June 21, 2019

Via Electronic Mail

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
regs.comments@federalreserve.gov
Docket Nos. R-1628B & R-1658
RIN 7100-AF21 & AF45

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
comments@FDIC.gov
RIN 3064-AE96

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street, SW
Suite 3E-218
Washington, DC 20219
regs.comments@occ.treas.gov
Docket ID OCC-2019-0009
RIN 1557-AE63

Re: Proposals to Tailor the Regulatory Capital and Liquidity Requirements and Certain Enhanced Prudential Standards for Foreign Banking Organizations

Ladies and Gentlemen:

We appreciate the opportunity to comment on (i) the proposed rules issued jointly by the Board of Governors of the Federal Reserve System ("Federal Reserve"), the Office of the Comptroller of the Currency ("OCC") and the Federal Deposit Insurance Corporation ("FDIC") (collectively, the "Agencies") that would, among other things, revise the thresholds for applying certain aspects of the Agencies' regulatory capital and liquidity rules to foreign banking organizations ("FBOs") that have significant U.S. operations (the "FBO Interagency Proposal");[1] and (ii) the Federal Reserve's parallel proposal that would revise its enhanced prudential standards

[1] *Proposed changes to applicability thresholds for regulatory capital requirements for certain U.S. subsidiaries of foreign banking organizations and application of liquidity requirements to foreign banking organizations, certain U.S. depository institution holding companies, and certain depository institution subsidiaries*, 84 Fed. Reg. 24,296 (May 24, 2019).

regulations ("EPS") applicable to large FBOs (the "FBO EPS Proposal"[2] and, together with the FBO Interagency Proposal, the "FBO Proposals").

We applaud the Agencies' efforts to review and, consistent with the Economic Growth, Regulatory Relief and Consumer Protection Act ("EGRRCPA"), improve the tailoring of the post-crisis frameworks establishing regulatory capital standards, liquidity requirements and EPS. With respect to the specific questions posed by the Agencies in the FBO Proposals, we recommend the following:

- As noted in our comment letter in response to the domestic tailoring proposals[3] (the Domestic Proposals and the FBO Proposals are collectively referred to hereafter as the "Proposals"), we support the risk-based threshold approach currently included in the Proposals for classifying banking organizations, which we believe provides an appropriate and transparent methodology for these purposes. As discussed further below, we also believe that no additional risk-based indicators are necessary for the Category II boundary, as the existing asset and cross-jurisdictional activity indicators are sufficient to identify when an organization is "large" or "internationally active" and, thus, should be subject to the additional Basel-based standards applicable to such firms (such as, for example, the Advanced Approaches for determining risk-weighted assets and the "Full" Liquidity Coverage Ratio ("LCR")). If, however, the Agencies determine to include additional risk-based indicators for the Category II boundary, the threshold for such indicators should be set at no less than $210 billion and should be indexed to the growth of the U.S. banking industry.

- We support the proposal to simplify the definition of "highly liquid assets" ("HLA") under Regulation YY and more closely align the definition of HLA with the definition of "high quality liquid assets" ("HQLA") under the LCR rule. However, in order to maintain the intended and beneficial difference between the internal, company-designed stress tests conducted under Regulation YY and the standardized, regulatory-defined LCR, we believe that the standardized restrictions on HQLA under the LCR rule should *not* be super-imposed on company-run stress tests conducted under Regulation YY.

Our comments and recommendations are discussed in more detail below. We view these recommendations as distinct from the considerations in the Domestic Proposals. Therefore, we urge the Agencies to finalize the Domestic Proposals expeditiously and separately address these and other comments on the FBO Proposals.

---

[2] *Prudential Standards for Large Foreign Banking Organizations; Revisions to Proposed Prudential Standards for Large Domestic Bank Holding Companies and Savings and Loan Holding Companies*, 84 Fed. Reg. 21,988 (May 15, 2019).

[3] *Proposed Changes to Applicability Thresholds for Regulatory Capital and Liquidity Requirements*, 83 Fed. Reg. 66024 (Dec. 21, 2018) (hereinafter the "Domestic EPS Proposal"); *Prudential Standards for Large Bank Holding Companies and Savings and Loan Holding Companies*, 83 Fed. Reg. 61408 (Nov. 29, 2018) (hereinafter the "Domestic Interagency Proposal" and, collectively with the Domestic EPS Proposal the "Domestic Proposals").

I. Proposed Risk-Based Thresholds for the Application of Category II Standards

The FBO Proposals would generally divide FBOs into four categories based on the same asset and risk-based measures that would apply to U.S. banking organizations under the Domestic Proposals. As noted in our comment letter in response to the Domestic Proposals,[4] we believe the proposed risk-based threshold approach provides an appropriate and transparent methodology for classifying banking organizations for these purposes. The proposed risk-based measures and thresholds (if indexed) effectively distinguish among banking organizations based on risk and business model and result in more congruent groupings of banking organizations than the current regulatory capital, liquidity and EPS frameworks.

The FBO Proposals request comment on whether the Category II boundary should include indicators for weighted short-term wholesale funding ("wSTWF"), nonbank assets or off-balance sheet exposures, in addition to the originally proposed asset and cross-jurisdictional activity indicators. We do not believe that any additional risk-based indicators are necessary for the Category II boundary. As recognized by the Agencies in the Domestic Proposals, Category II is largely designed to identify those banking organizations that should be considered "large, internationally active" and, thus, subject to international standards developed by the Basel Committee on Banking Supervision ("Basel Committee"), such as the Advanced Approaches for determining risk-weighted assets and the "Full LCR."[5] As such, we believe the current $700 billion in total consolidated assets or $75 billion in cross-jurisdictional activity indicators are sufficient, as they identify banking organization that are "large" or "internationally active" and no additional indicators are necessary for the Category II boundary.

Should the Agencies nevertheless determine that wSTWF, nonbank asset or off-balance sheet exposures should be included as additional indicators for the Category II boundary, the level for such indicators should be set at no less than $210 billion to (i) maintain proportional parity between a firm's asset size and the risk-based indicators for the Category II and Category III boundaries; (ii) avoid potential negative implications for the availability of credit to businesses, consumers and local governments; and (iii) maintain the overall integrity of the categories of banking organizations proposed by the Agencies.

Under the Proposals, a Category IV organization would become a Category III organization once it has either (i) $250 billion in total consolidated assets or (ii) $75 billion in wSTWF, nonbank assets or off-balance sheet exposures. Thus, the total consolidated assets threshold for the Category II boundary ($700 billion) is 2.8x the total consolidated assets threshold for the Category III boundary ($250 billion).

If wSTWF, nonbank assets or off-balance sheet exposure indicators are to be included as part of the Category II boundary, this same multiple (2.8) should be used in adjusting the Category III

[4] *See* Letter from Capital One Financial Corporation, The PNC Financial Services Group, Inc, and U.S. Bancorp to the Agencies, dated January 22, 2019.

[5] Domestic Interagency Proposal, 83 Fed. Reg. 61,410 (Nov. 29, 2018) ("Like Category I, [Category II] would include standards that are based on standards developed by the [Basel Committee] and other standards appropriate to very large or internationally active banking organizations.").

$75 billion wSTWF, nonbank assets and off-balance sheet exposure thresholds for the Category II boundary. This would maintain the relative proportionality of the indicators to total assets constant between the Category III and Category II thresholds. For example, a banking organization with $700 billion in total consolidated assets and $210 billion in wSTWF would have the same ratio of wSTWF to total assets (2.8) as a firm with $250 billion in total consolidated assets and $75 billion in wSTWF. In other words, the *relative reliance* of the two firms on wSTWF would be the same. Accordingly, we believe any additional indicators included for the Category II boundary should be set at no less than $210 billion in order to maintain the relative relation between asset size and other risk-based indicators for Category II and Category III organizations.

Setting the threshold for additional Category II risk-based indicators at the lower end of the range proposed by the Agencies ($100 billion) could also impair the ability of Category III banking organizations, like the undersigned, to meet the credit needs of businesses, consumers and local governments. Our banking organizations are primarily engaged in traditional banking activities, including extending credit to middle market businesses, consumers and local governments. Our organizations have limited broker-dealer businesses and derivative exposures, especially relative to banking organizations that would be classified in Categories I and II. Indeed, the vast majority of our "off-balance sheet exposures" consist of traditional lines of credit extended to corporate customers and local governments, as well as lines of credit (such as home equity lines of credit and credit cards) to consumers. Setting the Category II boundary for off-balance sheet exposures at the lower end of the range suggested in the FBO Proposals could cause our organizations to, either now or in the future, carefully manage—and potentially reduce—the lines of credit we provide customers in order to remain below the Category II threshold.

In addition, setting the threshold for off-balance sheet exposures at the lower end of the proposed range would fundamentally alter the four categories of banking organizations initially proposed by the Agencies in the Domestic Proposals. Given that our organizations are engaged in traditional lending activities, a Category II threshold for off-balance sheet exposures set at the lower end of the proposed range would significantly increase the likelihood that a regional bank would cross the Category II threshold *even if its business model did not change*. Indeed, the U.S. globally systemically important banks (excluding the specialized custody banks) have an average ratio of off-balance sheet exposures to total assets of approximately 28%, with a significant percentage of these exposures composed of derivative exposures.[6] We see no reason why a regional bank should be forced into Category II at a lower ratio of off-balance sheet exposures to total assets, especially when the vast majority of regional bank off-balance sheet exposures arise from traditional lending commitments, rather than derivative exposures.

Finally, any risk-based indicators included for Category II should be indexed to the amount of total assets of commercial banks, as published periodically by the Federal Reserve on the H.8 Assets and Liabilities of Commercial Banks in the United States statistical release.[7] Indexing

---

[6] FR Y-15 data as of December 31, 2018.

[7] Federal Reserve, *Statistical Release H.8 - Assets and Liabilities of Commercial Banks in the United States*, *available at* https://www.federalreserve.gov/releases/h8/ (providing weekly aggregate balance sheet for a representative sample of commercial banks).

any additional risk-based indicators to the recommended measure is critical to ensuring that the relative relationship between the thresholds, the share of the banking industry represented by a particular banking organization and the banking industry overall is maintained through time. Absent a dynamic link between the risk-based thresholds and the U.S. banking industry as a whole, the thresholds will over time capture banking organizations that represent a smaller proportion of, and, therefore, a lesser degree of risk to, the industry and the broader economy. To enhance the transparency and certainty for covered banking organizations under the regulatory framework, any indexing should be codified as part of the Agencies' final rules to ensure that the thresholds are adjusted regularly and automatically.

II. Definition of "Highly Liquid Assets" under Regulation YY

The FBO EPS Proposal requests comment on whether assets that qualify as HLA for purposes of the Regulation YY liquidity buffer requirement should be more closely aligned with the definition of HQLA under the LCR rule. The existing internal, company-designed liquidity stress testing requirements under Regulation YY and the standardized, regulatory-designed LCR rule together create a robust and complementary liquidity stress testing and risk measurement framework. These two liquidity requirements serve two different purposes: one a uniform benchmark of liquidity adequacy, the other an internal measure of idiosyncratic liquidity risk. Thus, any substantive changes to the definition of HLA should preserve and enhance the most essential and risk-sensitive aspects of the current stress testing framework.

Specifically, we believe the Federal Reserve should revise the HLA definition to include assets that meet the LCR definition of HQLA in 12 CFR 249.3, without limitation and without requiring Federal Reserve approval under Regulation YY. Expressly providing that HQLA qualifies as HLA without Federal Reserve approval would simplify the liquidity stress testing rules and reduce the Federal Reserve's administrative burden by eliminating formal individual determinations. Moreover, it achieves these goals without decreasing the quality of the Federal Reserve's liquidity risk oversight, as Federal Reserve supervisory staff and examiners would still review how an organization incorporates specific types of HQLA as HLA in the organization's liquidity stress testing program during their assessment of the organization's liquidity position and risk management. While HQLA should be included within the definition of HLA, the HLA definition should retain flexibility for an organization to demonstrate to the Federal Reserve that assets that do not qualify as HQLA under the LCR rule are still highly liquid for purposes of the liquidity stress testing requirements.

Notwithstanding the foregoing recommendations, it is critical to keep internal liquidity stress tests distinct from the LCR requirement. Liquidity stress testing frameworks are set by each organization to reflect the organization's own view of its liquidity risk and broader risk profile, and are tailored to its particular activities and balance sheet composition. On the other hand, the LCR is a standardized measure of liquidity adequacy that provides regulators and external stakeholders a uniform view of the industry's liquidity risk and a single metric to compare across organizations. Keeping these requirements distinct creates a diversity of liquidity risk measurement tools and ensures that organizations manage their liquidity against a more robust overall liquidity framework. To that end, the Federal Reserve should *not* incorporate into the company-run stress tests under Regulation YY the additional restrictions on HQLA that apply to calculations of the LCR, such as "eligible HQLA," HQLA haircuts, or quantitative limits on the composition of the HQLA amount. For the same reason, the Federal Reserve should not require HQLA under the LCR rule to meet the other requirements for HLA set forth in Regulation YY.

It is unnecessary to apply uniform HQLA restrictions on HLA because each organization already places its own additional restrictions on HLA, such as haircuts for specific types of HLA, based on the organization's individual liquidity risk analysis and profile. Applying the "eligibility," haircut and other requirements of the LCR to HLA prevents an organization from setting similar requirements tailored to the organization's specific risks, effectively turning the liquidity stress test more into a uniform standard than a tailored and distinct risk management tool. If restrictions and underlying assumptions for HLA matched those for HQLA, then, to meet liquidity requirements, organizations would be pressured to align corresponding stress outflow assumptions with the standardized ones provided in the LCR rule. The result would not be an institution's view of its liquidity reserves or a view of how stressed liquidity outflows would be tailored to the institution's risk profile. These additional restrictions would also increase uncertainty and operational risk, as it would not be clear what other LCR requirements supervisors would expect an organization to incorporate into its internal stress tests.

Making the liquidity stress test more like the LCR, thus, would run counter to the objective of having two, separate and independent views of liquidity risk—a firm-developed view under Regulation YY, which reflects assumptions tailored to the specific products and risk profile of the company, and a standardized, regulatory-imposed view under the LCR rules (including any tailored or modified LCR applied to certain Category III or Category IV organizations), which facilitates a transparent assessment of firms' liquidity positions under a standard stress scenario and facilitates comparison across firms.[8]

* * *

The undersigned regional banking organizations appreciate the opportunity to comment on the FBO Proposals and respectfully ask for consideration of the recommendations and suggestions in this letter. If you have any questions regarding the content of this letter or would like more information on our recommendations, please do not hesitate to contact any of the individuals listed in Attachment 1 to this letter.

Sincerely,

Capital One Financial Corporation
The PNC Financial Services Group, Inc.
U.S. Bancorp

[8] Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations, 79 Fed. Reg. 17,240, 17,253 (Mar. 27, 2014) ("The proposed U.S. LCR and the enhanced liquidity requirements included in this rule were designed to complement one another. Whereas the final rule's internal liquidity stress-test requirements provide a view of an individual firm under multiple scenarios, and include assumptions tailored to the specific products and risk profile of the company, the standardized measure of liquidity adequacy that would be provided by the proposed U.S. LCR would facilitate a transparent assessment of firms' liquidity positions under a standard stress scenario and facilitate comparison across firms. Both requirements would enhance the liquidity position of bank holding companies while requiring robust liquidity risk management practices.").

Attachment 1

Robert Zizka
Executive Vice President – Capital Markets & Analytics
Capital One Financial Corporation
Phone: 703-720-1777
robert.zizka@capitalone.com

Randall C. King
Executive Vice President, Treasurer
The PNC Financial Services Group, Inc.
Phone: 412-762-2594
randall.king@pnc.com

John C. Stern
Executive Vice President and Treasurer
U.S. Bancorp
Phone: 612-303-4171
john.stern@usbank.com