



August 8, 2017

By electronic submission

regs.comments@federalreserve.gov

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Amendments to the Capital Assessments and Stress Testing Information Collection (FR Y-14A/Q/M; OMB Control No. 7100-0341) June 9, 2017.

Ladies and Gentlemen:

HSBC North America Holdings Inc. (“HNAH”) appreciates the opportunity to comment on the proposed amendments by the Board of Governors of the Federal Reserve System (the “Board”) to revise the FR Y-14A/Q/M reports applicable to bank holding companies (“BHCs”) with total consolidated assets of \$50 billion or more and U.S. intermediate holding companies (“IHCs”) established by foreign banking organizations (“FBOs”).¹ The proposal expands the applicability of the global market shock (“GMS”) to certain IHCs, including HNAH. Newly covered firms would be required to submit certain FR Y-14Q trading and counterparty forms effective as of September 30, 2017 and to incorporate the GMS scenario into the 2018 Comprehensive Capital Analysis and Review (“CCAR”) submission.

EXECUTIVE SUMMARY

HNAH supports the efforts U.S. banking agencies have made to strengthen regulatory capital requirements, improve the quality and amount of capital in the banking system and implement capital planning programs such as stress testing. Recently the Board has recognized that, nearly seven years since the approval of the Dodd-Frank Act, it is time to reassess the effectiveness and appropriateness of these regulations as well as ensure greater transparency around the supervision process. We support Governor Powell’s view that the Board “should continue to tailor our requirements to the size, risk and complexity of the firms subject to those requirements” and that “we should assess whether we can adjust regulation in common-sense ways that will simplify rules and reduce unnecessary burden without compromising safety and soundness.”² Further, we are encouraged by Chair Yellen’s comment that the Board “strives for

¹ Volume 82 Federal Register. 26793 (June 9, 2017).

² Governor Jerome H. Powell, Testimony on the Relationship between Regulation and Economic Growth, Senate Committee on Banking, Housing and Urban Affairs (June 22, 2017).

transparency in our supervision and regulation of financial institutions” and “will continue to seek ways to ensure that the CCAR and stress testing programs remain effective, but not overly burdensome.”³

Our understanding is that the GMS is a component of the supervisory stress testing process, applicable to firms with “significant trading operations” designed specially “to assess potential losses stemming from trading books, private equity positions, and counterparty exposures.”⁴ Currently firms with total consolidated assets greater than \$500 billion are subject to the GMS.⁵ The Board has proposed changing this threshold such that the GMS would apply to any IHC or BHC with either aggregate trading assets and liabilities of \$50 billion or more or aggregate trading assets and liabilities equal to 10% or more of total consolidated assets.⁶

While we understand the importance of the GMS requirements for firms with significant trading operations, we have the following concerns with the current proposal:

1. The proposal significantly reduces the current thresholds for GMS and, consequently, subjects firms with much smaller trading activities to the same requirements as the six BHCs currently required to incorporate the GMS component. While the proposed amendments will impose substantial new regulatory costs on firms newly covered by GMS, we believe the proposal falls short in providing a transparent rationale for lowering the thresholds and applying the same requirements for firms with significantly smaller trading operations. We support the recommendations made by the Institute for International Bankers (“IIB”) and The Clearing House (“TCH”) not to adopt the proposed changes at this time. More transparent and careful consideration on the appropriate thresholds is needed. See Recommendation One below.
2. The proposed GMS thresholds are not risk-based. This could result in capturing firms that may breach an absolute threshold despite having relatively low levels of traded risk in their portfolios. As discussed above, we recommend the Board conduct further analysis and review of these thresholds. Specifically, we recommend that U.S. Treasuries be excluded from the final threshold given the low risk of these securities. See Recommendation Two below.
3. The proposal does not sufficiently tailor FR Y-14Q trading and counterparty reporting requirements for GMS firms by considering the relative size and complexity of firms’ trading books. We recommend the Board consider simplified schedules for firms with smaller trading operations. We set out below three ways in which the Board could tailor the FR Y-14Q forms to reduce the regulatory burden for firms with smaller trading operations. See Recommendation Three below.
4. To implement GMS requirements as set out in the proposal, firms will need to invest significant resources and time. We are concerned with the short timeframes outlined in the proposal given the substantial resources required, for instance, to extract data, program validation and edit checks, implement significant IT system changes, develop and validate models, and produce the

³ Letter, dated June 16, 2017, from Chair Yellen to Hon. Blaine Luetkemeyer, Chairman, House Subcommittee on Financial Institutions and Consumer Credit.

⁴ CCAR 2017 Summary Instructions for LISCC and Large and Complex Firms.

⁵ These firms are J.P. Morgan, Goldman Sachs, Citigroup, Morgan Stanley, Bank of America and Wells Fargo.

⁶ Large and noncomplex firms would not be subject to the GMS under the current proposal.

documentation required. Should the Board proceed with adopting the GMS requirements currently set out in the proposal, we would recommend establishing a phased approach to provide firms with sufficient time to implement the large-scale programs needed to meet the GMS requirements. See Recommendation Four below.

RECOMMENDATION ONE: THE BOARD SHOULD NOT ADOPT THE GMS REQUIREMENTS WITHOUT A MORE TRANSPARENT REVIEW OF THE APPROPRIATE GMS THRESHOLDS

As noted above, we are pleased with the recent comments that the Board is committed to a transparent regulatory process. We would suggest, however, that the GMS proposal lacks adequate transparency on the rationale for calibration of the thresholds, in particular given that this is a significant change from the current rules. It is not clear, for example, what analysis was conducted to assess the costs and benefits of lowering the thresholds to the proposed levels. These are complex requirements with potential unintended consequences that need to be carefully assessed.

We therefore concur with industry trade groups and respectfully request that the Board not adopt the proposed changes to the GMS thresholds at this time. Instead, we would welcome further review and analysis on the appropriate calibration of the GMS thresholds. In particular, we strongly support the IIB's proposal that additional analysis and support should be taken through a more thorough notice-and-comment procedure on a proposed rulemaking. This will help ensure that the costs and benefits of this substantive change are subject to an open and transparent debate.

RECOMMENDATION TWO: THE BOARD SHOULD ADOPT A MORE RISK-BASED THRESHOLD THAT EXCLUDES U.S. TREASURIES

The Board states that applying the GMS to certain U.S. IHCs “would help the Board more accurately identify the firms’ risks and capital needs” and “result in a more comparable treatment to large domestic bank holding companies with similar exposures and business models.”⁷ Thresholds that determine whether a firm is subject to GMS should, in principle, be based on the amount of risk firms have in their trading operations. We would argue that the proposed thresholds, which are based solely on accounting balances for traded assets and liabilities, serve as an imperfect proxy for the risk on firms’ balance sheets. In particular, firms that are primary dealers with sizable market-making activities in U.S. Treasuries may have high trading balances but low traded risk.

We recommend that the Board, at a minimum, exclude U.S. Treasuries in the final determination of the GMS reporting thresholds. This would provide a more risk-based metric and could be implemented as follows:

- Each quarter, firms would calculate their trailing four-quarter average aggregate trading assets and liabilities excluding U.S. Treasuries and populate these figures in the relevant FR Y-14Q forms.
- If the thresholds are breached, the Board would automatically be notified, and firms would be required to populate the relevant FR Y-14A and FR Y-14Q forms.

⁷ Volume 82 Federal Register. 26793 (June 9, 2017).

RECOMMENDATION THREE: THE BOARD SHOULD TAILOR THE GMS REPORTING REQUIREMENTS TO ACCOUNT FOR DIFFERENCES IN THE SIZE AND COMPLEXITY OF FIRMS' TRADING OPERATIONS

The current proposal does not sufficiently tailor the reporting requirements for GMS firms and will impose undue regulatory burden on firms with relatively smaller and simpler trading operations without an incremental benefit from a regulatory perspective. For example, GMS firms – irrespective of size or complexity – would need to complete the same extensive FR Y-14Q traded risk and counterparty credit risk schedules and undergo the same level of analysis and documentation for calculating the GMS losses used in the CCAR exercise. Even where firms have immaterial risk positions, the current proposal would still require firms to implement substantial IT change programs to populate the forms in the format the Board is requesting, imposing further regulatory compliance costs. For firms with relatively low traded risk, the costs to implement and maintain the GMS requirements seem disproportionate to the benefits the Board would receive in gathering this level of detailed data from these firms.

To move to a more tailored approach, we recommend that the Board review options for reducing the complexity and intensity of the FR Y-14Q schedules for firms that meet the GMS threshold but that may have significantly smaller and simpler trading operations than the existing GMS firms. There are three main dimensions we see for tailoring the FR Y-14Q schedules.

1. Instead of setting one threshold for GMS that leaves firms, irrespective of size or complexity, with the same regulatory burden, a second threshold could be established to delineate between those firms with the largest trading operations and firms with significantly lower traded risk. For instance, firms that breach the first but not the second GMS threshold could be required to populate a subset of the 156 traded and counterparty credit risk worksheets based on the Board's assessment of which of these worksheets are most important for the Board to conduct a robust stress of the firm's trading positions.
2. Firms with smaller trading operations (with thresholds determined as described in the first point above) could be allowed to submit the FR Y-14Q forms on an annual rather than quarterly basis as part of each CCAR submission, with the submission being limited to providing only the P&L impacts based on the specified risk-factor shocks from the annual GMS scenario rather than the full range of shocks currently required by the forms. These impacts would be based on the specified as-of date for the traded risk scenario that the Board provides with the publication of the annual CCAR scenarios.
3. For each worksheet within a FR Y-14 Q form, minimum thresholds could be set, below which firms would only need to populate certain fields within the worksheet. For example, in the "Equity by Geography" worksheet, firms could first be required to populate the delta and gamma fields at in the aggregate geography rows (e.g. advanced economies, emerging Europe, etc). If these fields were below a pre-determined threshold indicating low risk in equity positions, then the firm would not be required to populate other parts of the worksheet such as the vega-by-tenor fields.

RECOMMENDATION FOUR: THE BOARD SHOULD PROVIDE NEWLY COVERED FIRMS WITH A SUITABLE TRANSITION PERIOD TO ENSURE A LEVEL-PLAYING FIELD

The current proposal would require firms to submit a significant number of FR Y-14Q trading and counterparty forms and worksheets for the as-of date of September 30, 2017 and to incorporate all of the GMS requirements for both the BHC and FRB scenarios in the 2018 CCAR exercise. We respectfully submit that the current proposal provides an unrealistic timeframe for firms to resource and implement the substantial requirements imposed by GMS, in particular for those firms that may have only been made aware of being subject to the GMS when the proposal was released in June. The GMS requirements are extensive. For example:

- The FR Y14-A/Q trading and counterparty schedules are lengthy and complex. Overall, there are 156 pages of worksheet schedules and 70 pages of instructions. Significant time and resources will be needed to conduct a detailed review of these schedules, evaluate the requirements for each field in each worksheet and implement large-scale system changes to calculate the fields and ensure robust validation and reconciliation procedures are in place.
- While not explicitly mentioned in the proposal, the Board requires significant supporting documentation to be submitted alongside the FR Y-14 schedules. Industry experts have indicated that the current GMS firms typically submit tens of thousands of pages in supporting documentation for the trading and counterparty schedules. The Board should ensure newly covered firms have sufficient time to build these capabilities.
- New models will need to be developed and put through robust independent validation procedures.
- The Board itself estimates that the “annual reporting burden associated with the addition of the five U.S. IHCs to the global market shock is estimated at 9,736 hours per firm.” Clearly, the resources required for the actual implementation of GMS will be multiples of these estimated ongoing resource requirements.

We are committed to meeting supervisory expectations and ensuring that regulatory filings are accurate and complete. Given the large-scale changes firms will have to implement to meet these new regulatory requirements, we recommend the Board provide firms with a suitable transition period through a phased approach as follows:

- FR Y-14Q requirements should be delayed by one year from the date specified in the current proposal such that firms would commence reporting based on their balance sheet as-of September 30, 2018. This would also provide the Board with more time to conduct analysis on the thresholds and develop options for tailoring the requirement (as discussed in the first three recommendations set out in this letter). In the interim, firms would informally submit FR Y-14Q schedules to facilitate feedback from the Board and allow Board staff to analyze the data to further their understanding of the risks inherent in a firm’s trading portfolio. This would provide firms with more realistic timeframes to implement the system changes for regulatory reporting.

- Firms should not be subject to the GMS component of the stress test until the 2019 CCAR cycle. We concur with both the IIB and The Clearing House who recommend that the Board should not include the GMS component for any covered IHCs in either the formal quantitative or qualitative assessment for the CCAR 2018 exercise.

We would emphasize that the June 9, 2017 proposal was the first indication that HNAH received that we would be subject to the GMS component of the stress test.

CONCLUSION

HNAH appreciates the opportunity to comment on the proposal and your consideration of our recommendations. Respectfully, we submit that the Board not adopt the proposal at this time. Additional analysis should be conducted, which should then be taken through a more thorough notice-and-comment procedure on a proposed rulemaking. If the Board determines to apply the global market shock requirements, we would encourage the Board to consider our other recommendations to make the threshold more risk based, tailor the FR Y14 forms based on the size of firms trading operations and ensure an appropriate transition period, which would allow the newly covered GMS firms sufficient time to implement this substantial change in requirements.

We would be pleased to provide further information or assistance to the Board or its staff.

Please address any questions related to this comment letter to the undersigned or Jacques Herman, Head of the Regulatory Liaison Office, at 212-525-6012.

Yours sincerely,



Gerard Mattia
Chief Financial Officer
HSBC North America Holdings, Inc.



Rhydian Cox
Chief Risk Officer
HSBC North America Holdings, Inc.