The Credit Roundtable

THE VOICE OF THE BUYSIDE

January 20, 2023

Re: FDIC Advance Notice for Public Comment (“ANPR”)

The Credit Roundtable[1] appreciates the opportunity to comment on the question of whether an extra layer of loss-absorbing capacity could improve optionality in resolving a large banking organization or its insured depository institution as proposed by the Board of Governors of the Federal Reserve System ("Board") and the Federal Deposit Insurance Corporation (“FDIC”).

Credit Roundtable members invest in large regional banks’ debt capital across the maturity spectrum and capital structure. The proposed rule has given rise to a number of concerns, questions and recommendations which we have grouped into the following sections:

1. **Subordination**

   The ANPR solicits comment on the appropriateness of recognizing debt issued by various legal entities within a holding company structure in determining compliance with any long-term debt requirement.

   We believe there should be a clear ruling on which entities are permitted to issue regulatory qualifying long-term debt. Clarity will ensure investors in the senior unsecured, subordinated and preferred equity of large regional banks have an improved understanding of their relative position in a resolution/liquidation scenario as well as being better positioned to evaluate and value such debt when issued.

[1] [1] Formed in 2007, The Credit Roundtable (“CRT”) is a group of large institutional fixed income managers including investment advisors, insurance companies, pension funds, and mutual fund firms, responsible for investing more than $4 trillion of assets. The Credit Roundtable advocates for creditor rights through education and outreach and works to improve fixed income corporate actions, ineffective covenants, and the underwriting and distribution of corporate debt. Its mission is to improve risk assessment and management through education and seeks to benefit all bond market participants through increasing transparency, market efficiency and liquidity.

The Credit Roundtable, 25 North Broadway, Tarrytown, New York 10591
Website: www.thecreditroundtable.org
Email Address: info@thecreditroundtable.org

To provide greater optionality and reflect the ongoing growth of non-bank activities of the larger regional banks, the issuance of qualifying long-term debt from the holding company would likely be most practical. This approach seeks to avoid possible complications in a resolution, as such debt issued by the operating bank should not be included in the long-term debt requirement.

Holding companies should be instructed as to how they can preposition TLAC at material subsidiaries such that holding company debt can absorb severe losses at material operating entities.

To enable the banks affected by the implementation of such a rule, we believe the most efficient solution is to provide the banks with a grace period over three years in order to replace bank level debt with holding company debt. We recognize the issuance of this holding company debt will likely be at higher cost and lower rated than comparable bank level debt. However, we note international peers including the mid-sized European banks are operating under similar debt requirements so questions regarding competitiveness should be placed within that context.

The sole ability of the holding company to issue qualifying regulatory debt reflects the view that resolution via the holding company is likely the better course of action to preserve the operating bank's franchise value and bear the least cost to the Deposit Insurance Fund.

The appropriate calibration of a long-term requirement for each large regional bank should likely reflect each of the banks' relatively smaller size and simpler business model compared to that of a typical G-SIB. To that extent, the exact calibration of long-term debt should reflect a sliding scale from the more complex G-SIBs to the lesser complex regional banks comprising of Category II and Category III firms. Similar to the G-SIB banks, limitations on dividends and bonus payments should be disclosed should long-term debt limits be breached.

The proposed scaling of a qualifying long-term debt requirements driven by an institution's size will likely result in more firms qualifying to become G-SIBs as they grow, as well as allow firms to shed the G-SIBs status should their size be reduced. In a sense such a scaling requirement would provide both entry and exit points to G-SIB status rather than create bright-line thresholds.

2. **Liquidity**

The trading volume of regional bank paper tends to be less than that of the G-SIBs, reflecting lower amounts of total debt outstanding of these banks. As such, there is a smaller investor base and thus, a limited willingness of the larger regional banks' securities arms to trade in regional bank paper.

Liquidity in regional bank paper could further suffer if the regional banks are prohibited from owning the debt of other regional banks for market making purposes. As a result, this would likely effect the pricing of regional bank bonds. Regional banks should be allowed to make markets in the debt of other regional banks within specified guidelines similar to those followed by the G-SIBs

3. **Disclosure**
Long-term debt holders face the risk of becoming equity holders of a recapitalized bank holding company. To fully understand the risks involved and priority of claims, larger regional banks should be required to declare, quarterly (in-line with GSIBs), the quantum and percentage of qualifying long-term debt relative to required minimum requirement.

The importance of debt holders should not be overlooked by regulators. In the event of a resolution, any bridge bank will need external debt financing as part of the transition. As such, participation of institutional debt investors will be integral to the success of that transition. We therefore believe that respective regulators should engage institutional debt investors on an annual basis.

Please direct any questions to Kelly Byrne Skarupa of The Credit Roundtable at kbyrne@taminc.com or (914) 332-0042.

Sincerely,

The Credit Roundtable