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June 03, 2016

Mr. Robert deV. Frierson, Secretary
Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Single-Counterparty Credit Limits for Large Banking Organizations

Docket No. R-1534, RIN 7100-AE 48

Ladies and Gentlemen:

Deutsche Bank AG ("**Deutsche Bank**") appreciates the opportunity to provide comments on June 3, 2016 to the Notice of Proposed Rulemaking entitled Single-Counterparty Credit Limits for Large Banking Organizations (the "**Proposal**") issued by the Board of Governors of the Federal Reserve System (the "**Board**").

Deutsche Bank supports efforts by the Board to minimize the impact a large banking organization failure would have on the financial system. We also recognize the need for a system that limits interconnectedness among large financial companies and appreciate the Board incorporating comments received on the earlier 2011[1] and 2012[2] proposals. Particularly, Deutsche Bank welcomes the Board's proposal to explicitly exempt credit exposures to (i) qualifying central counterparties ("**QCCPs**"), (ii) the United States ("**U.S.**") government or foreign sovereign entities that receive a zero percent risk weight under Regulation Q, and (iii) a foreign banking organization's ("**FBOs**") exposure to its home country sovereign. These will help maintain incentives for banks to hold high quality liquid assets, and continue moving derivatives exposures to centrally cleared venues.

[1] https://www.gpo.gov/fdsys/pkg/FR-2012-01-05/pdf/2011-33364.pdf

[2] https://www.gpo.gov/fdsys/pkg/FR-2012-12-28/pdf/2012-30734.pdf

In Deutsche Bank's view, several areas in the Proposal may benefit from the comments and recommendations that we put forth to the Board for consideration. Our comments are in addition to those highlighted in the response letters to the Proposal by The Clearing House ("**TCH**") and the Institute of International Bankers ("**IIB**"), which we broadly support. Below are broad thematic areas for consideration, while specific comments and suggestions can be found in the attached Annex.

- **The Proposal should support a level playing field for FBOs:** Under the Proposal, the U.S. operations of FBOs will be separately subject to two SCCL calculations: one at the intermediate holding company ("**IHC**") level and one at the combined U.S. operations level. Considering Deutsche Bank will be subject to a similar rule in the EU, implementing the Basel Committee on Banking Supervision ("**BCBS**") Large Exposures Framework[3], an SCCL that applies only to an FBO's U.S. IHC, based on IHC capital, would be more appropriate. If the Board maintains the requirement for FBOs to calculate the SCCL at the IHC and at the combined U.S. operations, then the Board should eliminate the cross-trigger mechanism, which mandates that neither the IHC nor combined U.S. operations be permitted to increase counterparty exposure if either breaches the limit.

- **Derivatives Calculation Methodology**: We believe that issues of complexity and unlevel playing field can be largely dealt with by delaying implementation of SCCL until the Standardised Approach for Counterparty Credit Risk ("**SA-CCR**") is finalized in the United States.[4] This avoids the need to build out an SCCL system based on an outdated Current Exposure Method ("**CEM**") methodology, and then rebuild the same system once the SA-CCR enters into force. It also mitigates building out a fragmented framework that would result in the unfair treatment of an FBO's IHC that will predominantly utilize the Standardized Approach ("**SA**") and use CEM while peer U.S. banks are able to use the Advanced Approach ("**AA**").

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[3] http://www.bis.org/publ/bcbs283.pdf

[4] http://www.bis.org/publ/bcbs279.pdf

- **Covered Company Consolidation:** U.S. Generally Accepted Accounting Principles ("**GAAP**") should be used for determining what entities are captured in credit exposure computations because it aligns SCCL with the U.S. Basel III risk based capital rules. Covered companies already have the required infrastructure to consolidate on this basis. The requirement to consider assets of a counterparty outside the regulatory consolidation group adds significant complexity and compliance costs, which will far outweigh any meaningful benefit from applying a broader covered company definition.

- **Calculation of Securities Financing Transactions ("SFT") exposures:** The Board should update the proposed calculation methodology for SFT exposures to the Standardized Approach for Credit Risk ("**SACR**") adopted by the BCBS.[5] SACR is a relatively straight-forward approach that balances enhanced risk sensitivity with simplicity by allowing for netting and diversification benefits, which are not currently available under the collateral haircut approach. Additionally, contrary to the U.S. Basel III risk based capital rules, which acknowledges the benefits of eligible collateral and its effect on counterparty risk, the Proposal requires that a covered company risk shift its exposure on a dollar for dollar basis to a collateral issuer regardless of the quality of the eligible collateral. At a minimum, the covered company should be allowed to use its discretion whether it wants to reduce its exposure to the original counterparty and risk shift to the issuer of collateral.

- **Timing:** Ideally, the implementation of SCCL should align with the timing of the finalized U.S. Standardized Approach for measuring SA-CCR. However, if the Board decides to complete the SCCL Proposal prior to the U.S. SA-CCR finalization, we believe that two years should be provided from the rule's effective date to comply (instead of the one year proposed for Large and Major covered companies) in order to allow sufficient time for implementation.

[5] http://www.bis.org/bcbs/publ/d347.pdf

- **Special Purpose Vehicle ("SPV") look-through approach:** Under the Proposal, large and major covered companies are required to look-through to the issuer of assets held by a securitization vehicle, investment fund, or other special purpose vehicle (collectively "SPV") if their exposure to the SPV exceeds one quarter percent (0.25%) of the respective capital base. While we appreciate the Board's inclusion of a de minimis threshold, we believe that large and major covered companies should only be required to look-through the issuer of assets held by an SPV where its exposure to the SPV is greater than the higher of: a half percent (0.5%) of the respective eligible capital base; and $50 million. We believe this alternative approach would more accurately capture those exposures to SPVs that may pose an actual material risk to the financial system.

- **Counterparties:** The Board appropriately includes a five percent (5%) materiality threshold for the economic interdependence test, and the same threshold should apply to the control relationship test. It is our view that counterparties that fall below the five percent (5%) threshold would not be material enough to put the covered company or the financial system at risk.

- **Daily Compliance Requirement:** Based on the complexity of the Proposal's look-through approach and Bank Holding Company Act ("**BHCA**")[6] counterparty consolidation approach, demonstrating daily compliance with the look-through approach for SPVs would impose significant costs and be a considerable challenge from an operational perspective. Because the composition of SPVs is typically only reported on a monthly basis or, in certain instances, on a less frequent basis, we believe that a compliance review on a monthly basis or when information becomes available with respect to changes in the SPV's composition is more appropriate.

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[6] 81 Fed. Reg. at 14,346

Deutsche Bank appreciates the opportunity to provide the Board with the foregoing comments and recommendations regarding the Proposal.

Respectfully submitted,

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ANNEX to Deutsche Bank's Comment Letter Dated June 03, 2016

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1. The Proposal should support a level playing field for FBOs

We agree with the points made in the IIB's response letter that the Proposal should support a level playing field for FBOs. The SCCL requirements of the Proposal fails to meet the Congressional mandate, set forth in Sections 115(b)(2)(A) and 165(b)(2)(A) of the Dodd–Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank Act**"), that the Board give due regard to national treatment and equality of competitive opportunity for FBOs. Under the proposal, the U.S. operations of FBOs will be subject to two distinct and simultaneous SCCL calculations (one at the IHC and one at the combined U.S. operations). Further, we note that the Proposal provides no background or justification for the enhanced SCCL requirements for FBO entities.

Considering Deutsche Bank will be subject to a similar rule in the EU, implementing the BCBS Large Exposures Framework[7], these multiple calculations and requirements would be burdensome. As such, an SCCL that applies only to an FBO's U.S. IHC, based on IHC capital, would be more appropriate. In addition to the operational and compliance challenges FBOs would face in implementing two SCCLs, there would be additional costs for FBOs to implement a second SCCL at the combined U.S. operations, which U.S. Bank Holding Companies ("**BHC**") would not face. We question the beneficial use of the monitoring of these results at the combined U.S. operations for risk management purposes and we ask you to reconsider how the SCCL proposal can be modified to more appropriately take into account Dodd-Frank Sections 115(b)(2)(A) and 165(b)(2)(A). Additionally, as stated in the March 4, 2016 Board Memo[8], we believe the Board should include language in the Final Rule that the calculation of IHC and combined U.S. operations' exposures to the foreign bank parent are excluded.

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[7] http://www.bis.org/publ/bcbs283.pdf

[8] https://www.federalreserve.gov/aboutthefed/boardmeetings/sccl-board-memo-20160304.pdf

Cross-trigger mechanism

If the Board maintains the requirement for FBOs to calculate the SCCL at the IHC and at the combined U.S. operations, then the Board should eliminate the cross-trigger mechanism. Under the Proposal the Board includes a cross-trigger mechanism that mandates that neither the IHC nor combined U.S. operations be permitted to increase counterparty exposure if either breaches the limit. Considering the higher capital base for the combined FBO entity (i.e. parent capital), there appears to be no logical basis for the requirement in the Proposal that a breach by the IHC, based on the IHC's capital base, should limit the combined U.S. operations from engaging in additional credit transactions provided there is no breach based on the higher FBO capital limit for the combined U.S. operations.

2. Derivatives Calculation Methodology

The Preamble of the Proposal states that the Board may consider the inclusion of the SA-CCR that was finalized by the BCBS in March 2014.[9] We agree that the SA-CCR should be the basis for the exposure measure. As the Board has previously stated,[10] SA-CCR is designed to be a more risk-sensitive measure than CEM.

Accordingly, to maintain consistency with the BCBS standard for calculating derivatives exposures, we believe it is not prudent to implement SCCL until the SA-CCR is finalized in the United States. This avoids the need for FBO entities to build a framework that initially relies on CEM for derivative exposures only to have to re-build a SA-CCR based framework at a later date.

Additionally, the current proposal would result in a fragmented implementation where certain banks can use Advanced Approaches ("**AA**") internal modeling while others would be subject to CEM. In order to support a level playing field for FBOs and non-AA banks, the Board should delay the implementation of SCCL until SA-CCR is finalized in the United States and only allow for the use of one consistent methodology across all banks to measure derivative exposures.

[9] http://www.bis.org/publ/bcbs279.pdf

[10] https://www.federalreserve.gov/mediacenter/files/open-board-meeting-transcript-20160304.pdf

3. Covered Company Consolidation

We believe GAAP financial reporting consolidation is the most logical approach for determining the exposures of the covered company. The Proposal uses the BHCA control definition as the method for determining what subsidiaries are included as part of the covered company. The BHCA control definition is much broader than what is required for GAAP consolidation under the U.S. Basel III risk based capital rules. Using the BHCA definition for covered company would lead to inconsistencies between prudential risk management efforts, as well as posing an implementation challenge for the covered companies.

Regarding implementation, the aggregation of exposures of entities that are not consolidated for risk-based capital purposes would be a significant challenge and is not easily adaptable. Under GAAP, where a bank controls a company, it would financially consolidate and typically assume operational control over the company. Further, the company is integrated into the bank's processes in such a way that allows for monitoring of that company's credit exposures. However, where a company may be "controlled" under the BHCA, the bank may have certain governance rights and access to information to ensure its responsibilities are fulfilled under the BHCA. However, where the bank only has a minority investment, it is unlikely that the bank will fully integrate such a minority subsidiary into its day-to-day operations, management and reporting framework. As such, it will be extremely cumbersome to set up a new manual process to monitor all of the credit exposures of such a minority entity to all of the entity's counterparties. Further, including exposures of a company the bank does not control will result in overstating the amount of maximum potential loss the covered company would be subject to.

Therefore, our view is that the exposures of a covered company should be based on credit exposures of subsidiaries that are consolidated under GAAP for U.S. regulatory capital purposes. Using GAAP would leverage existing architecture and ensure that the most important entities are captured. This also avoids the building out of a separate system for consolidating entities for covered companies.

Consolidation under the BHCA would also create inconsistencies within the Proposal. The capital base used to measure exposure against is based on GAAP consolidation under the U.S. Basel III risk based capital rules, whereas the exposure is based on BHCA consolidation. The fundamental formula governing SCCL, therefore, will have a misaligned numerator and denominator.

Finally, we support the statement made in the TCH comment letter around the evasion concern raised in the Preamble, and do not believe it necessitates incorporation of the BHCA control standard.[11]

4. Calculation of SFT Exposures

The Board should adopt the new SFT exposure measurement methodology introduced in the BCBS SACR. While being a simple method to implement, the Board's proposed collateral haircut method is non-risk-sensitive, and overly conservative, as it does not allow for recognition of any diversification benefits. In contrast, the SACR approach combines the Board's criteria of enhanced risk sensitivity and transparency while continuing to be relatively simple to implement.

Under the U.S. Basel III risk based capital rules, Section 36[12] requires banks to reduce the value of collateral by incorporating a maturity mismatch haircut which under the U.S. Basel III risk based capital rules is only applicable to guarantees and credit derivatives in certain circumstances. No maturity mismatch requirement exists for collateralized transactions that qualify for the collateral haircut approach (Section 37[13]). The Proposal, however, introduces the maturity mismatch requirement for repo-style and collateralized derivative transactions. The Proposal does not include an explanation for the departure from the risk-based capital rules and it appears unintentional and unwarranted. Therefore, covered companies should be permitted to use the collateral haircut approach as stated in the risk-based capital rules (subject to the restrictions set forth in section 252.74 (b)(1) and (2) of the proposal).

In general, we agree with the Board's approach to align exposure measurement methodologies in the Proposal with the exposure measurement in the risk based capital framework. We note that where a transaction qualifies for the collateral haircut approach under the U.S. Basel III risk based capital rules (limited to exposures that meet the strict regulatory definition of a repo-style transaction, eligible margin loan, or over the counter derivative), eligible collateral subject to haircuts are used to reduce the exposure to the original counterparty and there are no additional

[11] 81 Fed. Reg. at 14,331.

[12] https://www.gpo.gov/fdsys/pkg/FR-2013-10-11/pdf/2013-21653.pdf

[13] Idem

risk weight charges for qualifying collateral. This preferential treatment under the capital rules is based on the fact that the transactions are conducted under an agreement that provides the covered company the right to accelerate and terminate the contract and liquidate the collateral promptly upon an event of default. Additionally, the exposure must be margined on a daily basis by eligible collateral that is liquid and readily marketable.

Contrary to the U.S. Basel III risk based capital rules, which acknowledges the benefits of eligible collateral and its effect on counterparty risk, the Proposal requires that a covered company risk shift its exposure on a dollar for dollar basis to a collateral issuer regardless of the quality of the eligible collateral. As a result, the one for one risk shifting may disincentive a Bank from obtaining high grade liquid collateral to reduce its exposure to the original counterparty given the lack of sensitivity to the quality of collateral. The methodology appears to make no distinction between an uncollateralized loan versus a collateralized secured funding transaction, and there appears to be no significant benefit to the covered company by way of a reduction in the amount of risk-shifing required.

To avoid a situation where all the underlying collateral is concentrated in limited number of counterparties, it may be appropriate to have certain threshold requirements to measure such concentration instead of requiring that the covered company risk shift to the collateral issuers in all cases. Further collateral may be substituted by the counterparty (subject to Credit Support Annex terms) on a daily basis. It will be operationally challenging, however, to track exposures to individual collateral counterparties on a daily basis. At a minimum, the covered company should be allowed to use its discretion whether it wants to reduce its exposure to the original counterparty and risk shift to the issuer of collateral.

5. Timing

For Large and Major Covered Companies, the Proposal provides one year for implementation following the finalization of the rule. We believe the Board should align the timing of SCCL implementation so it coincides with the finalization of SA-CCR in the U.S. This would support a level playing field for FBOs by ensuring all banks use one consistent methodology for calculating derivative exposures.

If the implementation of SCCL is not aligned with finalization of SA-CCR in the U.S., then we believe two years from the finalization of SCCL would provide a more appropriate time frame to operationalize the complexities introduced by the rule.

6. SPV Look-Through Approach

Under the Proposal, large and major covered companies are required to look-through to the issuer of assets held by an SPV if their exposure to the SPV exceeds a quarter percent (0.25%) of the respective capital base. The requirement to look-through presents a number of operational challenges (outlined in more detail in the THC response) namely:

- Underlying data for SPVs is not typically produced on a daily basis and is generally not of sufficient granularity as required by the Proposal. This data challenge is compounded by the requirement to bucket unknown issuers of underlying assets into a single bucket and will, most likely, result in the majority of underlying issuers being attributed to this bucket.
- The look-through calculation examples provided in the Preamble of the Proposal present a very oversimplified picture of the calculation. In reality, SPVs will have a large number of underlying assets - each of which is unlikely to materially contribute to the company's exposure to a particular counterparty.

Further, we do not support the look through calculation methodology for a typical SPV as it results in exposures to individual underlying assets of the SPV that are in total greater than the company's exposure to the SPV. Increasing the limit as proposed below will reduce the number of instances where this will be realized.

- For example, if the company has a $5 exposure to an SPV (fifty percent (50%) pro rata share in a $6 senior tranche and fifty percent (50%) pro rata share in a $4 junior tranche) and that SPV invests $3 in bonds issued by company A and \$7 in bonds issued by company B, gross exposure to company A = \$3[14] and gross exposure to company B is \$5[15], which in total (\$8) is greater than our initial \$5 exposure to the SPV.

- The look-through requirement is agnostic to the underlying assets of SPV (e.g., retail, commercial, corporate). This is unnecessarily onerous, particularly in the instance of retail exposures, such as credit card or auto loan receivables, where the underlying assets are exposures to natural persons which would never conceivably approach the SCCL limit.

We fully support the TCH advocacy points around the SPV look-through approach, including:

- Exemptions from the look-through requirement for exposures to certain categories of SPVs altogether based on their structure, the granular nature of their underlying assets or the regulatory regime to which they are subject. In particular, we support the exemption of commercial mortgage backed-securities and retail asset-backed securities; and

- Requiring a look-through only in cases of exposures arising from the company's investment in SPVs limited to cash investments and synthetic positions in SPVs, as well as extensions of credit and liquidity facilities provided to SPVs.

Additionally, we propose an alternative approach to the application of the quarter percent (0.25%) look-through threshold. While we support the Board's efforts to reduce any undue burden on the requirement to apply the look-through approach, we believe, given the difficulties highlighted above and in the TCH letter, the quarter percent (0.25%) threshold would still capture a large population of SPVs for the majority of large and major covered companies. Therefore, we believe that look-through approach should only apply to the issuer of assets held by an SPV where its exposure to the SPV greater than the higher of:

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[14] Gross credit exposure to company A from senior tranche = 50% x Min (\$6, \$3) = \$1.5 ; Gross credit exposure to company A from junior tranche = 50% x Min (\$4, \$3) = \$1.5

[15] Gross credit exposure from company B to senior tranche = 50% x Min (\$6, \$7) = 3 ; Gross credit exposure to company B from the junior tranche = 50% x Min (\$4, \$7) = \$2

- Half percent (0.5%) of eligible capital base; and
- $50 million

For example, if our exposure to the SPV was $35 million and a half percent (0.5%) of the eligible capital base is $30 million, then we would not apply the look through because, although the exposure is greater than a half percent (0.5%) of the capital base, it is lower than $50 million.

The increased threshold will reduce the operational cost and complexity, while the "higher of" function will relieve the burden particularly on large and major covered companies with a relatively smaller capital base.

7. Counterparties

The definition of a counterparty in the Proposal includes all persons of which such company owns twenty-five percent (25%) or more of voting rights or total equity, as well as the additional requirement to look at influence over appointment or dismissal of management/governing body, and influence over policies. This requirement as proposed by the Board would result in significant operational challenges and the aggregation of exposures that are not considered interconnected. We believe a financial consolidation standard, such as BCBS Large Exposures Regime[16] approach, would be an appropriate alternative to the Proposal and would capture the majority of counterparties that are economically interconnected. As noted in the TCH response letter, this would ensure that the Proposal is aligned more closely with international standards and allow covered companies to align compliance mechanisms across global borders.

We support the five percent (5%) threshold for economic interdependence test and believe the same threshold should be incorporated in to the control relationship test. Counterparties that fall below the five percent (5%) threshold will not be considered large enough so as to pose a threat to the stability of the covered company and consequently the financial system. For the control relationship test, a covered company would be required to investigate for each counterparty with which it has a credit exposure whether it is connected to another counterparty based on the presence of voting agreements, the ability to select the majority of the members of the

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[16] http://www.bis.org/publ/bcbs283.pdf

governing body, or the ability to exercise a controlling influence over such other entity. It is questionable whether all the information required to perform the connected counterparties tests is publicly available and updated on a daily basis to allow for the tests to be performed accurately. At a minimum, for determining where a control relationship exists, the Board should use the BCBS threshold[17] of fifty percent (50%) (BCBS control relationship is satisfied if one entity owns more than fifty percent (50%) of the voting rights of the other entity, while the Board proposes a twenty-five percent (25%) threshold).

8. Daily Compliance Requirement

Given the complexities highlighted above, we believe the daily compliance requirement constitutes a significant operational challenge with respect to the look-through approach for SPVs. First, the daily compliance requirement for SPV look-through approach would be operationally challenging and would impose significant costs to monitor the daily changes in SPV composition. Additionally, because the composition of SPVs is typically only reported on a monthly basis or, in certain instances, on a less frequent basis, we believe reporting on a best efforts basis (e.g., if we can demonstrate an attempt to obtain the information) is more appropriate. A parallel for differing timing requirements can be drawn from the Leverage Ratio Rule where on-balance sheet items are required to be reported on a daily basis, whereas off-balance sheet items have a monthly averaging requirement.

Second, as noted above, the BHCA counterparty consolidation approach featured in the Proposal would pose an implementation challenge for Banks as it would be difficult to monitor all credit exposures of such entity to all of the entity's counterparties on a daily basis. Instead, GAAP should be used as the financial consolidation methodology, which would leverage existing architecture and help facilitate the monitoring and reporting of exposures for compliance purposes.

In accordance with the BCBS Large Exposures Regime reporting requirement[18], we believe any breaches to the Proposal's credit exposure limits should be promptly reported to the Board and rectified immediately. However, we do not believe a formal, daily compliance requirement is necessary for the SPV look-through

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[17] Idem

[18] http://www.bis.org/publ/bcbs283.pdf

approach given the complexity involved with the approach. At a minimum, it is our view that compliance should be required on a monthly basis or when information becomes available with respect to changes in the SPV's composition.

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