Agencies to work with Congress to modify Section 939A to the extent necessary to permit credit ratings to be used in bank capital regulations, including the MRC Rules, to the extent doing so is required for consistency with international standards, pending development of an appropriate alternative measure of credit risk. Forcing U.S. banks to continue to apply the current standardized measurement method for debt, securitization and re-securitization positions frustrates the important objective of international harmonization of capital requirements. There can be no question but that the Basel II.5 standards, using the words of the Agencies in the NPR, "would provide a more risk-sensitive treatment for these positions than exists under the current rule."

G. Question 8: What, if any, specific challenges are involved with meeting the proposed due diligence requirements and for what types of securitization positions? How might the Agencies address these challenges while still ensuring that a bank conducts an appropriate level of due diligence commensurate with the risks of its covered positions? For example, would it be appropriate to scale the requirements according to a position's expected holding period? How would such scaling affect a bank's ability to demonstrate a comprehensive understanding of the risk characteristics of a securitization position? What are the benefits and drawbacks of requiring public disclosures regarding a bank's processes for performing due diligence on its securitization positions?

Trading decisions must be made on an informed basis. We agree with the concern expressed by the BCBS in the July 2009 enhancements that "banks perform their own due diligence and do not simply rely on rating agency credit ratings."[22] And

[22] July 2009 Enhancements – Introduction, paragraph 4 (page 1). The NPR's language with respect to due diligence requirements for securitizations largely derives from Part VI,

we agree that basing trading decisions largely on ratings assigned by a third party rating agency is not sufficient. Ratings may be a factor in the decision-making process, but only a factor. Marketplace realities often require that trading decisions be made quickly, sometimes within a matter of minutes. Requiring a bank to "conduct and document" an analysis of "each securitization position" in the manner contemplated by the NPR, and potentially subject the bank to a notation on examination if the bank does not maintain a file for each securitization position demonstrating that the documentation was gathered and analyzed prior to the acquisition of the position, would force some trading desks to simply shut down and have other adverse unintended consequences. Compliance with the NPR's standards would be particularly challenging in connection with secondary trading. Trading desks likely would only make a market in transactions that their firms underwrote and issued in the marketplace or in a limited number of "on-the-run" securitization transactions that are highly liquid and for which there is easily accessible transactional and market information. This would limit the universe of transactions where banks will be willing to act as market-makers and provide liquidity. As a result, transactions that do not fit within the outlined criteria might be less liquid and could experience much wider bid-ask spreads resulting from diminished liquidity. This could potentially result in higher cost of liquidity that could be passed on to the broader economy.

At a minimum, we therefore urge the Agencies to allow banks to satisfy the NPR's documentation requirements by the end of the day on which they acquire a securitization position other than a newly originated securitization position, rather than prior to the time of acquisition as specified in paragraph (d)(2)(i) of Section 10. For newly originated securitizations, the documentation required to comply with these requirements is often not available until several days after the related security is acquired. Therefore, for such originations, banks should be allowed at least three days to comply with the NPR's due diligence documentation requirements.

Further, we urge the Agencies to make appropriate grandfathering and transitional arrangements for securitization positions existing before the due diligence standards become effective. Similar arrangements have been made in Europe as banks there come into compliance with Article 122a of the revised Capital Requirements Directives.[23] Grandfathering and transitional arrangements would promote competitive equality and provide banks with the time necessary to develop the policies and

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Section 565, of Basel II.5 as added by the July 2009 Enhancements but is substantially more rigid.

[23] See paragraphs 131 to 137 of the Committee of European Banking Supervisors' Guidelines to Article 122a of the Capital Requirements, dated December 31, 2010 (the "**Guidelines**").

procedures needed to comply with the NPR's due diligence standards, while at the same time maintaining the broadest possible market for securitization positions (particularly traditional ABS) and not limiting arbitrarily the liquidity of these positions. A failure to implement transitional and grandfathering arrangements would disadvantage U.S. banks and damage markets for ABS instruments, since it would limit the participation of banks subject to the NPR in certain ABS markets.

The Associations agree that a bank's analysis of a securitization position must be commensurate with the complexity and materiality of the position in relation to capital as required under paragraph (d)(1) of Section 10. Consistent with the foregoing, we urge the Agencies to clarify that the specific elements outlined in paragraphs (d)(2)(i)(A) through (D) of Section 10 may be of greater or lesser importance depending on the specific risk characteristics of the securitization position. This could be accomplished by inserting the phrase "as appropriate" at the end of the introductory language in paragraph (d)(2) of Section 12. Taking this approach would be both sensible and bring the NPR's due diligence requirements into line with the Guidelines, thereby promoting international harmonization of due diligence standards.[24]

Finally, we do not believe that required public disclosure of due diligence practices is a sensible approach. The premise behind a disclosure approach would be that market discipline will force banks to behave in a prudent manner. We are very skeptical that, were this issue addressed in disclosure, the disclosure among banks subject to the MRC Rules would be sufficiently different so as to call market discipline into play.

H. Question 9: What alternative nonmodels-based methodologies could the Agencies use to determine the specific risk add-ons for securitization positions? Please provide specific details on the mechanics of and rationale for any suggested methodology. Please also describe how the methodology conservatively recognizes some degree of hedging benefits, yet captures the basis risk between non-identical positions. To what types of securitization positions would such a methodology apply and why?

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[24] See paragraph 82 of the Guidelines ("Consequently, the specific elements outlined in clauses (a) through (g) of Paragraph 4 [which list the information that credit institutions must obtain when investing and on an ongoing basis] should not be regarded as a minimum threshold to be met on a mechanical basis. In other words, specific elements of such clauses (a)-(g) may be of greater, lesser, or negligible importance, depending on the specific characteristics and risk profile of the trading book. Thus, while the scope of due diligence is defined by clauses (a)-(g) of Paragraph 4, the intensity of such due diligence with respect to each of these specific elements may vary (if justified) according to the specificities of the trading book versus the non-trading book.").

Although the Associations believe that consideration of non-models-based methodologies to determine the specific risk add-ons for securitization positions should be undertaken, we do not have a developed methodology to suggest at this time. However, in general and consistent with the discussion in Part III.A.6 and Part III.A.8, we believe that the specific risk add-on should not exceed the maximum potential loss of the securitization position and should permit de-construction of the components of the securitization position, so that the add-on does not result in additional capital requirements for risk-reducing hedges. We look forward to working with the Trading Book Group to consider possible methodologies.

I. Question 10: What are the benefits and drawbacks of the supervisory stress scenario requirements described above and what other specific stress scenario approaches for the correlation trading portfolio should the Agencies consider? For which products and model types are widely applicable stress scenarios most appropriate, and for which product and model types is a more tailored stress scenario most appropriate? What other stress scenario approaches could consistently reflect the risks of the entire portfolio of correlation trading positions?

The Associations support robust stress testing of correlation trading positions (and of covered positions more generally) and believe that banks and the Agencies must work together to enhance the approaches to and standards for stress testing over time. This is an area, though, where it is particularly important that the Agencies adopt a flexible approach and assess a bank's approach to stress testing as part of on-going oversight and supervision. Although stress scenarios must reflect differences in specific products and models, it will be equally important for the scenarios to cover both directional market moves as well as the basis risks that arise in typical trading strategies. In addition, the Associations support the need for more robust benchmarking of approaches through regular "test portfolio" type exercises.

J. Question 11: What, if any, specific challenges exist with respect to the proposed modeling requirements for correlation trading positions? What additional criteria and benchmarking methods should the Agencies consider that would provide an objective basis for evaluating whether to allow a bank to apply a lower surcharge percentage in calculating its comprehensive risk measure? What are the advantages and disadvantages of the proposed floor approach and the other potential floor approaches described above? What other alternatives should the Agencies consider to address the uncertainties identified above while ensuring safe and sound risk-based capital requirements for correlation trading positions?

The Associations believe this topic requires analysis by the Trading Book Group as part of its fundamental review. The floor approach, as proposed, has the consequence that a bank that adds a hedge to its correlation trading position becomes subject, on a net basis, to an increased capital requirement because under the floor approach the hedge will not be recognized and will actually attract a capital charge. That is an inappropriate result running counter to good policy. More generally, we believe that any decisions made regarding this topic should be based on an empirical assessment of how a bank's comprehensive risk measure approach would have fared during the financial crisis and should incorporate plausible forward looking stress scenarios, taking into account the double- and triple-counting in the market risk framework highlighted in Part.II.A. Pending the Trading Book Group's fundamental review, we request that the Agencies confirm our understanding that multiple correlation trading portfolios within the same bank can be treated on a combined basis for the application of the comprehensive risk measure and floor calculations.

We look forward to working with the Trading Book Group to develop a sensible approach to address the issues identified in Question 11.

K. Question 12: The Agencies seek comment on the effectiveness of the proposed disclosure requirements. What, if any, changes to these requirements would make the proposed disclosures more effective in promoting market discipline?

The NPR prescribes a number of risk measures that are required to be disclosed. We believe that banks should have the flexibility to (i) define or identify what is a "portfolio" for disclosure purposes, taking into account the bank's judgment as to the meaningfulness and materiality of the disclosure, and (ii) determine and disclose risk measures that are the most meaningful to their portfolios. The reporting of VaRs based on differing categorizations between what is in the trading book for regulatory capital purposes versus accounting standards is likely to add to market confusion rather than transparency. The Associations also view stress testing scenarios as proprietary and do not support detailed disclosure of stress tests that banks have applied. Other market participants may be able to reverse engineer the results to yield the exposures and thus compromise the market.

The Associations are also concerned that the timing of the proposal does not line up with the timing of disclosure requirements in Basel II. For Basel II banks, we believe that the market risk and Basel II disclosure regimes should become effective at the same time.

Finally, the Associations note that the proposal goes beyond Basel II.5 in asking for the median of various risk measures. We ask that the Agencies limit the required disclosures to the high, low and mean of any particular risk measure.

* * *

The Associations appreciate your consideration of the views expressed in this letter. If you have any questions, please contact any of the following representatives of the Associations: Joe Alexander of TCH at 212-612-9234 (e-mail: joe.alexander@theclearinghouse.org), Mark Tenhundfeld of the ABA at 202-663-5042 (e-mail: mtenhund@aba.com), David Schraa of the IIF at 202-857-3312 (e-mail: dschraa@iif.com), David Murphy of ISDA at 020-3088-3574 (e-mail: dmurphy@isda.org), or Kenneth Bentsen of SIFMA at 202-962-7400 (e-mail: kbentsen@sifma.org).

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Annex 1

The Associations

TCH is an association of major commercial banks. Established in 1853, TCH is the United States' oldest banking association and payments company. It is owned by the world's largest commercial banks, which collectively employ 1.4 million people in the United States and hold more than half of all U.S. deposits. TCH is a nonpartisan advocacy organization representing through regulatory comment letters, amicus briefs, and white papers the interests of its member banks on a variety of systemically important banking issues. Its affiliate, The Clearing House Payments Company L.L.C., provides payment, clearing, and settlement services to its member banks and other financial institutions, clearing almost $2 trillion daily and representing nearly half of the automated clearing-house, funds-transfer, and check-image payments made in the U.S. See TCH's web page at www.theclearinghouse.org.

The ABA represents banks of all sizes and charters and is the voice of the nation's $13 trillion banking industry and its 2 million employees. The majority of ABA members are banks with less than $165 million in assets. Learn more at www.aba.com.

The IIF is the world's only global association of financial institutions. Created in 1983 in response to the international debt crisis, the IIF has evolved to meet the changing needs of the financial community. The IIF now serves its membership in three distinct ways:

- Providing analysis and research to its members on emerging markets and other central issues in global finance.
- Developing and advancing representative views and constructive proposals that influence the public debate on particular policy proposals, including those of multilateral Agencies, and broad themes of common interest to participants in global financial markets.
- Coordinating a network for members to exchange views and offer opportunities for effective dialogue among policymakers, regulators, and private sector financial institutions.

The IIF is headquartered in Washington, D.C., and in November 2010 opened its Asia Representative Office in Beijing. IIF members include most of the world's largest commercial banks and investment banks, as well as a growing number of insurance companies and investment management firms. Associate members include multinational corporations, trading companies, export credit Agencies, and multilateral Agencies. Approximately half of the IIF's members are European-based financial

institutions, and representation from the leading financial institutions in emerging market countries is also increasing steadily. By 2011, the IIF's members include over 430 of the world's leading banks and finance houses, headquartered in more than 70 countries.

ISDA, which represents participants in the privately negotiated derivatives industry, is among the world's largest global financial trade associations as measured by number of member firms. ISDA was chartered in 1985 and today has over 800 member institutions from 54 countries on six continents. Our members include most of the world's major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end-users that rely on over-the-counter derivatives to manage efficiently the risks inherent in their core economic activities. For more information, please visit: www.isda.org.

SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to develop policies and practices which strengthen financial markets and which encourage capital availability, job creation and economic growth while building trust and confidence in the financial industry. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association.