Meeting Between Staffs of the Federal Reserve Board, the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and Barclays
November 1, 2016

Participants: Peter Clifford, Kevin Littler, Christopher Powell, Rena Miller, Dafina Stewart, Adam Cohen, Brian Chernoff, and Josh Strazanac (Federal Reserve Board)

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Summary: Staffs of the Federal Reserve Board, FDIC, and OCC met with representatives of Barclays to discuss the notice of proposed rulemaking to establish the Net Stable Funding Ratio in the United States. Specifically, the representatives discussed the treatment of derivatives under the proposed rule, including the treatment of gross derivatives liabilities, variation margin, and initial margin. The representatives also discussed the scope of institutions that should be subject to the proposed rule. Further details on the discussion are provided in the attachment.

Attachment

Proposed US NSFR Rule

November 2016

Agenda

1. Introduction
2. Key concerns
    1. Disparate treatment of Foreign Banking Organizations
    2. Trading securities
    3. Repo book asymmetry
    4. Short sales
    5. Extended settlements and trade date receivable fails
    6. Collateral substitution
    7. Off-balance sheet collateral swaps

1. Introduction

Barclays welcomes the concept of a longer-term measure of structural liquidity and the policy intentions of incentivizing financial institutions to develop and maintain sustainable funding structures;

However, we are concerned that the net stable funding ratio (NSFR) requirements as proposed do not strike an appropriate balance between:

- Supporting a safe and sound financial system, and
- Imposing a substantial economic and operational tax across several layers of market participants that would:
  - Restrict certain fundamental capital markets activities in the US to the point of noneconomic viability;
  - Increase bid-offer spreads, increase volatility and reduce market liquidity in primary and secondary markets;
  - Detract from financial stability; and
  - Result in higher operating costs for end-users such as pension funds, life insurers, asset managers, mortgage holders through the agency repo market, and the US Treasury through the Treasury repo market, as well as the customers they serve

We believe the financial stability benefits of the proposed NSFR could be delivered at lower cost

1.1 Background

The Basel Committee released the NSFR Framework with:

- Many new features that were added without consultation
- No supporting impact study or published empirical analysis
- No review period before migrating to Pillar 1 standard (as was usefully the case with the leverage ratio)

Banks are now turning their attention to the NSFR as the US and EU write rules. The key areas of concern and feedback from the industry are:

- Lack of empirical support for harsh treatment of repo and trading activities
- Significant number of technical issues (e.g., requiring funding for transactions that are self-funding, or methodologies that are not proportionate to the risk)
- Regulators' belief that the industry is broadly in compliance without acknowledging challenges to specific activities and the realities of internal cost allocations
- *Likelihood of material variation between adopted forms of NSFR in the US, the UK, and the EU*

1.2 Key concerns

Barclays is most concerned with three aspects of the proposed NSFR rule:

1. **Financing businesses would become uneconomic** – the additional costs of complying with the NSFR would create real challenges for certain financing businesses to produce returns above the cost of capital—up to 50% margin reductions in certain instances—with US Treasury and Agency repo and collateral swaps among the most impacted
2. **Insufficient impact analysis** – the Agencies may have neglected to include IHCs in their $39 billion estimate of the total US NSFR shortfall, which would represent a significant miscalculation of the total impact to the industry and resulting effects on the US financial system
3. **Disparate treatment of (and among) Foreign Banking Organizations (FBOs)** – the NPR requires some intermediate holding companies (IHCs) to comply with the "full" NSFR even if the profile of their domestic and international activities otherwise more closely resemble those of a Covered Company to which the Modified NSFR would apply

We believe there needs to be an urgent regulatory intervention that delivers a more realistic calibration of the standard which closes – but in all likelihood will not eliminate – the gap between the stable funding requirements of the standard and prudent industry and supervisory practices

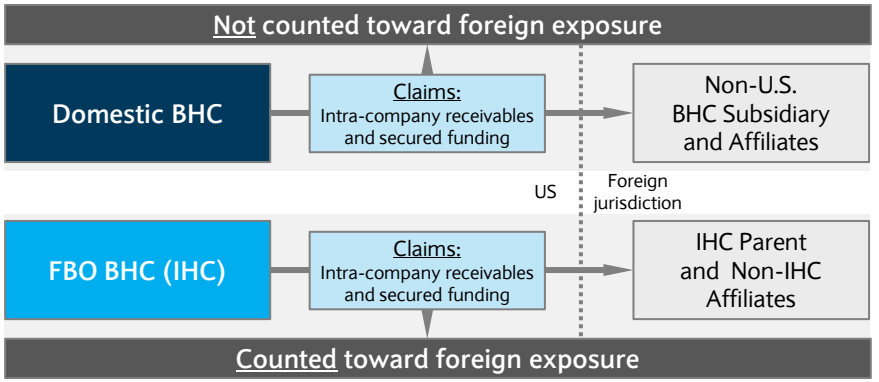
2.1 Disparate treatment of foreign banking organizations

The foreign exposure calculation applied by the proposed rule treats the IHCs of certain FBOs unfairly vis-à-vis US-based BHCs and other IHCs

Key concerns

- The proposed rule would include intra-company receivables between an IHC and its foreign parent and its non-IHC affiliates in the calculation of "foreign exposures", while US BHCs do not include intra-company claims of foreign affiliates
- This in turn would require an IHC to comply with the "full" NSFR requirement when the profile of its international activities more closely resembles that of a Covered Company to which the Modified NSFR requirements would apply
- The $10bn foreign exposure threshold was established nearly 10 years ago specifically to identify US-based BHCs that should therefore use advanced approaches to calculate risk-based capital ratios
- The threshold should not be applied to IHCs given i) the concept of an IHC did not exist when the threshold was established, ii) it did not contemplate commonplace intra-company transactions between an IHC and its foreign parent, and iii) IHCs are exempt from advanced approaches for risk-based capital calculations
- The $10bn foreign exposure threshold is not risk-sensitive and should be replaced with a more sophisticated method such as the BCBS systemic indicator approach that the Federal Reserve has implemented in the US for identifying D-SIBs and G-SIBs

Figure 1. Incongruent treatment of domestic and FBO intra-company transactions



Recommendations

- Exclude an IHC's exposures to both the foreign parent bank and affiliates and the foreign parent bank's home country sovereign from the foreign exposures calculation methodology
- Alternatively, consider removing the threshold altogether in lieu of a risk-sensitive framework such as the BCBS systemic indicator approach

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2.2 Trading securities (1/2)

NSFR weightings are derived from the LCR framework and are not appropriate for a one-year less-stressed measure

Key concerns

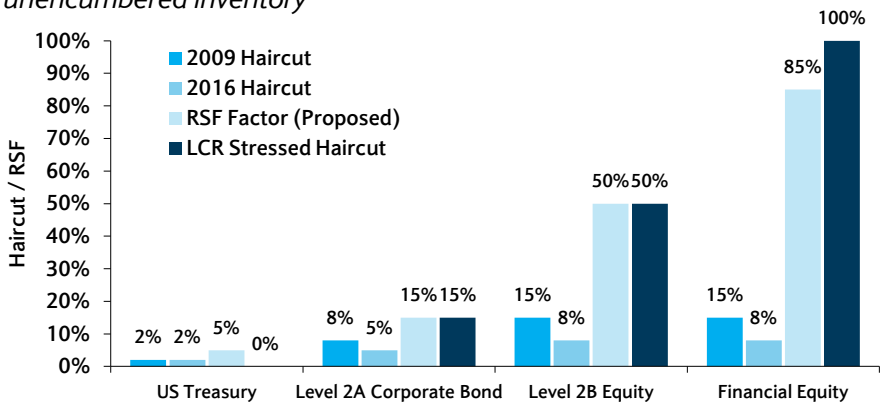
- Proposed RSF factors are the same or more severe than those used in the LCR rule—a metric calibrated to a severe stress—and effectively extend the LCR severe idiosyncratic liquidity stress to 180 days
- The RSF factor for securities is significantly higher than current secured funding haircuts, particularly for equity securities and securities issued by financial institutions—2.5x to 10.6x current repo haircuts, which is substantially higher than stressed haircuts observed during the recent financial crisis
- The RSF factor for a financial stock is materially higher than a level 2B equity despite no significant difference in repo market haircuts; this read-across from the LCR is conceptually inconsistent with a less stressed NSFR measure

Figure 2. Average ASF factors for whole financial liabilities

Tenor	3M	6M	9M	1Y	2Y	5Y	10Y
Average ASF	0%	0%	17%	25%	62.5%	85%	92.5%

- NSFR also impacts the same low-risk market-making and repo activities that are also impacted by the leverage requirement

Figure 3. RSF factors vs. tri-party funding haircuts and LCR haircuts for unencumbered inventory



Sources: Bank for International Settlements, Federal Reserve, Barclays Analysis

Recommendations

- Recalibrate the RSF factors in a manner consistent with the ASF factors and address the substantial disincentive to make markets in financial institution debt and equity
- Remove the LCR restrictions on financial securities
- Lower the 5% RSF factor for Level 1 HQLA to 0% (as is the case in the LCR, which is a more severe scenario)
- Reduce the 50% RSF factor for main index equities to 25%, a value that reflects their resilient market liquidity and is supported by data

*For example, a one-year debt security issued by the bank would receive 50% ASF for the first six months and 0% for the second six months, for an average of 25% ASF.

2.2 Trading securities (2/2)

As proposed, the NSFR would exceed the cost of leverage requirements and result in a four-fold increase in the cost of capital

Figure 4. Impact of proposed NSFR on returns

Non-HQLA Exchange Traded Equity	RWA ($m)	Leverage ($m)
Notional	100.0	100.0
Exposure measure	17.6	108.0
Capital ratio required	12%	4%
Capital required	2.1	4.3
Cost of capital	0.2	0.4
Incremental cost of capital due to leverage reqmt		0.2
Incremental cost as a proportion of notional		20 bps

NSFR Calculation	($m)	
Required stable funding	85.0	
Available stable funding:		
Funding for haircut	3.7	
Capital	4.3	
Incremental term funding required	77.0	
Cost of incremental funding (bps)	100	
Total incremental cost of NSFR funding	0.77	
Incremental cost as a proportion of notional	**77bps**	
Cost of leverage and NSFR		**97bps**

Potential impacts

- We estimate an incremental 77bps NSFR cost for financing financial stocks, which significantly exceeds the c. 20bps incremental cost of the leverage requirements and results in a four-fold increase in the cost of capital
- We expect a significant impact on market liquidity as Covered Companies reduce activity in response to these extra costs

Assumptions

- Exposure measure for risk-weighted assets ("RWA") is calculated as the sum of general (8%) and specific market risk (8%) and a standardized counterparty credit risk of 20% on a haircut of 8%
- Exposure measure for leverage is the notional plus haircut
- Capital required is based on CET1 target of 12% and T1 leverage of 4%
- Internal cost of capital is 10%
- RSF on a financial stock is 85%, as per NSFR proposed rule
- RSF is reduced by the unsecured funding raised for the haircut and capital already raised for RWAs and leverage
- 100bps incremental cost of raising 1 year evergreen repo for a main index equity

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2.2.1 Tri-party Repo Infrastructure Reform Task Force – US Tri-Party Haircut Statistics*

The Proposed RSF factors for unencumbered assets and securities financing transactions (SFTs) are significantly higher for many asset classes, compared to the US Tri-party market haircut statistics

		As of Sep 12, 2016				Average				Max			NSFR RSF		RSF vs. Avg Median	
		Market Volume		Haircut (%)		Market Volume		Haircut (%)		($bn)	Haircut (%)					
	Asset Class	% of Total	$bn	Median	90th Percentile	% of Total	$bn	Median	90th Percentile	Market Volume	Median	90th Percentile	Asset RSF% [(a)]	SFTs RSF% (<6M)	Asset RSF% [(a)]	SFTs RSF% (<6M)
Non-Fedwire-Eligible	Equities	7%	$ 115.1	8.0	15.0	7%	$ 112.2	7.9	15.1	$ 168.5	8.0	20.0	50/85	15	6.3x / 10.7x	1.9x
	ABS Investment Grade	1%	14.1	5.0	10.0	1%	19.9	5.2	10.5	26.1	7.0	15.0	85		16.4x	2.9x
	ABS Non Investment Grade	2%	28.4	15.0	30.0	1%	22.5	8.2	18.9	39.5	15.0	30.0	85		10.4x	1.8x
	CDOs	0%	0.5	6.4	21.0	0%	1.5	7.4	16.0	3.5	15.0	25.0	85		11.4x	2.0x
	CMO Private Label Investment Grade	1%	8.9	7.0	15.0	1%	13.1	6.3	13.1	22.8	8.0	15.0	85		13.5x	2.4x
	CMO Private Label Non Investment Grade	1%	21.9	10.0	20.0	2%	26.3	7.7	17.8	41.2	10.0	25.0	85		11.0x	1.9x
	Corporates Investment Grade	3%	52.3	5.0	8.5	3%	56.6	5.0	9.1	88.2	5.0	10.0	15/50/85		3.0x / 10.0x / 17.0x	3.0x
	Corporates Non Investment Grade	2%	26.4	10.0	15.0	1%	24.9	8.1	15.4	37.8	10.0	20.0	50/85		6.2x / 10.5x	1.8x
	International Securities	0%	3.4	2.0	10.0	0%	3.0	2.8	5.7	6.2	5.0	15.0	15/50/85		5.3x / 17.8x / 30.3x	5.3x
	Money Market	1%	13.0	3.0	5.0	1%	19.6	4.5	5.1	31.7	5.0	6.0	15/50/85		3.3x / 11.1x / 18.9x	3.3x
	Municipality Debt	1%	12.2	5.0	8.0	1%	13.8	5.0	10.3	20.7	5.0	16.2	15/50/85		3.0x / 10.0x / 17.0x	3.0x
	Whole Loans	0%	0.9	6.0	15.0	0%	2.7	11.9	15.1	5.8	15.0	20.2	50/65		4.2x / 5.5x	1.3x
	Total Non-Fedwire-Eligible	**18%**	**$ 297.0**			**19%**	**$ 315.9**									
Fedwire-Eligible	US Treasuries excluding Strips	48%	784.5	2.0	2.0	35%	583.3	2.0	2.0	784.5	2.0	2.1	5	10	2.5x	5.0x
	US Treasuries Strips	2%	30.3	2.0	3.0	3%	42.3	2.0	2.6	58.5	2.0	3.0			2.5x	5.0x
	Agency Debentures & Strips	2%	40.4	2.0	3.0	6%	97.4	2.0	3.8	185.3	2.0	5.0	5/15	15	2.5x / 7.5x	7.5x
	Agency MBS	27%	438.5	2.0	3.0	32%	526.1	2.0	3.1	766.1	2.0	4.0			2.5x / 7.5x	7.5x
	Agency CMOs	3%	57.5	3.0	17.6	6%	99.6	3.0	7.9	152.5	4.0	20.0			2.5x / 4.9x	4.9x
	Total Fedwire-Eligible	**82%**	**$ 1,351.2**			**81%**	**$ 1,348.6**									
	Total Volume	100%	$ 1,648.2			100%	$ 1,664.5									

(a) RSF factors for assets that are unencumbered or encumbered for less than 6 month

*Source: https://www.newyorkfed.org/data-and-statistics/data-visualization/tri-party-repo#interactive/haircut

1. Data from May 2010 to Sep 2016 – 77 data points (one data point per month, 7th business day of each month)
2. US tri-party repo trades (excluding GCF repos) settled in the two US Tri-party Repo clearing banks (BNYM and JPMC) – data is reported by asset class with volumes (including Top 3 dealers share) and haircuts (the median, 10th and 90th percentile)

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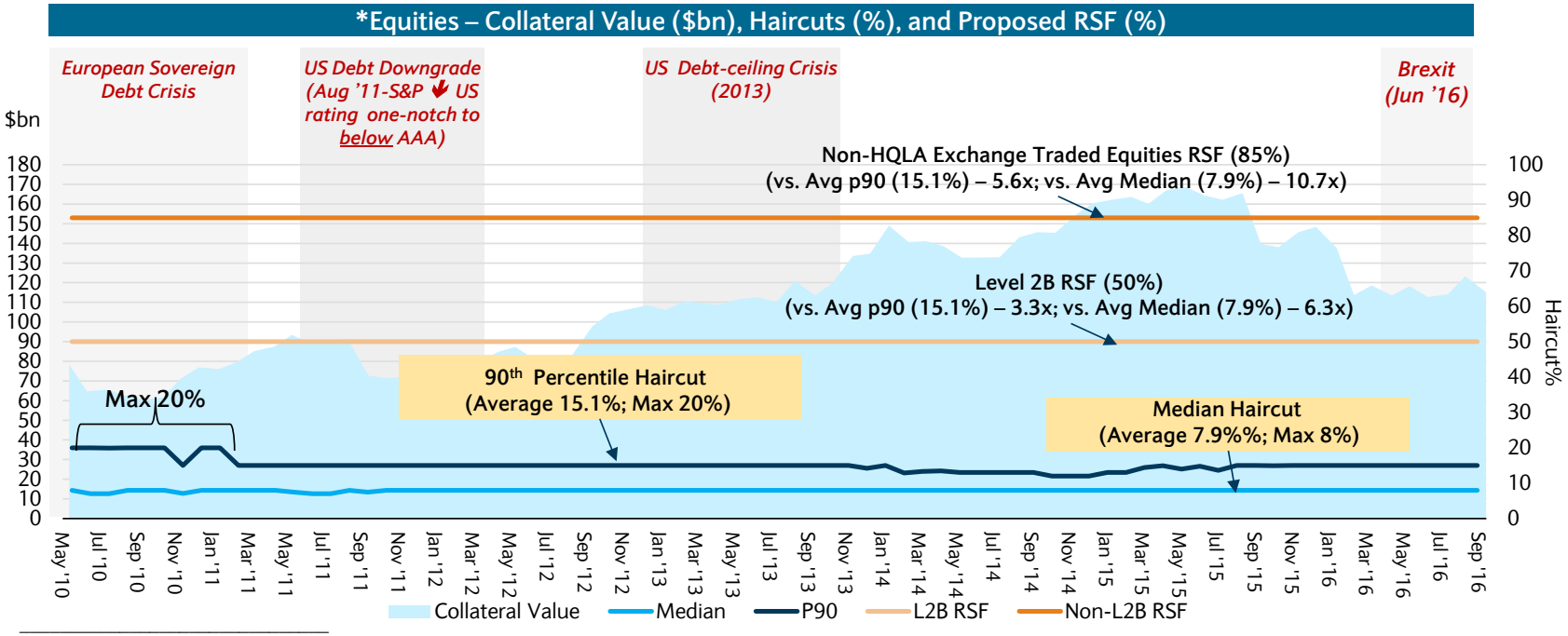
2.2.2 Equities Asset Class – US Tri-Party Haircut Trend*

Based on the historical haircuts (77 data points), the equities haircuts are well below the proposed NSFR RSF of 50/85% for unencumbered exchange-traded equities

- As of September 12, 2016, $115bn equities tri-party volume (~7% of the total US tri-party population of $1,648bn). Since the financial crisis in 2007-2008, the market has experienced a number of other financial crises/events
- The median haircut (~8%) is relatively stable; the average 90th percentile haircut of ~15% (Max at 20%); Compared to the market averages, the Proposed RSF factors are multiples higher:

Market Average	Non-L2B (85% RSF)	L2B (50% RSF)
90th percentile haircut of 15%	5.6x	3.3x
Median haircut of 8%	10.7x	6.3x



* Collateral Value and Haircut data sourced from "https://www.newyorkfed.org/data-and-statistics/data-visualization/tri-party-repo#interactive/haircut"

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2.3 Repo book asymmetry (1/2)

The asymmetrical treatment of repo transactions is not gauged to collateral quality, discourages prudent liquidity risk management, and would cause a further contraction of the repo market

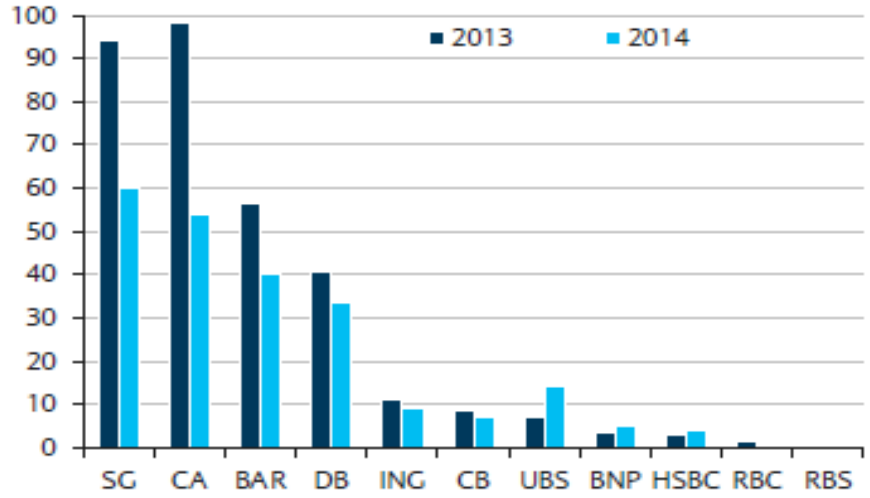
Key concerns

- Transactions in which a Covered Company enters into reverse repos (matched book or otherwise) would require RSF of 10% or 15% while financing these transactions with financial institutions for less than 6 months would attract a 0% ASF regardless of the quality of the asset collateralizing the repo liability
- The proposed rule assumes that Covered Companies would be unable to roll over repos secured by Level 1 HQLA, bearing in mind that 100% roll-over is assumed in the LCR rule (which is intended to capture a more severe scenario)
- The 10% RSF factor does not recognize that Covered Companies transact in reverse repos for purposes other than a matched book, such as short covering and as a tool for managing short-term liquidity mismatches and investing cash held in the liquidity buffer
- Assigning a 10% RSF for Level 1 reverse repos effectively discourages prudent risk management – in that investing in reverse repos is an extremely low liquidity risk activity – and incentivizes Covered Companies to purchase Level 1 HQLA outright on account of the lower 5% RSF even though this practice is more risky from both a liquidity and interest rate risk perspective

Figure 5. Reverse Repo RSF vs. Trading Inventory RSF

NSFR RSF	Level 1 HQLA	Level 2A Corporate Bond	Level 2B Equity	Financial Equity
Reverse Repo RSF	10	15	15	15
Holding asset outright RSF	5	15	50	85

Figure 5. Reverse repo and securities borrowing by bank, 2014 vs. 2013 balance sheet (USD bn)



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2.3 Repo book asymmetry (2/2)

As proposed, the NSFR would significantly reduce repo activity particularly for US Treasuries, which would reduce market liquidity and increase US Treasury yields

Recommendation

- Reduce the asymmetry for reverse repos secured by Level 1 HQLA, as these assets already provide stable funding and the punitive treatment for reverse repos compared to outright holdings of Level 1 HQLA contradicts prudent liquidity risk management practices

Potential impacts

- As the repo business is high volume and low margin, the additional costs of the proposed rule, particularly for the repo of US Treasuries, would alter the economics of the business and cause a further reduction in capacity that has already been driven down by the leverage ratio and other regulatory reform initiatives
- The repo market is important for overall market liquidity. The ability to finance assets and exchange cash for collateral influences the cash traders' capacity to enter and exit trades at or near the last traded price. Anything that inhibits the smooth functioning of the repo market lowers cash market liquidity. Figure 5 shows the reduction in reverse repo and securities borrowing by banks

Options to achieve NSFR compliance

- Raise term unsecured cash and hold it as an "NSFR buffer" – this would impact leverage balance sheet and require a reduction of other financial intermediation activities
- Term out the repo funding for greater than 6 months – but less than 10% of repo and reverse repo transactions in the market are greater than 3 months*
- Reduce activity – the most likely approach given the leverage and market liquidity constraints

*Source: ICMA European Repo Market Survey #30

2.4 Short sales (1/2)

Firm and client short sales are self-funding and therefore should not generate RSF

Key concerns

- For firm short sales, the proposed rule generates an RSF requirement at 10-15% of the notional and 0% ASF recognition despite the self-funding nature of the transaction (short sale proceeds are used to borrow securities and securities borrowed* are returned upon closure of transactions with no gap in funding created).
- Similarly, for client short sales the Covered Company would receive a 10-15% RSF when borrowing the security to settle the transaction despite the transaction being fully funded by cash provided by the client from the initial short sale
- To support the RSF, Covered Companies would need to raise additional long-term funding; as no liquidity is required by these transactions, the cash raised would serve no prudential purpose in relation to the transactions that require it

Recommendations

- Assign an RSF of 0% to reverse repo and securities borrowing transactions covering firm and customer short sales where no funding requirements are generated
- Assign a 0% RSF to cash collateral provided to securities lenders for purposes of covering client shorts

Potential impacts

- Increased costs would reduce the volume of firm and client shorting, resulting in less efficient markets and greater price volatility

Options to achieve NSFR compliance

- In order to support the stable funding requirement for this activity, a Covered Company would need to raise long-term funding. As no liquidity is required by these transactions, the cash raised would increase leverage balance sheet which – for leverage constrained banks - would need accommodating through reductions elsewhere. This would either require reducing the amount of short covering on behalf of clients or exiting the business entirely, with the knock on-effect on market liquidity

*Defined as an open maturity securities borrow / reverse repo where both legs are unwound together

2.4 Short sales (2/2)

Short sale example

Figure 6. Firm short sale transaction

Typical firm short transaction

- Step 1: Covered Company short sells a security and the cash proceeds are a liability on the Covered Company's balance sheet
- Step 2: Covered Company uses cash sourced from the short sale proceeds to reverse repo or borrow the security from a securities lender, which is recorded as an asset on the Covered Company's balance sheet
- Step 3: The securities lender provides the Covered Company with the security, typically on an open basis under which the security is callable by the lender
- Step 4: Covered Company settles the short sale transaction in the market with the borrowed security

Typical client short transaction

- Client short facilitation includes security borrows or reverse repos where the underlying security is subsequently re-hypothecated to cover a client short sale

Both transactions are effectively self funded and should require no stable funding over a 1 year horizon

2.5 Extended settlements and trade date receivable fails

Extended settlements for new debt issuance is common practice driven by issuer timing needs rather than representative of instability or risk of non-payment

Key concerns

- The proposed rule would assign a 100% RSF factor to inflows of cash expected to be received on a greater than T+5 settlement basis and to certain trade date receivables that fail to settle within the standard period
- Extended settlements beyond T+5 are common in SEC-registered debt securities offerings (particularly "private label" mortgage-backed and asset-backed securities) and debt securities offerings (particularly for high yield securities and, to a more limited extent, in the investment grade context)
- Extension of settlement in the new issue context is generally not due to an inability or unwillingness to pay on the part of investors, but, rather, is overwhelmingly driven by issuers' business needs, such as favorable market conditions and time to execute (e.g., assembling various types or large numbers of assets, establishes tranches, rating agency review, diverse set of investors, cash movements)
- Approximately 20% of new issue deals settle beyond T+5, which is regular-way under GAAP for this type of transaction; normal market fail practice assumes some percentage of fails on settlement day that then complete over the following few days
- For high yield corporate bonds the issuer is often coordinating the refinancing of a loan or accommodating another corporate finance transaction which can lead to an extended settlement period. Additionally, issuers of all types often require extended settlement if they are refinancing a tender for their outstanding securities to avoid "negative carry" during the period required by the US securities laws for a tender offer to remain open
- Trade date receivable fails create minimal liquidity risk over the long term, are typically offset by trade date payable fails, and are usually not funded unsecured. Counterparties are incentivized to resolve fails quickly due to the risk of buy-ins and the cost of fines (e.g., Treasury Markets Practices Group fails charge)

Recommendations

- Assign a 0% RSF factor for the duration of primary offering settlements to recognize that these types of common extended settlements are the result of issuer timing needs rather than representative of instability or risk
- Assign a 0% RSF factor to trade date receivables that fail to settle within the standard settlement period but that are still expected to settle, in accordance with the weighting assigned in the Basel NSFR Framework

Potential impacts

- Extended settlement receivables are currently included in risk-based capital requirements; adding an additional long-term funding requirement to the reduction in ASF through the existing capital charge would further penalize such transactions where no commensurate liquidity risk exists

2.6 Collateral substitution (1/2)

The proposed rule fails to recognize the liquidity risk management value of funding trades where the Covered Company has rights of substitution

Key concerns

- Covered Companies are required to apply a 10% - 15% RSF on all reverse repos with financial institutions irrespective of the purpose of the transaction, such as the transaction in Figure 7
- The proposed rule fails to recognize the liquidity value of funding trades where the Covered Company has rights of substitution, and in certain instances, it penalizes Covered Companies by requiring them to hold RSF on assets collateralizing the trades
- The encumbrance provisions of the Proposed Rule would require a Covered Company to apply a higher RSF on assets allocated to term trades (> six months) to match the ASF of the repo liability. For example, if a Covered Company raises one-year term corporate bond repo and the trade is collateralized with Treasury bonds reversed in, the encumbrance provision would require the Covered Company to apply a 100% RSF on the Treasury reverse repo to correspond to the 100% ASF on the one-year term repo. Applying the Proposed Rule at the security level does not recognize or provide benefit for the overfunding (Figure 8)
- Tri-party agents allocate collateral using proprietary algorithms that were not designed to optimize NSFR: two Covered Companies with similar liquidity profiles may have different NSFR outcomes depending on the collateral allocation utilized by the agent. Similarly, a Covered Company's NSFR requirement may change from day to day even though its liquidity profile is unchanged

Recommendations

- Exclude Level 1 Assets reversed in and pledged to tri-party repo trades executed to fund Level 2B and Non-HQLA Assets from the RSF calculation
- Revise the treatment of tri-party trades where the Covered Company has the operational and legal capability to exercise substitution rights such that the encumbrance provision is applied to the asset class and not to a specific security allocated to the repo trade; the Covered Company should be able to use the 100% ASF on term repo trades with substitution to offset RSF requirements on like or other securities eligible as per the lender collateral profile

2.6 Collateral substitution (2/2)

Collateral substitution examples

Figure 7. Treasury bond reserve repo to fill Corporate tri-party repo trade

Current

Liability	B/S Amount	ASF%	ASF$
1) Corporate triparty repo trade with one month to maturity (allocated Treasury bonds)	$ 100	0%	$ -

Asset	B/S Amount	RSF%	RSF$
2) Overnight Treasury bond Reverse Repo	$ 100	10%	$10

Net $10 RSF

Proposed

Liability	B/S Amount	ASF%	ASF$
1) Corporate triparty repo trade with one month to maturity (allocated Treasury bonds)	$ 100	0%	$ -

Asset	B/S Amount	RSF%	RSF$
2) Overnight Treasury bond Reverse Repo	$ 100	10%	$10

Collateral Substitution		
Yes/No?	RSF%	RSF$
Yes	0%	$ -

Net NSFR Neutual
$0 ASF = $0 RSF

Figure 8. Tri-party collateral allocation

Allocation #1

Liability	B/S Amount	ASF%	ASF$
1) Term corporate tri-party repo trade with one year remaining maturity (allocated Bond A)	$ 100	100%	$ 100
2) Overnight corporate tri-party repo trade (Bond B)	$ 100	0%	$ -

Total ASF $ 100

Asset	B/S Amount	RSF%	RSF$	Encumbrance RSF: Encumbered?	Encumbrance RSF: RSF%	Encumbrance RSF: RSF$
4) Long Inventory (HY Corporates Bond A)	$ 100	85%	$ 85	Yes	100%	$ 100
3) Overnight HY Corporates Reverse Repo (Bond B)	$ 100	15%	$ 15	Yes	15%	$ 15

Total RSF $ 115

Net $15 RSF
($100 AFS; $115 RSF)

Allocation #2

Liability	B/S Amount	ASF%	ASF$
1) Term corporate tri-party repo trade with one year remaining maturity (allocated Bond B)	$ 100	100%	$ 100
2) Overnight corporate tri-party repo trade (allocated Bond A)	$ 100	0%	$ -

Total ASF $ 100

Asset	B/S Amount	RSF%	RSF$	Encumbrance RSF: Encumbered?	Encumbrance RSF: RSF%	Encumbrance RSF: RSF$
3) Overnight HY Corporate Reverse Repo (Bond B)	$ 100	15%	$ 15	Yes	100%	$ 100
4) Long Inventory (HY Corporates Bond A)	$ 100	85%	$ 85	Yes	85%	$ 85

Total RSF $ 185

Net $85 RSF
($100 AFS; $185 RSF)

- Tri-party repo can be terminated as necessary leaving excess funding in place over the long term

- RSF increases from 15% to 100% due to encumbrance even though asset can be substituted for an asset to which a lower RSF factor would be assigned

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2.7 Off-balance sheet collateral swaps

The treatment of off-balance sheet collateral swaps breaks with the Basel Framework and creates significant operational challenges

Key concerns

- The proposed rule introduces additional RSF requirements for these transactions under Sections 102(c) and 106(d) when the off-balance sheet asset received under a lending transaction, asset exchange, or other means, is re-hypothecated to secure an NSFR liability or to settle a short sale
- Under such circumstances, an RSF factor is assigned as if the asset reported on the balance sheet were encumbered for the longer of the remaining maturity of the NSFR liability or any other encumbrance applicable to the provided asset under the terms of the off-balance sheet collateral swap
- In contrast, the Basel NSFR Framework explicitly excluded collateral swaps if the "securities do not appear on the balance sheet"
- We believe that Agencies have underestimated the impact of this departure from the Basel NSFR Framework, which would add burdensome, detailed reporting requirements to NSFR calculation

Recommendations

- Collaborate with the industry to assess the operational impacts associated with capturing the requisite data for off-balance sheet activity as we believe it would require a material change and be challenging to implement
- Provide clear and precise guidance on the specific off-balance sheet activities intended to be captured, as these sections of the proposed rule are a departure from the Basel NSFR Framework and have resulted in inconsistent interpretations within the industry

Potential Impact

- We believe the operational and systems requirements necessary to track collateral movements in this manner (i.e., linking sources and uses of off-balance sheet assets and liabilities to on-balance sheet assets and liabilities) for the sole purpose of identifying encumbrance would be challenging given the velocity and size of collateral movements and dependency on third parties such as tri-party custodians