

October 22, 2012

Office of the Comptroller of the Currency  
250 E Street, S.W.  
Mail Stop 2-3  
Washington, DC 20219  
**Docket IDs OCC-2012-0008, OCC-2012-0009,  
OCC-2012-0010  
RIN 1557-AD46**

Board of Governors of the Federal Reserve System  
20th Street & Constitution Avenue, N.W.  
Washington, DC 20551  
Attention: Jennifer J. Johnson, Secretary  
**Docket No. R-1442  
RIN 7100-AD87**

Federal Deposit Insurance Corporation  
550 17th Street, N.W.  
Washington, DC 20429  
Attention: Comments/Legal ESS  
Attention: Robert E. Feldman, Executive Secretary  
**RIN 3064-AD95, 3064-AD96, 3064-AD97**

Dear Sirs and Mesdames:

Deutsche Bank AG (“**Deutsche Bank**”) appreciates the opportunity to comment on the three joint notices of proposed rulemaking (the “**NPRs**”) issued by the Board of Governors of the Federal Reserve System (the “**Federal Reserve**”), the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (together, the “**Agencies**”) and published in the Federal Register on August 30, 2012, which would implement aspects of Basel III.<sup>1</sup>

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<sup>1</sup> Agencies, *Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III – Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action*, 77 Fed. Reg. 52,792 (Aug.

Deutsche Bank appreciates the Agencies' efforts in the NPRs to make capital requirements more risk sensitive and to harmonize capital rules in the United States with those applying globally to foreign banking organizations; however, it does have particular concerns about aspects of the Agencies' proposals. These concerns focus on a common theme – the operational burdens imposed on foreign-headquartered banking organizations subject to Basel requirements in their home jurisdiction in complying simultaneously with the new requirements of the NPRs for their sizeable U.S. operations. Although Deutsche Bank recognizes that certain of these operational burdens are a by-product of provisions in the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “**Dodd-Frank Act**”), it submits that where the Agencies do have discretion to take into account and give credit to home country implementation of Basel III, they should do so.

As the Agencies are aware, the EU is in the process of finalizing its rules to implement Basel III for European financial institutions such as Deutsche Bank (“**CRD IV**”). Deutsche Bank is concerned that there are already a number a material differences between the EU and U.S. proposals, not only with respect to implementation of the capital components and deduction regimes set forth in Basel III but also with respect to implementation of the risk weighting regimes set forth in Basel II and modified in Basel III. Deutsche Bank encourages the Agencies to coordinate and consult closely with their counterparts in the EU to ensure greater harmonization of capital standards across jurisdictions. International consistency in the

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30, 2012); Agencies, *Regulatory Capital Rules – Standardized Approach for Risk-Weighted Assets; Market Discipline and Disclosure Requirements*, 77 Fed. Reg. 52,888 (Aug. 30, 2012) (the “**Standardized Approach NPR**”); Agencies, *Regulatory Capital Rule: Advanced Approaches Risk-Based Capital Rules; Market Risk Capital Rule*, 77 Fed. Reg. 52978 (Aug. 30, 2012) (the “**Advanced Approaches NPR**”).

implementation of Basel III will reduce operational burden and result in a more level playing field for both U.S. and non-U.S. banking organizations that operate in the global market.

**I. With Respect to Model Validation, the Agencies Should Bear in Mind the Substantial Operational Costs for Foreign Headquartered Banks in Complying With Multiple Validation Requirements.**

As a universal bank organized under the laws of the Federal Republic of Germany, Deutsche Bank is subject to supervision by the *Bundesanstalt für Finanzdienstleistungsaufsicht* (the “**BaFin**”) on a group-wide basis, in addition to being subject to the United States’ bank capital regime with respect to its U.S. operations. Deutsche Bank’s U.S. operations are sufficiently significant that it is expected that the capital rules in the Advanced Approaches NPR will apply to them in some manner.

Under the Advanced Approaches NPR, there is a substantial process relating to a banking organization’s receiving regulatory approval to calculate its risk-based capital requirements using internal ratings-based and advanced measurement approaches (the “**Advanced Approaches**”), including development of an implementation plan and ongoing compliance with the qualification requirements of the Advanced Approaches.<sup>2</sup> For example, the Advanced Approaches NPR requires prior written regulatory approval to use the internal models methodology for measuring counterparty credit risk and the advanced CVA approach, and to use the double default treatment

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<sup>2</sup> Advanced Approaches NPR, §§\_\_\_\_.121 – 123.

and internal models approach for equity exposures.<sup>3</sup> Similarly, the Market Risk Final Rule requires written regulatory approval to use internal models to measure market risk.<sup>4</sup> The BaFin, however, has its own requirements for banking organizations subject to its jurisdiction that wish to use internal risk methodologies, with an application process followed by supervisory approval of an institution's models; these home country requirements achieve substantially similar outcomes.<sup>5</sup>

Although Deutsche Bank understands that implementation of the Advanced Approaches in the United States must require U.S. supervisors to make some assessment of the models used by the U.S. operations of non-U.S. banking organizations, it would urge the Agencies to give due consideration to a foreign banking organization's internal models, methodologies, governance, and validation processes that are deemed satisfactory by the home country supervisors of those institutions. U.S. regulators, of course, should be satisfied that the home country supervisors have implemented an adequate regime for validating the banking organization's internal systems. If such an adequate regime exists, U.S. regulators should seek to reduce overlapping validation requirements, which will impose significant operational costs on the U.S. operations of foreign banking organizations. A foreign banking organization should be permitted, as part of its U.S. validation procedures for the Advanced Approaches, to demonstrate how its internal processes meet the qualification requirements of its home country supervisor and how those requirements

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<sup>3</sup> Id. § \_\_\_\_.122.

<sup>4</sup> Agencies, Joint Final Rule, Risk-Based Capital Guidelines, Section 3.

<sup>5</sup> BaFin, Guidelines for applications to use the IRBA for calculating minimum capital requirements, April 1, 2007. *See also* Solvency Regulation (*Solvabilitätsverordnung*) (approval process for advanced internal approaches to market and operational risk).

are comparable to those required by the Advanced Approaches NPR.<sup>6</sup>

## **II. The Agencies Should Act to Reduce the Burdens Imposed by the Multiplicity of Minimum Capital Requirements for Foreign Banking Organizations Operating in the United States.**

In addition to reflecting Section 939A of the Dodd-Frank Act, which eliminates the use of external credit ratings in regulations, the NPRs seek to give effect to the requirements of the so-called Collins Amendment contained in Section 171 of the Dodd-Frank Act. Section 171 would be implemented via the Standardized Approach NPR, which would impose a minimum capital floor for those banking organizations that use the Advanced Approaches: that is, an Advanced Approaches banking organization would need to calculate its risk-based capital ratios using *both* the internal-models based methodologies under the Advanced Approaches NPR and the non-models based methodologies prescribed by the Standardized Approach NPR, and then would be required to use the lower of these two sets of ratios to determine compliance with minimum risk-based capital requirements.

By requiring Advanced Approaches banking organizations to calculate their capital twice, the NPRs increase the complexity of capital and risk management systems required of banking organizations. The differences between the Advanced Approaches and the Standardized Approach are far-ranging, including the risk-weights for corporate loans, the treatment of exposures to securities firms, the treatment of exposures to residential mortgages, weightings for

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<sup>6</sup> The ongoing Basel Peer Review Process, and particularly Level 3's focus on risk-weighted assets, will provide useful reference points for assessing comparability.

past due and non-accrual loans, and the treatment of off-balance sheet items and OTC derivatives contracts.

When applied to a foreign banking organization like Deutsche Bank, Section 171 has the effect of requiring four sets of parallel capital calculations for U.S. operations. The first and the second – a German advanced approach and a required Basel I floor<sup>7</sup> – are required under home country capital requirements. The third and fourth are imposed by the U.S. Advanced Approach and the U.S. Standardized Approach.

Given this multiplicity of capital requirements, the Agencies should re-assess whether their proposed departures from the Basel II Standardized Approach – which reflects an agreement among international regulators and has since been implemented in many foreign jurisdictions – are warranted. In particular, Deutsche Bank would urge the Agencies to reconsider, for complex banking organizations that have had their internal models approved in the supervisory process, (i) the absence of risk sensitivity in the calculation of risk-weighted assets for corporate loans under the Standardized Approach NPR, (ii) the fact the Standardized Approach NPR does not permit the use of the Simple VaR methodology or the Internal Models Methodology (“**IMM**”) to calculate exposures on repo-style transactions and eligible margin loans, and (iii) the fact that the Standardized Approach NPR does not permit the use of the IMM to calculate exposures on over-the-counter derivatives and the valuation of credit risk mitigants. Deutsche Bank would further propose that the Agencies give such complex banking organizations the option to follow a more risk sensitive version of the Standardized Approach in these and similar areas, even if this option is not available to less sophisticated institutions that do not have supervisorily-approved internal

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<sup>7</sup> The Basel I floor under BaFin requirements will be phased out between 2015 and 2017.

risk assessment methodologies. For a foreign banking organization that is required to demonstrate appropriate risk management capabilities to a home country regulator that has implemented an adequate, Basel-based regulatory capital framework, being permitted to implement more risk-sensitive measures for calculating risk-weighted assets is consistent with aligning required capital with actual risks.

### **III. The Agencies Should Permit Foreign Banking Organizations to Use the Segmentation Regime They Have Developed In Accordance With Their Home Country Capital Regulations.**

Under the NPRs, differences in segmentation schemes, assigned risk weights, and correlation factors will require substantial operational changes to processes and systems. In Deutsche Bank's case, it uses an Advanced Internal Ratings-Based Approach developed under the BaFin's supervision that has its own segmentation regime, and it also calculates capital under the BaFin's Basel I Standardized Approach. As noted in Section II, as a result of Section 171 of Dodd-Frank as proposed to be implemented by the NPRs, Deutsche Bank will be required to make two additional capital calculations for its U.S. operations.

With respect to these additional required calculations, the Agencies' Standardized Approach NPR would, among other things: introduce a whole new segmentation regime for residential mortgages; eliminate risk sensitivity with respect to the treatment of corporate loans; expand risk weight categories for past due loans; change the hierarchy of approaches to securitization exposures; expand treatment categories for equity investments; and increase the risk-weighting assigned to exposures to securities firms. Many of these proposed changes depart

from the internationally agreed upon Standardized Approach under Basel II.<sup>8</sup> In addition, the Advanced Approaches NPR would, among other things: amend various aspects of the counterparty credit risk framework (including changes to assumed collateral holding periods and margin periods of risk and requiring banks to consider stressed inputs when calculating their capital requirements for counterparty credit risk); impose a new capital charge for credit valuation adjustment; change the capital treatment of securitization exposures; and take a more restrictive view of eligible collateral by excluding from the definition of eligible collateral resecuritizations, conforming residential mortgages and non-investment grade debt. Under both the Standardized Approach NPR and the Advanced Approaches NPR, previously zero risk-weighted transactions such as repurchase agreements and derivatives cleared through central counterparties would be subject to risk-weighting under a new framework for cleared transactions.

Because the changes to Deutsche Bank's current segmentation regime mandated by the NPRs would impose significant operational costs, Deutsche Bank would request that under the Advanced Approaches NPR, it, and other similarly situated foreign banking organizations, be allowed to retain the segmentation regime that it has developed with the approval of its home country regulator. In addition, these operational costs support the need for the modifications to the Standardized Approach suggested in Section II above.

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<sup>8</sup> The Basel Committee on Banking Supervision (“**Basel Committee**”), in its preliminary Basel III regulatory consistency assessment of U.S. Basel III implementation efforts, identified a number of areas in which the Agencies’ proposals depart from the international Basel capital framework. In particular, the Basel Committee’s assessment report determined the Agencies’ proposed capital treatment for securitization exposures to be “materially non-compliant.” See Basel Committee, *Basel III Regulatory Consistency Assessment (Level 2) Preliminary Report: United States of America*, 13 (Oct. 2012), available at [http://www.bis.org/bcbs/implementation/12\\_us.pdf](http://www.bis.org/bcbs/implementation/12_us.pdf).

#### **IV. The Agencies Should Tailor The Public Disclosure Requirements for Foreign Banking Organizations to Account for Existing Required Disclosures.**

Under the BaFin’s implementation of Basel II, Deutsche Bank, on the group level, already makes significant disclosures with respect to its capital and risk-weighted assets. Under the NPRs, there are new requirements for detailed public disclosure for institutions subject to the NPRs, such as qualitative and quantitative reporting of securitization exposures, and disclosure related to operational and market risk. The NPRs do, however, provide an exemption for subsidiaries of non-U.S. banking organizations, as long as they are subject to “comparable public disclosure requirements in [their] home jurisdiction.”<sup>9</sup> This is consistent with the existing U.S. Basel II Advanced Approaches rules.<sup>10</sup>

In Deutsche Bank’s view, it is imperative that, as the NPRs are applied to U.S. holding and operating company subsidiaries of non-U.S. banking organizations, that the “comparability” requirement be applied in a manner that recognizes comity with other jurisdictions that are implementing Basel III. If a non-U.S. jurisdiction has meaningfully implemented Basel III’s disclosure requirements, the rationale for the U.S. disclosure requirement will have been satisfied, and the foreign banking organization should be spared the burden of multiple reporting requirements. Such treatment will accord with the treatment of U.S. banking organizations under the NPRs, which are required to make the relevant disclosures at the group, and not the single entity, level. Finally, Agency interpretation of the “comparable public disclosure” requirement

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<sup>9</sup> Standardized Approach NPR, § \_\_.61.

<sup>10</sup> See e.g., 12 C.F.R. 225 App. G, § 71(b)(1).

with a view to international comity could result in analogous, reciprocal treatment for U.S. banking organizations that have substantial subsidiaries in non-U.S. jurisdictions.

**V. The Agencies Should Consider the Effects of the Elimination of External Ratings When Measuring the Costs of Basel III Implementation.**

In both the Advanced Approaches NPR and the Standardized Approach NPR, the Agencies have implemented the requirement of Section 939A of the Dodd-Frank Act eliminating the use of external credit ratings in regulations. Although Deutsche Bank recognizes that this elimination follows a statutory mandate, it does wish to note that no similar requirement exists for it or other German banks under home country rules. As implemented by the NPRs, Section 939A has substantial effects: for example, (i) a firm may not rely on external ratings in the simple CVA approach; (ii) reliance on external ratings is not permitted for eligible credit default swap or securitization guarantors; (iii) such reliance is not permitted in calculating risk-weights for securitization exposures; and (iv) with respect to risk mitigation, recognition of collateral and guarantee eligibility is not based on external ratings, but rather there is a set of supervisory haircuts based on counterparty or guarantor type.

All of these proposed changes in the NPRs will substantially affect risk-weighted asset calculation processes, will introduce major revisions to the treatment of securitization exposures, and will mandate additional processes and systems for making regulatory capital calculations – thus imposing substantial additional costs for foreign banking organizations whose home country rules rely on external credit ratings and view the consideration of external ratings as effectively managing risk. Such costs must be balanced against the perceived benefits, as a risk

management matter, of eliminating consideration of external ratings, and also taken into account when considering the overall effects of the Agencies' proposed implementation of Basel III, particularly its effects on foreign-headquartered banking organizations that have sizeable U.S. operations.

## **VI. Considered As a Whole, The NPRs Will Impose Substantial Burdens on Complex Banking Organizations.**

A complex banking organization like Deutsche Bank operates its risk management infrastructure on a group-wide basis; as a foreign banking organization, this infrastructure in the first instance reflects supervision by its home country regulator, the BaFin. As discussed in the other sections above, the NPRs introduce numerous changes – some of them small, but others very substantial – to definitions and capital calculation methodologies.

Taken individually, certain of the proposed changes may have a small impact from a regulatory capital or compliance perspective when compared with other aspects of the proposals. Implementing all of the proposed changes across multiple risk and finance systems, and aggregating the resulting data on a consolidated legal entity basis, however, will be a significant undertaking. As described above, Deutsche Bank and other similarly situated foreign banking organizations could become subject, in the United States, to four sets of parallel capital calculations – two required by their home country regulator, the U.S. Advanced Approach NPR, and then the floor set by the Standardized Approach NPR, the last of which differs substantially

from the first three.<sup>11</sup> As a result, implementation of the proposals in their current form will require reviews of, and modifications to, multiple existing systems and algorithms to ensure compliance.

In addition to the general burdens of complying with multiple capital requirements, particular examples of changes requiring modifications to existing systems include, as discussed above, the changes required by the elimination of external ratings, changes in the definitions relating to securitizations, the reduced risk sensitivity of the Standardized Approach NPR for corporate loans and mortgages, and the Standardized Approach's treatment of off-balance sheet items and derivatives contracts. The extensive operational efforts required to comply with these new requirements, moreover, will likely not improve banking organizations' overall risk management practices and culture or their ability to comply with other prudential standards in effect or to be implemented in the near term. The Agencies should not underestimate the effects of substantial multiple demands on internal resources.

Although some of this increased implementation burden is merely the by-product of the move to Basel III generally, Deutsche Bank would submit that where the Agencies do have discretion – particularly in implementing the numerous regulatory model approval requirements set forth in the Advanced Approaches NPR for a foreign banking organization whose internal models have already been examined and determined to be satisfactory by its home country regulator – the Agencies focus on the overall compliance costs of the NPRs and the relative benefits of strict adherence to U.S. rules, given the foreign banking organization's already existing umbrella supervision. Doing so should also serve to reduce operational risk, as being

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<sup>11</sup> See Section II above.

required to manage multiple evolving systems can easily result in counterproductive complexity being introduced into a large banking group's risk management process. Through close coordination with home country regulators, the Agencies can both increase efficiencies for foreign banking organizations and bolster those organizations' risk management processes.

Deutsche Bank appreciates the opportunity to comment on the NPRs. If it would be useful, we would welcome the opportunity to meet and discuss our response.

Very truly yours,



Richard W. Ferguson

Chief Risk Officer, Americas