Santander

February 19, 2016

Mr. Robert deV. Frierson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Notice of Proposed Rulemaking on Total Loss-Absorbing Capacity, Long-Term Debt, and Clean Holding Company Requirements for Systemically Important U.S. Bank Holding Companies and Intermediate Holding Companies of Systemically Important Foreign Banking Organizations; Regulatory Capital Deduction for Investments in Certain Unsecured Debt of Systemically Important U.S. Bank Holding Companies. Docket No. R-1523 and RIN 7100-AE37

Dear Mr. Frierson:

Santander Holdings USA, Inc. (SHUSA) appreciates the opportunity to comment on the proposal to promote financial stability by improving the resolvability and resiliency of large, interconnected U.S. bank holding companies and the U.S. operations of large, interconnected foreign banking organizations pursuant to section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and related deduction requirements for all banking organizations subject to the capital rules issued by the Board of Governors of the Federal Reserve System (Board). We respectfully submit these comments to you for the Board's consideration.

Banco Santander, S.A. (Santander, S.A.), a foreign banking organization (FBO), is organized under a decentralized subsidiary model that would utilize a multiple-point-of-entry (MPOE) resolution strategy. SHUSA is a U.S. Bank Holding Company (BHC) subsidiary of Santander and has in place a holding company/operating company structure similar to other U.S. BHCs. SHUSA is the parent company of Santander Bank, N.A, and has a majority ownership interest in Santander Consumer USA Holdings Inc. (SC). SHUSA, an SEC registered company active in public debt markets, does not engage in material operations and focuses on managing the consolidated risks of the organization, coordinating the operations of the subsidiaries and raising long-term debt to support its liquidity buffer. SHUSA and its subsidiaries had approximately $131 billion in U.S. assets and approximately 14,700 employees as of September 30, 2015.

Santander supports the establishment of appropriate TLAC requirements for covered BHCs and covered IHCs. We believe such requirements will advance the Board's goal of ensuring sufficient resources are available in the U.S. to facilitate the resolution of covered entities and mitigate risks to U.S. financial stability arising from the failure of such entities.

In order to advance the shared goal of a stronger and more resilient U.S. financial system, we urge the Board to consider a final TLAC rule that incorporates and better reflects:

- the decentralized subsidiary business model's advantages, which are consistent with the Board's policy goals and priorities, including pre-positioning to facilitate an orderly resolution;
- existing rulemaking, including enhanced prudential standards (EPS) and capital requirements; and
- the systemic risk profile of covered institutions.

Comments on Proposed Rulemaking

Given the potential impacts to all covered IHCs, and specifically to firms that would be resolved through an MPOE resolution strategy, we submit for your consideration a summary of some of the most relevant proposed TLAC requirements for SHUSA and our recommendations for how identified issues could be addressed in the final rulemaking.

As context for the specific recommendations that follow, we begin with an overview of Santander's business model, including its alignment with current regulatory standards applicable to FBOs, and a summary of the risk profile of covered IHCs, such as SHUSA.

Decentralized Subsidiary Business Model: Santander's subsidiary model is well-established, deployed in the countries in which Santander operates, and optimal for an MPOE resolution strategy. The main strengths of Santander's business model include, but are not limited to:

- Legal Form & Supervision: Businesses are organized in distinct subsidiaries operating in different jurisdictions, and each subsidiary is primarily supervised by host country authorities.
- Governance: Santander provides group strategy and governance guidelines and supervises their implementation. However, governance structures are established and maintained at the subsidiary level. The governance structure includes a separate, independent board of directors with a majority of independent directors and fully accountable management, in addition to other local internal controls. Subsidiary executives manage their subsidiaries' risk based on local business needs and the economic environment.
- Funding: Each subsidiary manages its own capital and liquidity as well as its access to markets. Capital and liquidity standards are met at the parent and local levels independently. As a general principle, the subsidiaries do not depend on subsidiary and/or parent interconnectivity, thereby limiting an organization's contagion risk and aiding host and/or home country resolution. Intragroup support may be provided from time to time, but it is transparent, temporary, and at market prices. Overall, there are very limited intragroup positions, a key feature of the decentralized business model.
- Resolution: Given Santander's decentralized business model, Santander would implement an MPOE resolution strategy – as decided by the Single Resolution Board (SRB, European resolution authority) and Santander's Crisis Management Group (CMG) – that would facilitate the resolution of local subsidiaries by having the host country lead the resolution process. This strategy creates natural firewalls in financial crises, containing the financial disruption within the local entities rather than transmitting it outside of the jurisdiction and weakening affiliates.

Santander, S.A.'s Resolution Strategy: The Single Resolution Board (SRB) is Santander, S.A.'s resolution authority, responsible for Santander, S.A.'s resolution strategy and its implementation. The SRBs mandate is to take all measures available to stabilize the entity and to preserve critical operating functions.

The SRB has concluded that Santander would not be subject to liquidation but rather to resolution procedures. Those resolution procedures would follow Spanish resolution law that implements the European Banking Recovery and Resolution Directive.

Santander's Crisis Management Group (CMG)[1] has adopted an MPOE resolution strategy for Santander. In a scenario in which Santander, S.A. failed, SHUSA can remain healthy. This corporate structure allows SHUSA's operating subsidiaries to remain going concerns during Santander, S.A.'s resolution. The local authorities have all resolution powers to activate the local resolution plan for subsidiaries, if needed. In addition, the structural subordination of the U.S. BHC ensures that SHUSA's creditors absorb losses ahead of the creditors of any of its subsidiaries.

Compatibility with EPS and IHC Rules: The strengths of a decentralized business model and the MPOE resolution strategy that would be employed by Santander are consistent with the goals of the Board's EPS framework to mitigate risks to U.S. financial stability posed by FBOs.

As noted in the Board's staff memorandum for the final EPS rule for FBOs: "A firm that relies significantly on centralized resources may not be able to provide support to all parts of its organization."[2] As further noted in the final EPS rule, "[t]he Board believes that the final [EPS] rule reduces the need for a foreign banking organization to contribute additional capital and liquidity to its U.S. operations during times of home country or other international stresses, thereby reducing the likelihood that a banking organization that comes under stress in multiple jurisdictions will be required to choose which of its operations to support."[3]

Santander's decentralized subsidiary business model is uniquely aligned with and highly compatible to the IHC requirement for covered FBOs, a requirement that is among the most significant aspects of the EPS rule.[4]

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1 Crisis Management Groups bring together home and key host authorities of all Global Systemically Important Financial Institutions (G-SIFIs). Santander's Crisis Management Group is currently composed of the Single Resolution Board, as the consolidated resolution authority, The Bank of Spain, The Bank of England, and the Bank of Brazil. Other supervisory and resolution authorities are invited to attend meetings.

2 Board Memorandum, Final rules to implement the enhanced prudential standards of section 165 of the Dodd-Frank Act (February 7, 2014).

3 Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations; Final Rule; 79 Fed. Reg. 17240 (Mar. 27, 2014).

4 Ibid.

The IHC requirement marked a fundamental shift in U.S. regulatory treatment of larger FBOs by, among other things, increasing the resiliency of their U.S. operations and facilitating a level playing field between foreign and U.S. banking organizations operating in the United States in furtherance of the principles of national treatment and competitive equality. The requirement moved foreign banking organizations away from a capital and liquidity system that promoted an overreliance on the parent company for financial support of an FBO's U.S. operations, the continuance of which would have required the Federal Reserve "to make regular and detailed assessments of each firm's home-country regulatory and resolution regimes, the financial stability risk posed by each firm in the United States, and the financial condition of the consolidated banking organization."[5]

The EPS rule implemented an IHC structure for FBOs that involved the creation of a top-tier U.S. holding company through which capital, liquidity, and other regulatory requirements would have to be met in the U.S. The IHC provides a structure for the supervision and regulation of U.S. subsidiaries of FBOs that closely resembles the framework under which U.S. BHCs are supervised and regulated.

Santander welcomed the new IHC requirement and broader EPS rulemaking for FBOs[6], as this framework is aligned with the decentralized operating model under which Santander was already operating.

Risk Profile: As a group, covered IHCs represent relatively low risk to U.S. financial stability. The Financial Stability Oversight Council's Office of Financial Research released a study in 2015 showing significant differences among the U.S. systemic risk profiles of 33 large BHCs, including BHCs of FBOs that operate in the U.S. through regional banks (see Appendix 1).

For example, SHUSA's overall *Systemic Risk Score* was tied for fourth lowest – representing a fraction of the average systemic risk scores reported by both the six largest BHCs and all BHCs. SHUSA also had the second lowest *Interconnectedness* score among BHCs, and the lowest overall *Substitutability* score. Based on the study's results, the risk profile for SHUSA is more analogous to, and in most cases lower than, other U.S. BHCs.

The importance of these risk factors, particularly with respect to the development and application of more stringent prudential standards, is underscored in the "Tailored Application" section of EPS[7], under which the Board is authorized to "differentiate among companies on an individual basis or by category, taking into consideration their capital structure, riskiness, complexity, financial activities (including the financial activities of their subsidiaries), size, and any other risk-related factors that the Board of Governors deems appropriate."

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5 Federal Reserve Board Governor Daniel K. Tarullo, "Regulation of Foreign Banks" (Yale School of Management Leaders Forum, New Haven, Connecticut, November 28, 2012).

6 SHUSA Comment Letter on Notice of Proposed Rulemaking on Enhanced Prudential Standards and Early Remediation for Foreign Banking Organizations and Foreign Nonbank Financial Companies. (April 30, 2013).

7 Dodd-Frank Act § 165(a)(2)(A).

In summary, SHUSA is concerned that the Board's TLAC and LTD proposal undermines the MPOE resolution strategy that is designed to reduce systemic risk and facilitate resolution at the host level; is contrary to EPS and IHC requirements and could force a return to financial overreliance on the covered IHC's foreign parent; and does not reflect SHUSA's similarity to other U.S. BHCs or its low systemic risk profile.

Recommendations

As previously stated, Santander supports the establishment of appropriate TLAC requirements for covered BHCs and covered IHCs. We believe such requirements will advance the Board's goal of ensuring that sufficient resources are available in the U.S. to facilitate the resolution of covered entities and mitigate risks to U.S. financial stability arising from the failure of such entities. We urge the Board to consider adopting a final TLAC rule which ensures that those covered IHCs which have a business model and structure aligned with EPS, similar to local competitors, and pre-positioned to facilitate an orderly resolution, receive equal treatment to their covered BHCs peers.

The following recommendations reflect SHUSA's priorities with respect to the proposed rulemaking:

I. Internal LTD Requirement

Under the proposal, a covered IHC's outstanding eligible internal LTD amount is comprised of eligible internal debt securities, which are debt instruments that, among other things, are issued by a covered IHC to, and remain held by, a company organized outside of the United States that directly or indirectly controls the covered IHC.

- *The Board invites comment on all aspects of the requirement that eligible internal LTD be issued to a foreign parent entity that controls the covered IHC. In particular, the Board invites comment with respect to whether covered IHCs that are expected to enter resolution themselves in a failure scenario should be permitted to issue eligible internal LTD to third parties, as covered BHCs would. Should internal LTD be required to be issued to the top-tier foreign parent of the covered IHC. (Question 36 of the proposal)*

Comments:
The combination of Santander, S.A.'s resolution strategy and SHUSA's holding company/operating company structure, which provides for structural subordination of holding company creditors, allows SHUSA's healthy operating subsidiaries to remain going concerns during Santander, S.A.'s resolution process. As such, we believe an internal-only LTD requirement is unwarranted in the case of covered IHCs with an MPOE resolution strategy. In addition, we believe that an internal LTD requirement for covered IHCs with an MPOE resolution strategy would increase interconnectivity with the foreign parent in a way that is contrary to supervisory guidance, EPS rules, and best practices for liquidity risk management, and may contribute to a heightened risk of cross-border contagion where financial disruption occurring at the parent company could potentially be exported to the U.S. IHC.

The Board provides several reasons why a covered IHC's TLAC must be internal: (1) losses incurred by the covered IHC would be upstreamed to the foreign parent, thereby minimizing risks that such losses may pose to U.S. financial stability; and (2) the conversion of internal TLAC into equity will not result in a change in control over a covered IHC which "could create additional and undesirable regulatory and management complexity during a failure scenario and would severely disrupt an SPOE resolution strategy."[8]

(1) Since the prudential regulatory framework and corporate structure of resolution entity covered IHCs and covered BHCs are analogous, as previously noted, it would not seem appropriate to apply an *internal-only* LTD provision – aimed at minimizing the risks that an entity's potential losses pose to U.S. financial stability – to covered IHCs.

(2) With respect to change in control concerns, a resolution entity covered IHC relies on an MPOE resolution strategy because, by its nature, it is part of a decentralized organization. Because each subsidiary of a financial group stands on its own, there should be fewer complications in transferring ownership of such subsidiaries than would be the case for subsidiaries that are highly interconnected. As a result, any disruption to financial stability due to a transfer of ownership should be relatively small.

To summarize, the similarities in prudential regulatory framework and corporate structure of covered BHCs and resolution entity covered IHCs present a compelling argument for similar treatment in meeting new loss absorbency requirements aimed at mitigating risks to U.S. financial stability due to a financial institution's failure.

Liquidity Risk Management Issues: By requiring that all TLAC, including eligible internal LTD, be issued to the foreign parent of a covered IHC, the proposal is contrary to supervisory guidance, EPS rules, and best practices for liquidity risk management.

<u>Interagency Policy Statement on Funding and Liquidity Risk Management (SR 10-6)</u>:
The agencies state that, "[c]ritical elements of sound liquidity risk management include…an appropriately diverse mix of existing and potential future funding sources," among other factors. The interagency guidance elaborates on this point by stating that "[f]unding diversification should be implemented using limits addressing counterparties, secured versus unsecured market funding, instrument type, securitization vehicle, and geographic market. In general, funding concentrations should be avoided. Undue over-reliance on any one source of funding is considered an unsafe and unsound practice."

<u>Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations (12 CFR Part 252.34 (g))</u>: The EPS rule provides that BHCs of a certain asset size "must monitor sources of liquidity risk and establish limits on liquidity risk," including limits on "[c]oncentrations in sources of funding by instrument type, single counterparty, counterparty type, secured and unsecured funding, and as applicable, other forms of liquidity risk."

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[8] Total Loss-Absorbing Capacity, Long-Term Debt, and Clean Holding Company Requirements for Systemically Important U.S. Bank Holding Companies and Intermediate Holding Companies of Systemically Important Foreign Banking Organizations; Regulatory Capital Deduction for Investments in Certain Unsecured Debt of Systemically Important U.S. Bank Holding Companies; Proposed Rule, 80 Fed. Reg. 229 (Nov. 30, 2015).

In contradiction of the above interagency guidance and EPS standards, the proposed internal LTD would require a covered IHC to meet its funding requirement by issuing a single debt instrument type (unsecured, longer than one year, issued under U.S. law, contractually subordinated and including contractual conversion trigger provisions) to a single counterparty in a single geographic market (the parent company). Meeting such a narrowly defined funding requirement would increase the covered IHC's interconnectivity with, and overreliance on, its parent company for financial support – contributing to a heightened risk of cross-border contagion where financial disruption occurring at the parent company could potentially be exported to the U.S. IHC.

FSB TLAC Standard: We also note that a minimum external TLAC requirement is established for resolution entity covered IHCs under the final version of the Financial Stability Board's (FSB) TLAC standard.[9] Under the FSB standard, "[e]xternal TLAC must be issued and maintained directly by resolution entities."[10] The FSB standard views internal TLAC as appropriate *only* for those entities that are not expected to independently enter resolution.[11] As such, the Board's requirement that resolution entity covered IHCs meet their TLAC requirement through internal-only issuances represents a departure from the FSB's approach.

RECOMMENDATION: The combination of Santander, S.A.'s resolution strategy and SHUSA's holding company/operating company structure, which provides for structural subordination of holding company creditors, allows SHUSA's healthy operating subsidiaries to remain going concerns during Santander, S.A.'s resolution process. As such, we believe an internal-only LTD requirement is unwarranted in the case of covered IHCs with an MPOE resolution strategy. In addition, we believe an internal LTD requirement for covered resolution entity IHCs would increase interconnectivity with the foreign parents in a way that is contrary to supervisory guidance, EPS rules, and best practices for liquidity risk management, and may contribute to a heightened risk of cross-border contagion where financial disruption occurring at the parent company could potentially be exported to the U.S. IHC.

To the extent that an LTD requirement for covered IHCs is preserved in the final rule, and in keeping with the FSB standard requiring external TLAC for resolution entity covered IHCs, we request that the Board allow covered resolution entity IHCs to maintain funding diversification by permitting such firms to have the flexibility to raise their TLAC and LTD requirement externally.

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9 Principles on Loss-absorbing and Recapitalisation Capacity of G-SIBs in Resolution: Total Loss-absorbing Capacity (TLAC) Term Sheet, Final Rule (Nov. 9, 2015).

10 As defined in the FSB TLAC standard: "A resolution entity is an entity to which resolution tools will be applied in accordance with the resolution strategy for the G-SIB. Depending on the resolution strategy, a resolution entity may be a parent company, an intermediate or ultimate holding company, or an operating subsidiary. A G-SIB may have one or more resolution entities."

11 The FSB standard describes the primary objective of internal TLAC as "ensuring the appropriate distribution of loss-absorbing and recapitalisation capacity within resolution groups," which are defined as subsidiaries of resolution entities that "are not themselves resolution entities."

RECOMMENDATION *(continued)*: If the Board opts to retain the internal LTD requirement in order to avoid any potential change in control issues, we request that the Board permit a cap aligned with the "unrelated liabilities" concept applied to covered BHCs, as provided for in the clean holding company requirement of the proposal. Since the Board has determined that this ratio of unrelated liabilities to the overall TLAC requirement would not pose an undue risk to the resolution of a covered BHC, we ask for equal treatment and flexibility for covered IHCs to be able to meet their TLAC requirements through a similar ratio of external debt issuance to the overall TLAC requirement.

At a minimum, we request that the Board grandfather from the provisions of the final rule a covered IHC's combined equity and LTD securities that were issued or incurred by a covered IHC before the effective date of the final rule.

II. Contractual Subordination and Contractual Conversion Trigger for Internal LTD

Under the proposal, eligible LTD instruments for covered IHCs must be contractually subordinated and include provisions by which the Board could order the covered IHC to cancel or convert them into equity under specified conditions, including if "the top-tier foreign banking organization or any subsidiary outside of the United States is placed into resolution proceedings."

- *The Board invites comment on the appropriateness of the proposed contractual subordination requirement for eligible internal LTD. (Question 37 of the proposal)*

- *The Board invites comment on all aspects of the contractual conversion trigger requirement, including the appropriateness of the requirement for foreign GSIBs with SPOE and MPOE resolution strategies, whether an alternative to the "in default or in danger of default" standard would be more appropriate, and any legal risks associated with the Board's conversion of eligible internal LTD into equity in order to recapitalize the covered IHC (Question 38 of the proposal)*

- *The Board invites comment on whether the conversion condition that refers to the placement of a foreign banking organization that controls the covered IHC or any subsidiary of the top-tier-foreign banking organization being placed into resolution in its home country is appropriate in scope. (Question 40 of the proposal)*

Comments:
Given that SHUSA's operating subsidiaries, if healthy, would be maintained as going concerns during Santander, S.A.'s resolution, and SHUSA's existing holding company/operating company structure already provides for the structural subordination of its creditors in case of a U.S.-based resolution, the benefit of imposing contractual subordination and contractual conversion trigger requirements on such a covered IHC is outweighed by the cost, as outlined below.

The Board states that the principal rationale for the contractual conversion trigger is "to ensure that losses incurred by the covered IHC are shifted to a foreign parent without the covered IHC's having to enter a resolution proceeding."[12] We believe that this requirement is unnecessarily restrictive and should not apply to resolution entity covered IHCs. Like U.S. BHCs, under an MPOE resolution strategy, the resolution entity covered IHC would be placed into a resolution proceeding, where debt can be written down or converted to equity, as appropriate, without the continuity of operations in the underlying bank being affected. There is no need for a contractual trigger to write down or convert debt to equity outside of such proceedings.

Requiring that eligible internal LTD be contractually subordinated and contractually subject to an internal debt conversion order would also put covered IHCs at a competitive disadvantage to U.S. GSIBs that can build their LTD requirements with senior unsecured debt at a comparatively lower cost.

Covered IHC Cost Impact: In addition to its limited usefulness, particularly in the case of covered IHCs that will rely on an MPOE resolution strategy, a requirement for LTD to include a contractual conversion trigger comes at a significant funding cost to covered IHCs. Because covered IHCs are subject to arm's-length pricing requirements even for internally placed eligible LTD, the contractual conversion trigger requirement, along with the contractual subordination requirement, will substantially increase the cost of borrowing for covered IHCs.

Of further concern to covered IHCs is that the contractual conversion trigger, coupled with the subordination required for internal LTD and prohibition on all acceleration clauses, could result in the U.S. Internal Revenue Service challenging the deductibility of interest paid on internal LTD for covered IHCs. A requirement that debt be converted to equity on the occurrence of specified triggers outside of a bankruptcy or other resolution proceeding could call into question the status of internal LTD as debt for U.S. tax purposes. Should such characteristics require internal LTD to be treated as equity, it would unnecessarily and substantially increase the costs to covered IHCs of complying with the Board's TLAC requirements.[13] Such unfavorable tax treatment could also, by extension, harm the market for eligible debt securities, resulting in further cost increases to covered IHCs required to issue the debt.

SHUSA Cost Impact: The eligible internal LTD costs would represent a significant increment in annual interest expense over the cost of meeting the requirement with senior unsecured debt available generally to covered BHCs. We estimate that the internal LTD requirement, as currently proposed, could cost SHUSA 100 to 150 basis points more than equal duration senior unsecured debt. This financial impact would be made worse by the tax implications outlined above.

Covered IHCs should not be subject to the additional funding costs and negative tax implications that result from these additional eligible internal LTD requirements which are not imposed on covered BHCs – particularly given the Board's acknowledgement that "covered IHCs that are

[12] Total Loss-Absorbing Capacity, Long-Term Debt, and Clean Holding Company Requirements for Systemically Important U.S. Bank Holding Companies and Intermediate Holding Companies of Systemically Important Foreign Banking Organizations; Regulatory Capital Deduction for Investments in Certain Unsecured Debt of Systemically Important U.S. Bank Holding Companies; Proposed Rule, 80 Fed. Reg. 229 (Nov. 30, 2015).

[13] IRS Notice 94-47.

not designated as non-resolution entities are more analogous to covered BHCs, which are themselves resolution entities."[14] Furthermore, without some tangible evidence that contractual subordination and contractual conversion trigger requirements would be reasonably related to reducing risk to U.S. financial stability, it is unclear whether the price incurred would be justified. These additional requirements are even more questionable in light of the fact that SHUSA, and all other covered IHC's have risk profiles that are much more similar to non-covered BHC than to covered BHCs.

RECOMMENDATION: Given that covered IHCs, such as SHUSA, are held to many of the same regulatory and resolution requirements as covered BHCs we request that covered IHCs have the same flexibility to meet any applicable LTD requirement without the unnecessary cost burden resulting from the proposed debt subordination and conversion trigger requirements.

While we do not believe resolution entity covered IHCs should be subject to an internal LTD requirement, as previously stated, if the Board opts to retain an internal LTD requirement for such firms, we request that eligible debt securities are excluded from a contractual subordination requirement. SHUSA's existing holding company/operating company structure already provides for the structural subordination of its creditors in case of a U.S.-based resolution. In addition, the proposed clean holding company framework for covered BHC and IHCs provides for eligible debt to be structurally subordinated. The combination of these factors, we believe, makes the contractual subordination requirement duplicative and, therefore, unnecessary as it may apply to resolution entity covered IHCs.

If the requirement for conversion features in the LTD requirement is maintained, a "conversion to equity" feature would be the preferred alternative given that a "cancellation of debt" feature could represent taxable debt forgiveness income.[15]

In addition, if the requirement for conversion features in the LTD requirement is maintained, we request that the Board consider alternatives to the proposed conversion condition which could trigger conversion if "the top-tier foreign banking organization or any subsidiary outside of the United States is placed into resolution proceedings." Given that SHUSA's healthy operating subsidiaries would be maintained as going concerns while the foreign parent (Santander, S.A.) or any of its non-U.S. subsidiaries is resolved, we recommend revising this proposed language to provide for a conversion trigger only in the case where an IHC subsidiary or company in the ownership structure between the covered IHC and the top-tier foreign parent is placed into resolution proceedings.

14 Total Loss-Absorbing Capacity, Long-Term Debt, and Clean Holding Company Requirements for Systemically Important U.S. Bank Holding Companies and Intermediate Holding Companies of Systemically Important Foreign Banking Organizations; Regulatory Capital Deduction for Investments in Certain Unsecured Debt of Systemically Important U.S. Bank Holding Companies; Proposed Rule, 80 Fed. Reg. 229 (Nov. 30, 2015).

15 IRS Code 108.

III. LTD Calibration for Covered IHCs

Under the proposal, a covered IHC's total internal TLAC amount is equal to the sum of its (a) tier 1 regulatory capital (CET 1 and additional tier 1 capital) issued to its top-tier foreign banking organization parent or to an intermediate entity that directly or indirectly controls the covered IHC and (b) the covered IHC's internal LTD. With respect to internal LTD, a covered IHC's outstanding eligible internal LTD amount must equal the greater of 7% of risk-weighted assets or 4% of average total consolidated assets.

- *The Board invites comment on the appropriateness of subjecting eligible internal LTD to the same requirements as apply to eligible external LTD. (Question 34 of the proposal)*

Comments:
The calibration of minimum TLAC and LTD requirements for IHCs is inconsistent with the methodology used to calibrate the corresponding requirements applicable to covered BHCs and does not incorporate an adjustment for balance-sheet depletion. Specifically, it appears that the minimum risk-weighted LTD ratio applicable to IHCs was not reduced by a 1 percentage point allowance to reflect expected balance-sheet depletion the way the corresponding ratio for covered BHCs has been. As a result, covered IHCs, including SHUSA, would be required to maintain LTD equal to at least 7% of their risk weighted assets (RWAs), while the analogous requirement for Covered BHCs sets the minimum at 6% of RWAs.

We observe the Board's rationale for providing all covered BHCs with a uniform 1 percentage point allowance for balance-sheet depletion is that such an allowance "is appropriate under the capital refill theory because the losses that the covered BHC incurs leading to its failure will deplete its risk-weighted assets as well as its capital. Accordingly, the pre-failure losses would result in a smaller balance sheet for the covered BHC at the point of failure, meaning that a smaller dollar amount of capital would be required to restore the covered BHC's pre-stress capital level."[16]

Resolution entity IHCs are expected to enter U.S. bankruptcy or Title II proceedings and be resolved just like a covered BHC, and there is no material difference between covered BHCs and resolution entity IHCs as far as any expected balance sheet depletion is concerned at the point of failure and entry into resolution. As such, we believe it is reasonable for the Board to reduce the minimum risk-weighted LTD ratio applicable to resolution entity IHCs by a 1 percentage point allowance to reflect expected balance-sheet depletion the same way the corresponding ratio for covered BHCs has been calibrated.

In order to preserve the principle of national treatment and promote a level playing field, the applicable internal LTD requirements should be calibrated based on the same methodology that

[16] Total Loss-Absorbing Capacity, Long-Term Debt, and Clean Holding Company Requirements for Systemically Important U.S. Bank Holding Companies and Intermediate Holding Companies of Systemically Important Foreign Banking Organizations; Regulatory Capital Deduction for Investments in Certain Unsecured Debt of Systemically Important U.S. Bank Holding Companies; Proposed Rule, 80 Fed. Reg. 229 (Nov. 30, 2015).

the Board used to calibrate the corresponding requirements applicable to covered BHCs, except for any G-SIB surcharges, unless the IHC has itself been designated as a G-SIB.

RECOMMENDATION: To the extent that an LTD requirement for covered IHCs is preserved in the final rule, we request the eligible internal LTD calibration for IHCs be based on the same methodology that the Board used to calibrate the corresponding requirements applicable to covered BHCs. This would result in a reduction of the minimum risk-weighted LTD ratio applicable to covered IHCs reflecting the 1% allowance for expected balance-sheet depletion under the capital refill framework.

IV. Regulatory Capital versus TLAC Requirements

The Board's proposal recognizes only "tier 1 regulatory capital (common equity tier 1 capital and additional tier 1 capital) issued from the covered IHC to a [foreign parent entity] and (b) the covered IHC's eligible internal LTD" as eligible instruments for purposes of meeting the TLAC requirements of covered IHCs. This proposal introduces a material divergence from the Final Basel III rules at 12 C.F.R. Parts 208, 217 and 225 , under which all capital instruments, internal and external, count toward capital ratios, capital management, and CCAR stress testing requirements.

Comments:
The result of these diverging requirements for covered IHCs is that instruments which count toward capital ratios would not be eligible to count toward TLAC or LTD ratios, and vice versa. Upon implementation of the proposed rule, covered IHCs will be left with outstanding additional tier 1 (AT1) or tier 2 (T2) instruments that will continue to count for capital ratios but will not count for TLAC or LTD purposes. Regulatory capital instruments, even if externally issued, have been shown to have loss-absorbing capacity and, therefore, should count toward a covered IHC's TLAC or LTD requirements.

Furthermore, the Board's proposal does not state whether the issuance, servicing, and redemption of internal LTD would be deemed to be capital actions that need to be approved by the Board under its capital plan rule (12 C.F.R.225.8). We believe it is important that the Board provide clarification on this issue in its final rule.

RECOMMENDATION: We request that the final rule take steps to harmonize regulatory capital and TLAC capital requirements – reflecting the loss-absorbing capacity of both sets of instruments, whether issued internally or externally.

We also request that the Board provide greater clarity on the treatment of TLAC internal long-term debt instruments to clarify whether the issuance, servicing, and redemption of these instruments would be deemed to be capital actions that need to be approved by the Board under its capital plan rule (12 C.F.R.225.8.)

Conclusion

Santander appreciates the standard the Board has set for itself in its rulemaking approach to foreign banking organizations: "[to] remain mindful of the benefits that foreign banks can bring to our economy and of the important policies of national treatment and comparable competitive opportunity."[17] Equal treatment of foreign banking organizations from a prudential regulatory perspective was also a fundamental goal of the Board's EPS rulemaking: "By imposing a more standardized regulatory structure on the U.S. operations of foreign banks, we can ensure that enhanced prudential standards are applied consistently across foreign banks and in comparable ways between U.S. banking organizations and foreign banking organizations."[18]

Adoption of the above recommendations will not only demonstrate the Board's continuing commitment to this important standard but will also advance the shared goal of improving the resolvability and resiliency of banking organizations operating in the U.S. in a way that is reflective of covered entities' business model, resolution strategy, and risk profile. Such an approach will also help to ensure that credit availability for customers of covered institutions will not be unduly impacted or restricted by the imposition of overly burdensome capital requirements.

Santander is a retail bank whose purpose is to help people and businesses prosper. We thank you for the opportunity to comment on this proposal and to share the views of SHUSA. Please do not hesitate to contact me at (617) 646-2528.

Sincerely,

Jerry Plush
Chief Financial Officer
Santander Holdings USA, Inc.

17 Federal Reserve Board Governor Daniel K. Tarullo, "Regulation of Foreign Banks" (Yale School of Management Leaders Forum, New Haven, Connecticut, November 28, 2012).

18 Ibid.

Appendix 1

BCBS Systemic Importance Indicators Reported by Large U.S. Bank Holding Companies ($ billions)*

Bank Holding Company	Size	Interconnectedness			Substitutability			Complexity			Cross-Jurisdictional Activity		2013 SCORE (percent)
	Total exposures	Intrafinancial system assets	Intrafinancial system liabilities	Securities outstanding	Payments activity	Assets under custody	Underwriting activity	Amount of OTC derivatives	Adjusted trading and AFS securities	Level 3 assets	Foreign claims	Total cross-jurisdictional liabilities	
Weight (percent)	20	6.7	6.7	6.7	6.7	6.7	6.7	6.7	6.7	6.7	10	10	
JPMorgan Chase & Co.	3,570	422	544	599	321,458	21,320	508	68,004	446	69	693	674	5.05
Citigroup Inc.	2,895	421	513	596	300,783	11,096	331	59,472	130	46	839	742	4.27
Bank of America Corp.	2,696	294	220	489	83,705	136	390	54,887	203	32	387	246	3.06
Wells Fargo & Co.	1,961	110	129	508	28,761	2,400	86	4,880	128	37	70	130	1.72
Goldman Sachs Group, Inc.	1,518	337	107	310	9,585	866	371	50,355	138	43	347	319	2.48
Morgan Stanley	1,283	535	182	231	9,812	1,369	262	43,611	316	23	353	470	2.60
U.S. Bancorp	525	11	22	139	6,918	959	17	106	13	4	3	34	0.35
PNC Financial Services	425	18	13	68	2,004	161	10	252	26	11	5	2	0.30
Bank of New York Mellon Corp.	410	79	230	61	166,279	23,590	6	1,158	39	0	87	164	1.50
HSBC N.A. Holdings Inc.	406	36	55	50	1,061	43	49	5,194	40	4	43	1	0.38
State Street Corp.	345	30	209	43	59,122	20,411	-	1,141	54	8	47	125	1.48
Capital One Financial Corp.	336	14	2	94	914	3	2	63	16	4	9	2	0.19
TD Bank U.S.	277	15	5	8	2,393	10	-	151	18	2	35	1	0.14
SunTrust Banks, Inc.	229	3	1	50	644	64	11	183	15	3	2	2	0.14
BB&T Corp.	212	1	10	69	972	35	6	59	4	2	1	1	0.12
American Express Co.	177	7	37	162	144	-	-	42	4	-	30	20	0.17
Fifth Third Bancorp	174	4	9	38	1,187	240	5	64	7	0	4	1	0.10
BMO Financial Corp.	163	16	1	26	5,245	257	8	22	11	0	7	6	0.12
Ally Financial Inc.	153	6	17	108	290	-	-	62	9	0	2	2	0.11
UnionBanCal Corp.	146	10	6	20	1,058	120	-	64	8	2	2	3	0.09
RBS Citizens Financial Group, Inc.	146	4	4	1	2,816	7	-	43	1	0	2	1	0.05
Regions Financial Corp.	146	1	7	27	755	22	45	74	5	0	1	0	0.11
Northern Trust Corp.	142	44	12	16	32,997	5,576	-	255	12	0	28	51	0.49
Key Corp.	134	6	1	26	984	82	5	62	2	3	2	0	0.08
M&T Bank Corp.	105	2	5	22	1,594	101	26	21	1	0	0	0	0.08
Bancwest Corp.	103	1	8	12	443	3	-	16	1	0	1	1	0.04
BBVA Compass Bancshares, Inc.	101	4	2	13	199	3	80	18	1	0	1	2	0.12
Santander Holdings USA, Inc.	98	4	0	12	24	-	-	18	12	0	4	1	0.05
Comerica Inc.	98	8	4	17	246	53	1	21	2	0	2	2	0.05
Discover Financial Services	96	7	0	74	321	-	-	12	1	0	0	0	0.06
Zions Bancorp.	75	3	3	11	437	3	0	3	3	1	0	2	0.04
Huntington Bancshares Inc.	65	2	0	16	303	80	1	8	3	1	1	-	0.04
Deutsche Bank Trust Corp.	64	20	26	12	58,495	-	-	14	0	0	4	0	0.20

* Basel Committee on Banking Supervision
Sources: Company Y-15 reports, OFR analysis