



INSTITUTE OF INTERNATIONAL BANKERS

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regs.comments@federalreserve.gov

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

Re: Proposed Revisions To Federal Reserve Board Form FR Y-7
(OMB Control Number 7100-0297)

Dear Mr. Frierson:

The Institute of International Bankers (“**IIB**”) appreciates the opportunity to comment on the recently proposed revisions to Form FR Y-7 (Annual Report of Foreign Banking Organizations).¹ The IIB’s membership is comprised of banks headquartered outside the United States which engage in a variety of banking and other financial activities in the United States. IIB member banks comprise virtually the entirety of the FR Y-7 reporting panel.

The Proposal would add new Report Item 5 to the FR Y-7 to collect information from a foreign banking organization (“**FBO**”) on its compliance with applicable U.S. risk committee and home country capital stress testing requirements under Regulation YY, promulgated by the Board of Governors of the Federal Reserve System (the “**Board**”) pursuant to Section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“**Section 165**”).² The applicable requirements under Regulation YY are effective as of July 1, 2016, and the proposed revisions to Form FR Y-7 would be reportable effective with fiscal year-ends beginning September 30, 2016.³

¹ 80 Fed. Reg. 75457 (Dec. 2, 2015) (the “**Proposal**”).

² 79 Fed. Reg. 17240 (March 27, 2014).

³ Thus, for example, an FBO with a September 30, 2016 fiscal-year end would be required to complete Report Item 5 for the FR Y-7 it must submit by January 31, 2017, and an FBO with a December 31, 2016 fiscal-year end would be required to complete Report Item 5 for the FR Y-7 it must report by April 30, 2017.



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Specifically, the Proposal is intended to facilitate implementation of the following requirements of Regulation YY applicable to the following types of FBOs:

- FBOs with total consolidated assets of more than \$10 billion and less than \$50 billion
 - Section 252.122(a) – Compliance with home country capital stress testing requirements (Report Item 5(a))
- Publicly-traded FBOs with total consolidated assets of \$10 billion or more and less than \$50 billion
 - Section 252.132(a) – Annual certification of compliance with the U.S. risk committee requirement (Report Item 5(b))
- FBOs with total consolidated assets of \$50 billion or more but combined U.S. assets of less than \$50 billion
 - Section 252.144(a) – Annual certification of compliance with the U.S. risk committee requirement (Report Item 5(c))
 - Section 252.146(b) – Compliance with home country capital stress testing requirements (Report Item 5(d))
- FBOs with combined U.S. assets of \$50 billion or more
 - Section 252.158(b)(1)(i) and (ii), and (b)(2) – Compliance with home country capital stress testing requirements (Report Item 5(e))⁴

The Board proposes a standardized approach whereby an FBO would check either a “yes” or “no” box to indicate its compliance with those requirements to which it is subject and an “N/A” box to indicate those to which it is not subject.

Assessing it strictly from a reporting perspective, we support the simplicity of this approach and believe it has considerable utility.

However, as discussed below, with respect to implementing the Proposal, we have concerns regarding interpretive questions on certain of the underlying regulatory requirements and the Board’s supervisory expectations with respect thereto. Regarding the U.S. risk

⁴ It is our understanding that Report Item 5(e) does not extend to the information reporting requirements prescribed in Section 252.158(c), compliance with which is not addressed in Form FR Y-7. As discussed in connection with the adoption of Regulation YY, FBOs are accorded broad discretion in determining how to implement this reporting requirement. See 79 Fed. Reg. at 17306.



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committee requirement, there are questions about its composition and how it applies to “two-tier” board structures. There also is a lack of clarity regarding certain components of the home country capital stress testing requirement. These concerns are reinforced by the potential remedial actions to which an FBO could be subject for failure to satisfy the applicable requirements of Regulation YY. The impact of such actions could be especially severe with respect to the home country capital stress testing requirements.

We also raise below questions regarding other certification or reporting requirements under Regulation YY which present potential compliance challenges for FBOs but are not addressed by the Proposal – specifically, the following:

- For FBOs with total consolidated assets of \$50 billion or more, the requirement to certify their compliance with home country risk-based and leverage capital requirements (Section 252.143(a), applicable to such FBOs with combined U.S. assets of less than \$50 billion, and Section 252.154(a) of Regulation YY, applicable to those with combined U.S. assets of \$50 billion or more).
- For FBOs with total consolidated assets of \$50 billion or more but combined U.S. assets of less than \$50 billion, the requirement in Section 252.145(a) of Regulation YY to report annually the results of internal liquidity stress tests that meet the requirements prescribed by the Board.

To address these matters, we respectfully request that the Board:

- **before finalizing the Proposal, resolve the questions raised in this letter regarding U.S. risk committee and home country capital stress testing requirements; and**
- **publish for comment a proposal to implement the certification/reporting regimes for Sections 252.143(a), 252.145(a) and 252.154(a) of Regulation YY and, in connection therewith, clarify its expectations regarding FBOs’ compliance obligations with the underlying regulatory requirements.**

We believe that expeditious action on these matters is necessary in order to allay our members’ increasing compliance anxieties as the July 1, 2016 effective date for these requirements fast approaches.

DISCUSSION

Our consideration of the Proposal is informed by our general understanding that, consistent with fundamental principles of comity, the requirements of Regulation YY discussed in this letter are not intended to modify applicable home country requirements or to disrupt FBOs’ compliance with those requirements, an approach we strongly support. Rather, incorporating an FBO’s compliance with certain of its home country requirements into the



Regulation YY framework is intended to provide an additional frame of reference to facilitate the Board's regulation and oversight of the FBO's U.S. operations within the parameters of the Section 165 enhanced prudential standards.

A. The Importance of Resolving Interpretive Questions Regarding the U.S. Risk Committee

Each FBO subject to the applicable provisions of Regulation YY covered by the Proposal are required to maintain a "committee of its global board of directors (or equivalent thereof)" that, among other things, oversees the risk management policies of the FBO's combined U.S. operations. The interpretive question is whether this U.S. risk committee must be composed entirely of members of the FBO's global board or can be configured in other ways which appropriately take into account the size, scale and complexity of an FBO's combined U.S. operations, most effectively utilize the expertise of those most familiar with the risks of these operations and provide the Board assurance that the FBO's board of directors is devoting appropriate attention to and exercising proper oversight over these risks. A closely related question is how the requirement should be applied to those FBOs which, in accordance with applicable non-U.S. law, have a "two-tier" board structure—a supervisory board and a management/executive board.⁵

Resolving these questions is critically important to FBOs covered by the Proposal, and especially those whose U.S. operations are not complex (for example, their U.S. banking operations are conducted solely through a federal or state-licensed branch or agency and they have no or only very limited nonbanking operations in the United States) and whose U.S. "footprint" (however structured) is relatively small in absolute terms and is not material to their global operations. We recognize the critical need for FBOs to undertake appropriate risk management oversight of their U.S. operations and that an FBO's board of directors plays a key role in this process. However, a strict interpretation requiring that the U.S. risk committee be comprised exclusively of members of an FBO's global board in many instances would not conform to the corporate governance requirements and principles applicable to the FBO in its home country and the arrangements and practices implemented by the FBO pursuant thereto. The potentially disruptive impact of such an interpretation would be similar to the impact on a U.S.-headquartered banking institution were it required by the law of another country in which it conducts operations (regardless of their size, complexity and relative importance to the bank's global business) to establish a risk committee charged with oversight of the bank's risks in that country and populate that committee exclusively with members of its global board.

⁵ The same interpretive questions apply to FBOs with combined U.S. assets of \$50 billion or more which are not required to establish a U.S. intermediate holding company ("IHC") or, if they are, are able to elect, and elect, to maintain their U.S. risk committee as a committee of the global board of directors (or equivalent thereof). We note that these FBOs are not required under Regulation YY to certify to having a U.S. risk committee and therefore are not covered by the Proposal. Resolving the interpretive questions raised in this letter regarding the U.S. risk committee requirement nevertheless is of equal urgency to these FBOs.



As the July 1, 2016 effective date for Regulation YY draws nearer, there is a very real prospect that, notwithstanding that as a practical matter an FBO may have in place policies, procedures and practices that ensure effective oversight of its U.S. risks, these may not comply with the terms of a strict interpretation of the regulation and therefore would preclude the FBO from certifying its compliance on Form FR Y-7. We do not believe that such a triumph of form over substance is intended, nor would it promote the core purposes of the U.S. risk committee requirement.

B. The Need for Clarification of Certain Aspects of the Home Country Capital Stress Testing Requirement

As a preliminary matter, we believe consultation by the Board with relevant home country authorities regarding its expectations under Regulation YY for the country's capital stress testing regime would help to mitigate FBOs' concerns with this requirement and facilitate their compliance efforts. Any information the Board could share about its efforts and intentions in this regard, whether in connection with finalizing the Proposal or otherwise, would be greatly appreciated.

Similarly, FBOs would benefit from clarification and guidance regarding the intended relationship between this requirement under Regulation YY and the Internal Capital Adequacy Assessment Process ("ICAAP") an FBO implements in accordance with applicable home country requirements. For example, is satisfactory completion of such an ICAAP review sufficient to meet the requirements of Regulation YY and thus enable an FBO to report it is in compliance on Form FR Y-7?

In addition to the foregoing considerations, we respectfully request clarification of the following specific aspects of the home country capital stress testing requirement:

- The home country capital stress testing regime must include the following requirements as prescribed in Regulation YY:
 - Stress testing must be conducted annually.

We have two questions regarding this requirement:

- We understand that in certain jurisdictions capital stress testing is required, whether conducted by the relevant home country supervisor or by the FBO (and then evaluated and reviewed by the supervisor), but not on an annual basis. In these cases, an FBO would simply be unable to comply with Regulation YY as the result of circumstances entirely outside its control. What are the Board's expectations for how such FBOs should respond to the applicable parts of Report Item 5?



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In connection with its adoption of Regulation YY the Board considered comments asking that it allow for a multi-year rather than annual stress test cycle and set forth its reasons for retaining the annual requirement.⁶ Where an FBO's noncompliance with the home country capital stress testing requirements of Regulation YY is attributable to the fact that such testing is not required to be conducted on an annual basis, we would urge the Board to take a flexible approach when considering any potential remedial actions.

- Whether or not conducted annually, what is the appropriate point of reference for purposes of responding to the applicable provisions of FR Y-7, Report Item 5? Presumably, it is intended that the response refer to the most recently completed capital stress test, whether or not that test was completed within the period covered by the FR Y-7.
- There must be “requirements for governance and controls of stress testing practices” by relevant management and the board of directors.
 - In adopting Regulation YY the Board indicated its intention that FBOs be permitted to apply these requirements flexibly.⁷ We support this approach, which presumably allows FBOs to exercise their reasonable discretion in determining how to respond to the relevant parts of Report Item 5.
- The FBO must “meet any minimum standards set by its home-country supervisor with respect to the stress tests.”

As with applicable governance and controls, presumably the Board intends to allow FBOs to exercise their reasonable discretion in determining how to respond to the relevant parts of Report Item 5, but clarification on both of these points would facilitate FBOs' compliance efforts.

C. Other Reporting/Certification Requirements under Regulation YY

1. Compliance with Home Country Risk-Based and Leverage Capital Requirements

Regulation YY prescribes two separate requirements in this area. First, FBOs must provide the Board reports relating to their compliance with home country capital adequacy

⁶ See 79 Fed. Reg. at 17305.

⁷ *Id.*



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requirements. It is our understanding that the Board has implemented this requirement through previously-adopted revisions to Form FR Y-7Q.⁸

Second, the FBO must certify to the Board that it meets applicable home country capital adequacy standards on a consolidated basis. Regulation YY does not prescribe the frequency of such certification (presumably, it is annual), its as-of date or the means by which the certification is to be made. We respectfully, but urgently, request the Board to clarify these questions and issue for comment its proposal for implementing the certification requirement.

Regarding the substantive underpinnings for the certification, and in particular the question of whether home country standards are consistent with the Basel Capital Framework, the Board has helpfully explained that it does not intend to require a one-to-one correspondence with that framework and instead intends to consider materiality when assessing consistency with the Basel Capital Framework and also will take into account the results of the Basel Committee's peer review process.⁹

We support this approach, which presumably allows FBOs to exercise their reasonable discretion in making the required certification. In this regard, we believe that a finding by the most recently-completed peer review that a home country's standards overall are compliant with the Basel Committee Framework should be sufficient (but not necessary) to enable an FBO from that country to certify its compliance with the applicable requirements of Regulation YY that are within the scope of the review. The FBO otherwise should be permitted reasonable discretion to determine whether it can provide the required certification.

As with the home country capital stress testing requirements discussed above, we believe consultation between the Board and a home country authority regarding any concerns the Board may have with the consistency of the home country's standards with the Basel Capital Framework would be helpful. In addition, should such concerns arise, we would urge the Board to take a flexible approach when considering any potential remedial actions related to an FBO's certification.

2. Compliance with Internal Liquidity Stress Testing Requirements

As an initial matter, we note that Regulation YY requires only that the results of the prescribed internal liquidity stress test be reported annually; an FBO is not required to have "passed" the test in any manner. That said, it is unclear what is intended to constitute the "results" of the test and, accordingly, what an FBO is required to provide in order to comply with the requirement. This latter consideration is complicated by the prospect that an FBO might be restricted or prohibited under home country law from disclosing the results of such test (or some

⁸ See too 79 Fed. Reg. at 17284.

⁹ See 79 Fed. Reg. at 17284.



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parts thereof) to the extent they are treated as the equivalent of confidential supervisory information.

FBOs are provided a welcome degree of flexibility in that the test must be consistent with the Basel Committee principles for liquidity risk management – the determination of which presumably is left to the FBO’s reasonable discretion – and the FBO may choose as it sees fit to apply the test to its consolidated operations or its combined U.S. operations. Regarding the scope of the test it is unclear, however, whether the FBO is restricted (or prohibited) from conducting the test on the basis of its consolidated operations one year and subsequently on the basis of its combined U.S. operations and vice versa.

Our principal concern is the additional requirement that the test must incorporate 30-day, 90-day, and one-year stress-test horizons. It is our understanding that not all jurisdictions that require internal liquidity stress testing specifically require these three time horizons. In this regard, the requirement appears to be significantly more prescriptive, and to pose a greater risk of conflicting with applicable home country requirements (particularly with respect to the FBO’s consolidated operations), than the home country capital stress testing requirement.

The potential extraterritorial overreach of this requirement is of keen concern to those of our members subject to the reporting mandate, and we respectfully request that the Board clarify its expectations and whether these highly prescriptive provisions of the regulation are intended to apply equally regardless of whether stress testing applies to an FBO’s consolidated operations or only its combined U.S. operations. For example, is it intended that the three prescribed time horizons are required only where the internal stress testing is based on the FBO’s combined U.S. operations and that those based on consolidated operations may be reported on the basis of home country standards that the FBO reasonably determines are consistent with the Basel Committee principles?

We believe that the prospect that an FBO might be found in noncompliance with this requirement because its home country standards do not track the strict requirements of Regulation YY (assuming that is the intended interpretation of the requirements) – a matter outside the control of the FBO – should be given significant weight in the determination of any potential remedial action that might be taken for noncompliance.

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We appreciate the Board's consideration of our comments on the Proposal and would welcome the opportunity to discuss them further. Please contact the undersigned if we can be of further assistance.

Sincerely,

A handwritten signature in black ink, appearing to read 'Richard Coffman', written in a cursive style.

Richard Coffman
General Counsel

cc: Jack Jennings
Kwayne Jennings
Board of Governors of the Federal Reserve System
Division of Banking Supervision and Regulation

Kevin Stiroh
Patricia Meadow
Federal Reserve Bank of New York