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Via Electronic Delivery

Board of Governors of the Federal Reserve System
20th Street & Constitution Ave., NW.
Washington, DC 20551

Re: Proposed Capital Planning and Stress Testing Amendments
Docket No. R–1548; RIN 7100 AE–59

Ladies and Gentlemen:

American Express Company ("American Express") appreciates the opportunity to provide comments to the Board of Governors of the Federal Reserve System (the "Federal Reserve") in response to the Federal Reserve's proposed rule to revise its capital planning and stress test rules for bank holding companies ("BHCs") with $50 billion or more in total consolidated assets and U.S. intermediate holding companies of foreign banks (the "Proposed Rule"). [1]

Among other adjustments, the Proposed Rule would provide limited relief for a subset of firms currently subject to the Federal Reserve's capital planning rules. Under the Proposed Rule, BHCs defined as "large and noncomplex" firms would no longer be subject to the qualitative assessment portion of the Comprehensive Capital Analysis and Review ("CCAR") process.[2] Accordingly, these firms would no longer be subject to the provisions of the capital planning rules whereby the Federal Reserve may object to a capital plan on the basis of qualitative deficiencies in the firm's capital planning process.

American Express strongly supports the efforts of the Federal Reserve to tailor the application of the capital planning and stress testing rules. However, as described in

1 Amendments to the Capital Plan and Stress Test Rules, 81 Fed. Reg. 67239 (Sept. 30, 2016).

2 The qualitative assessment of the capital plans of "large and noncomplex" firms instead would be conducted outside of CCAR through the supervisory review process. These firms would, however, remain subject to the quantitative assessment in CCAR.

greater detail below, American Express believes that it is neither statutorily required nor appropriate as a supervisory matter for the Federal Reserve to define the term "large and noncomplex" for purposes of the U.S capital planning process using a series of static, outdated, and non-risk-sensitive thresholds.

These thresholds do not appropriately reflect the complexity, business models, international activity or actual risk profiles of banking organizations. Further, two of these thresholds were developed approximately 13 years ago in a separate context to segment the U.S. banking industry for different purposes. Accordingly, we respectfully request that the Federal Reserve re-evaluate the use of these thresholds for purposes of identifying "large and noncomplex" firms. American Express believes that the use of alternative measures, such as the systemic indicator approach used to identify global systemically important banks ("G-SIBs"), would ensure that the scope of relief proposed by the Federal Reserve is and remains properly calibrated to achieve its purpose of tailoring expectations for firms with a lower systemic risk profile.

I. The Use of Static, Outdated, and Non-Risk-Sensitive Thresholds Results in an Inappropriate Segmentation of the Industry that is Inconsistent with the Purposes of the Proposed Rule

The Proposed Rule is intended to further the objective of the Federal Reserve to tailor supervisory expectations for firms with a lower systemic risk profile, while simultaneously protecting financial stability and improving the resiliency of and the availability of credit from the largest and most complex firms.[3] In particular, the Proposed Rule reflects the concern of the Federal Reserve that the public profile of the CCAR qualitative review could encourage large and noncomplex firms to over-invest in stress testing and capital planning processes that are unnecessary to adequately capture the risks of these firms.[4] American Express strongly agrees with these objectives. However, the Federal Reserve has proposed using thresholds that do not properly identify "large and noncomplex" firms and which, accordingly, are not consistent with the stated purposes of the Proposed Rule.

The Proposed Rule sets out three static thresholds for identifying a "large and noncomplex" firm. As proposed, a BHC or U.S. intermediate holding company with (i) total consolidated assets of $50 billion or greater but less than $250 billion; (ii) on-balance sheet foreign exposure of less than $10 billion; and (iii) nonbank assets of less than $75 billion would be considered a "large and noncomplex" firm. A BHC exceeding any of these thresholds would not be eligible for relief under the proposed rule.

Two of these thresholds are not new. The Federal Reserve has increasingly relied upon the threshold levels of $250 billion in total consolidated assets or $10 billion in foreign exposure to segment the industry in a number of supervisory contexts (the "250/10 Thresholds"). However, there is no statutory requirement or regulatory imperative that necessitates using the 250/10 Thresholds for CCAR purposes, and we do

3 81 Fed. Reg. at 67241.

4 Id.

not believe it is appropriate or consistent with the policy goals of the Proposed Rule to do so here.

The 250/10 Thresholds are static, arbitrary measures that are unique to the United States and were developed in 2003 – prior to the 2008-09 Financial Crisis – to identify those "internationally active" banking organizations to which the U.S. Advanced Approaches capital rules would apply. Post-crisis, the Basel Committee on Banking Supervision (the "Basel Committee") and the Federal Reserve have developed a far-more comprehensive measure for size, complexity, and overall systemic risk of individual banks. The expanding use of the pre-crisis 250/10 Thresholds, when more sophisticated, comprehensive, and internationally recognized tools are available, is inappropriate.

At the time the thresholds were first established, the Federal Reserve made clear that the implementation in the United States of standards for "internationally active" banking organizations was intended to reach only the "largest, most complex banks," i.e., those that were the "most complex banking institutions" and were truly "internationally active."[5] These thresholds may have been an appropriate proxy at the time for identifying a group seemingly equivalent to today's G-SIBs, but were not developed for application of the CCAR or other domestic U.S. supervisory initiatives. However, the 250/10 Thresholds are increasingly being used by the Federal Reserve in other contexts unrelated to the work of the Basel Committee or the definition of "internationally active." Unfortunately, because they are static, outdated, and not risk sensitive, these thresholds now capture certain regional and other traditional banking organizations that, due to their business models and limited risk profiles, do not warrant application of the same rules that apply to the "most complex banking institutions," such as the U.S. G-SIBs.

Segmenting the U.S. financial services industry in this manner causes the inappropriate imposition of unnecessary regulatory requirements on institutions outside of the group of G-SIBs solely because they have crossed one or more arbitrary thresholds. This results in incongruent groupings of banking organizations that are not aligned with business models or corresponding risk profiles. However, vast differences exist between the firm-specific business models and systemic risk profiles of traditional banking organizations and the G-SIBs. As a result of the 250/10 Thresholds not taking into account these differences, regulatory requirements such as the proposed CCAR relief are not being appropriately calibrated to the risk profile of institutions and unnecessary regulatory obligations and supervisory expectations are being imposed on traditional banking organizations.

In addition to the 250/10 Thresholds, the Proposed Rule also includes a new threshold that is based upon a banking organization's "nonbanking" assets. According to the preamble accompanying the Proposed Rule, this additional threshold is similarly

5 Testimony of Vice Chairman Roger W. Ferguson, Jr., Basel II, Before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, June 18, 2003, available at http://www.federalreserve.gov/boarddocs/testimony/2003/20030618/default.htm; see also Federal Reserve, Capital Standards for Banks: The Evolving Basel Accord, 89 Fed. Res. Bull. 395 (Sept. 2003).

intended to "include large firms with complex capital markets activities, but . . . not include firms with less complex structures or activities."[6] However, in creating this new threshold the Federal Reserve has simply proposed an additional arbitrary static threshold that substitutes a crude balance sheet measurement of assets for a factual analysis of banking organizations' business models and actual risks. As discussed below, the Basel Committee and the Federal Reserve have already developed far more sophisticated analytical tools for assessing complexity. As such, we believe it is not appropriate to introduce a third static threshold that is neither risk sensitive nor otherwise tailored to the purposes of the Proposed Rule.

It is important to note that the 250/10 Thresholds currently capture banking organizations with significantly divergent characteristics. Two distinct groups – the largest and most complex banking organizations, as well as regional and other traditional banking organizations – are both captured under this same 250/10 Threshold. However, there is a wide gulf between these two groups, especially in terms of business model and risk profile. For example:

• Relative to larger and more complex organizations (such as the U.S. G-SIBs), traditional banking organizations have relatively simple organizational structures, primarily focusing on traditional retail and commercial banking products and services, and have only limited trading and capital markets operations. Broker-dealers and other nonbank operations outside of service-providing affiliates comprise only a small portion of their overall operations.

• Traditional banking organizations' exposure to capital markets and derivatives activities pale in comparison to that of U.S. G-SIBs.

Accordingly, and as discussed further below, we believe the 250/10 Thresholds should be revised in a manner that ensures appropriate calibration of regulatory requirements based on banking organizations' business models and actual risk profile. Notably, revisiting the 250/10 Thresholds, and their application to regional and other traditional banking organizations, would be consistent with recent Congressional direction included in the House Committee on Appropriation's report accompanying the 2016 Financial Services and General Government Appropriations Bill, which was incorporated into the 2016 Consolidated Appropriations Act enacted in December 2015, which provides:

> Basel Standards.—The Committee is concerned that the U.S. prudential regulators have inappropriately applied several standards developed by the Basel Committee on Bank[ing] Supervision (Basel), which are explicitly designed for only the most internationally active, globally systemic, and highly complex banking organizations to less complex organizations, like regional banking organizations, which have only limited foreign exposure and do not pose a threat to the U.S. or global financial system. The Committee encourages Treasury and other prudential

[6] 81 Fed. Reg. at 67243.

regulators to reexamine the impact of certain liquidity and capital standards as they apply to U.S. regional banks and other less complex organizations.[7]

Fundamentally, static balance-sheet-based thresholds are a poor proxy for risk or complexity, and the Federal Reserve has far better and more sophisticated tools at its disposal. As discussed below, we believe an appropriate alternative approach would be to replace the thresholds in the Proposed Rule with a more sophisticated, dynamic measure that would ensure that the scope of the rule remains properly calibrated to capture the largest and most complex global banking organizations, such as the systemic indicator approach used to identify G-SIBs.

II. More Sophisticated Methods Exist to Calibrate Regulatory Requirements

The international regulatory community and the U.S. federal banking agencies have developed more sophisticated, dynamic tools that we believe should be leveraged to better calibrate regulatory requirements based on the actual risk profile of banking organizations. Specifically, the U.S. banking agencies participated in the international development of the systemic indicator approach,[8] which the Federal Reserve has implemented in the United States for identifying G-SIBs.[9] The systemic indicator approach takes into account not only size, but also interconnectedness, substitutability, complexity, and cross-jurisdictional activity. Moreover, the systemic indicator approach is far more sensitive and dynamic than a thresholds-based approach because the comprehensive set of attributes that the systemic indicator approach takes into consideration, and the denominators that are used to evaluate those attributes, are updated periodically.[10] Such an approach would ensure more appropriate calibration of regulatory requirements based on banking organizations' business models and actual risk profile.

A cursory review of the systemic indicator approach quickly demonstrates that it provides much more powerful insights into complexity, international activities and the actual risk profile of a banking organization than the rudimentary asset- and on-balance sheet foreign exposure-based measures incorporated into the 250/10 Thresholds. The systemic indicator data also highlight the vast difference between traditional banking organizations and the largest, most complex banking organizations (such as the U.S. G-

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7 H.R. Rep. No. 114-194 (2015), at 10.

8 Basel Committee, Global systemically important banks: updated assessment methodology and the higher loss absorbency requirement (July 2013).

9 See Regulatory Capital Rules: Implementation of Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Final Rule, 80 Fed. Reg. 49,802 (Aug. 14, 2015).

10 The Federal Reserve's FR Y-15 Banking Organization Systemic Risk Report, which collects data comprising the five components underlying the systemic indicator approach (size, interconnectedness, substitutability, complexity, and cross-jurisdictional activity), is submitted by bank holding companies with total consolidated assets of $50 billion or more on a quarterly basis. The aggregate systemic indicators used as the denominators to calculate a banking organization's systemic indicator score are updated on an annual basis.

SIBs), and why continuing to deploy the 250/10 Thresholds is no longer appropriate. For example, based upon publicly available information:

• As for size, the eight U.S. banking organizations identified as G-SIBs account for 76% of total exposures for all U.S. bank holding companies required to submit the Federal Reserve's FR Y-15 Banking Organization Systemic Risk Report ("FR Y-15 Filers"),[11] and whereas the smallest non-custody G-SIB has total exposures of $1.28 trillion, the largest traditional banking organization has only $539 billion.

• With respect to the amount of over-the-counter ("OTC") derivatives, an important measure of complexity, U.S. G-SIBs account for 98% of the notional value of all OTC derivatives for all FR Y-15 Filers, and the smallest non-custody G-SIB has OTC derivatives with a notional value of $5.6 trillion, compared to the largest traditional banking organization, which has only $278 billion. Similarly, U.S. G-SIBs accounted for 87% of trading and available-for-sale securities (less high quality liquid assets) for all FR Y-15 Filers; the smallest non-custody G-SIB has $135 billion of such securities, compared to only $16 billion for the largest traditional banking organization.

• As for international activities, the U.S. G-SIBs account for 94% of all cross-jurisdictional claims and 95% of all cross-jurisdictional liabilities for FR Y-15 Filers, representing the vast majority of all international claims and liabilities for FR Y-15 Filers. No traditional banking organization has cross-jurisdictional claims or liabilities exceeding 1% of the aggregate amounts for FR Y-15 filers, consistent with the domestic focus and limited international activity of traditional banking organizations.

In addition to size, complexity and international activity, the remaining systemic indicators similarly demonstrate the vast gulf between U.S. G-SIBs and regional and traditional banking organizations. Perhaps more telling are the ultimate scores of systemic importance when calculated using the systemic indicator data. For example:

• Under the Federal Reserve's systemic indicator methodology a U.S. bank holding company is deemed to be a G-SIB if its systemic indicator score is 130 or more. Based upon public information, the G-SIB cutoff (130) is more than three times greater than the systemic indicator score of the largest non-custody U.S. banking organization that is not identified as a G-SIB (39); and

• The average systemic indicator score of the eight U.S. G-SIBs (280) is over seven times greater than that of the largest non-custody U.S. banking organization that is not G-SIB (39).[12]

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[11] All FR Y-15 data in this letter are as of December 31, 2014.

[12] Systemic indicator scores were calculated based on FR Y-15 reports as of December 31, 2014, and the Basel Committee's 2014 systemic indicator denominators (converted into U.S. Dollars based on the spot USD/EUR exchange rate prevailing on December 30, 2014). A report compiled by the Office of Financial Research ("OFR") draws similar conclusions using the Basel Committee's essentially identical methodology. See Allahrakha et al., Office of Financial Research Brief, Systemic Importance Indicators for 33 U.S. Bank Holding Companies: An Overview of Recent

The systemic indicators and score data make it clear that the U.S. G-SIBs are significantly more complex and internationally active than traditional and regional banking organizations.[13] In light of the stark differences between U.S. G-SIBs and regional and traditional banking organizations and the policy goals of the Proposed Rule, we believe that the systemic indicator approach should be applied instead of the 250/10 Thresholds in order to properly identify "large and noncomplex" firms for purposes of the Proposed Rule.

III. Conclusion

American Express respectfully submits that, for the reasons described above, the Federal Reserve should forego use of its proposed static thresholds in favor of relying upon the more tailored systemic indicator approach in identifying "large and noncomplex" firms. We believe that these changes would produce a definition of "large and noncomplex" that more appropriately captures the risk associated with covered organizations, asset classes, and liabilities, and thus would result in a supervisory focus that is better aligned to the objectives of the Federal Reserve.

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Data (Feb. 12, 2015), available at http://financialresearch.gov/briefs/files/2015-02-12-systemicimportance-indicators-for-us-bank-holding-companies.pdf.

13 More generally, we believe it is especially critical for the U.S. banking agencies to keep these very real differences between U.S. G-SIBs and regional and other traditional banking organizations in mind, particularly given the increasing use of the 250/10 Thresholds outside the context of the Basel Committee's standards.

Thank you for considering our comment letter. We appreciate the opportunity to share our views with the Federal Reserve and would be happy to discuss any of them further at your convenience. If we may be of further assistance, please contact me at 212-640-2396 or david.l.yowan@aexp.com.

Sincerely,

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