May 29, 2020

Via Electronic Submission

Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC, 20551

Re: Regulatory Capital Rule: Temporary Exclusion of U.S. Treasury Securities and Deposits at the Federal Reserve Banks from the Supplementary Leverage Ratio[1]

Dear Ladies and Gentlemen:

The Securities Industry and Financial Markets Association ("**SIFMA**")[2] appreciates the opportunity to comment on the Board of Governors of the Federal Reserve System's (the "**Federal Reserve**") interim final rule providing a temporary exclusion from the Supplementary Leverage Ratio ("**SLR**") for U.S. Treasury securities and deposits at the Federal Reserve Banks (the "IFR").

We support the Federal Reserve's strong and multifaceted response to the COVID-19 crisis, which poses unique and unprecedented challenges for communities, businesses, households and individuals. The Federal Reserve's timely interventions, including through the establishment of emergency lending programs, have helped to contain the impact of economic and market disruptions associated with the COVID-19 crisis. The IFR complements these wider efforts and increases the capacity of large U.S. bank holding companies and intermediate holding companies of foreign banks to extend credit and make markets at this critical time. Accordingly, we support the IFR.

This letter responds to the questions raised in the IFR reflecting the views of 19 SIFMA member firms subject to the SLR. Based on our members' asset mixes, business strategies and

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[1] Docket No. R-1707; RIN 7100-AF81.
[2] SIFMA is the leading trade association for broker-dealers, investment banks, and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly 1 million employees, we advocate on legislation, regulation, and business policy affecting retail and institutional investors, equity and fixed income markets, and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA).

organizational structures, the IFR impacts each firm differently. Consequently, our recommendations in this letter would not have uniform impacts across SIFMA member firms and may have greater relevance for certain firms.

The IFR is an appropriate response to the COVID-19 crisis and is consistent with safety and soundness

One of the immediate economic impacts of the COVID-19 crisis was a large increase in customer deposits received by strong banking organizations, including SIFMA's member firms. In the absence of the IFR, the SLR would have potentially limited the capacity of banking organizations to extend credit to the economy and deploy balance sheets in support of market-making, since any increase in deposit liabilities results in a corresponding increase in a firm's assets and total leverage exposure. The IFR appropriately encourages banking organizations to perform their critical deposit-taking role in our nation's economy. Since the IFR limits relief to deposits placed by banking organizations at Federal Reserve Banks, it is also consistent with safety and soundness, as such cash placements are effectively riskless exposures.

The COVID-19 crisis has also led to a wide-ranging response by the U.S. government, which has necessitated large increases in U.S. Treasury Department debt issuance. The U.S. Treasury Department has announced that, for the second quarter of 2020, it "expects to borrow $2,999 billion in privately-held net marketable debt, assuming an end-of-June cash balance of $800 billion. The borrowing estimate is $3,055 billion higher than announced in February 2020."[3] Primary dealers, including primary dealer subsidiaries of holding companies subject to the SLR, play a critical role in making markets in U.S. Treasury Department debt. Accordingly, the IFR's exclusion of U.S. Treasury securities removes a potential impediment that might otherwise impair market-making capacity. This exclusion is also consistent with safety and soundness, as any U.S. Treasury securities held by banking organizations pose effectively no credit risk.

Potential refinements to the IFR

As noted above, we support the IFR as well as the Federal Reserve's broader policy response to the COVID-19 crisis. We also applaud the Federal Reserve's swift decision to adopt the IFR as the COVID-19 crisis was unfolding in its initial weeks, which has facilitated banking organizations' ability to dynamically support customers and markets during a devastating economic period.

Our member firms have identified several areas where modest adjustments to, or expansions of, the IFR would be consistent, we believe, with the policy objectives of supporting the economy and protecting safety and soundness. While the impact of these potential adjustments

[3] U.S. Treasury Department, "Press Release: Treasury Announces Marketable Borrowing Estimates" (May 4, 2020), available at: https://home.treasury.gov/news/press-releases/sm997

varies by firm, we believe that they are all appropriate recommendations for the Federal Reserve[4] to consider as it calibrates its policy response to the COVID-19 crisis in the coming months.

- Expiry date. The relief in the IFR expires March 31, 2021, meaning that banking organizations will be required to include the full value of Federal Reserve Bank deposits and U.S. Treasury securities in their SLR exposures as of April 1, 2021. We are uncertain at this time whether economic conditions will have sufficiently stabilized and improved by the date. Instead of a fixed expiry date, the Federal Reserve might consider leaving the IFR relief in place until specified benchmarks or criteria are met. This approach might be paired with similar termination mechanisms for the Federal Reserve's emergency lending and asset purchase programs, which currently have variable termination dates.

- Transitional provisions. The IFR does not contain any wind-down transitional provisions. As a result, banking organizations will have full exclusions for Federal Reserve Bank deposits and U.S. Treasury securities through March 31, 2021, followed by a full inclusion beginning April 1, 2021. While it is difficult to predict the exact size of these excluded asset categories across SIFMA member firms months in advance, we expect that they will remain elevated through early 2021. Similar to transitional provisions included in a range of Federal Reserve capital rulemakings, we encourage the Federal Reserve to consider staggering the phase-in of excluded assets in the SLR when the IFR expires. A staggered phase-in would avoid abrupt "cliff effects" and permit banking organizations to manage their balance sheets in an orderly manner. A transitional provision would also improve the effectiveness of the IFR by reducing the possibility that banking organizations will take actions in late 2020 or early 2021 to mitigate the effect of an all-at-once March 31, 2021 expiry date.

- Repo-style transactions. Question 2 in the IFR asks whether the Federal Reserve should "exclude any specific repo-style transactions that would support banking organizations' role as financial intermediaries, and, if yes, why?" We believe that the IFR should exclude assets resulting from repo-style transactions to the extent such transactions are collateralized exclusively by U.S. Treasury securities. In practice, we expect that this exclusion would be most commonly applicable to reverse repurchase transitions collateralized by U.S. Treasury securities.

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[4] We recognize that the FRB, along with the other federal banking agencies, is taking other rulemaking and policy actions that may raise issues similar and adjacent to the points raised in this letter and the Interim Final Rule. This letter does not address any other rulemaking or policy actions, and SIFMA may separately comment on those matters in the future.

This exclusion can be justified on three grounds. First, a banking organization entering into a reverse repurchase agreement collateralized by U.S. Treasury securities has credit exposure, through the collateralization, to the U.S. Treasury Department. As such, conceptually, there is a strong basis for applying equivalent treatment to these exposures and to direct holdings of U.S. Treasury securities. Second, the historic and unprecedented increase in U.S. Treasury Department debt issuance may be expected to result in increases in the need for U.S. Treasury security financing arrangements, which could be met, in part, by banking organizations executing reverse repurchase transitions with clients and counterparties that are collateralized by these securities. Third, banking organizations commonly manage their liquidity reserves through a mix of direct holdings of U.S. Treasury securities and "reversing in" such securities through repo-style transactions. Extending the IFR to include repo-style transitions would recognize the similar liquidity risk profiles of the two categories.

- G-SIB Surcharge. U.S. GSIBs' institution-specific GSIB Surcharges are calculated based on FR Y-15 reporting data, which includes a size indicator. In the current environment, increases in banking organizations' Federal Reserve Bank deposits and U.S. Treasury securities holdings result, as is recognized by the IFR, from these organizations' roles as economic and market intermediaries, rather from risk-taking or other activities that pose systemic risk concerns. Accordingly, the exclusions recognized in the IFR should apply in equal measure to FR Y-15 reporting to avoid the possibility that SLR-excluded exposures will result in higher GSIB Surcharge requirements.

- Qualifying OECD central bank deposits. Question 2 in the IFR asks whether the Federal Reserve should "exclude deposits at certain foreign central banks"? We believe that the Federal Reserve should consider extending the IFR exclusion to qualifying OECD central bank deposits, for two reasons.

  First, extending the relief to qualifying OECD central bank deposits would recognize the global nature of COVID-19 impacts and the practical need for banking organizations to manage cash placements in major currencies. The Federal Reserve itself has taken strong actions to address currency pressures across major markets through its foreign central bank liquidity swap arrangements, which involves 14 major market central banks, including some non-OECD central banks. Extending the IFR relief to qualifying OECD central banks would similarly support banking organizations' ability to manage cash liquidity reserves throughout their global operations.

  Second, while exposures to the Federal Reserve and U.S. Treasury Department have a unique status in the U.S. prudential framework, exposures to OECD central banks involve similar characteristics. Similar to Federal Reserve Bank deposits and U.S. Treasury securities, U.S. Basel III assigns a zero percent risk-weight to OECD central banks.[5] Earlier this year, the Federal Reserve recognized an SLR exclusion for custody banks' deposits at "qualifying central banks," including qualifying OECD central banks.[6] This same definition and standard could be applied in an expansion to the IFR.

- Government National Mortgage Association securities. The regulatory capital framework generally applies the same treatment to the same categories of assets or exposures. Under U.S. Basel III, banking organizations apply a zero percent risk-weight to U.S. Treasury securities as well as to any other obligation that is "directly and unconditionally guaranteed by the U.S. government its central bank, or a U.S. government agency."[7] In practice, this category includes Government National Mortgage Association securities (GNMAs) but not obligations of certain other Government Sponsored Enterprises, which are generally subject to a 20 percent risk-weight.[8] We recommend that the Federal Reserve consider extending the IFR exclusion to GNMAs in recognition of their status in the regulatory capital framework as generally equivalent to U.S. Treasury securities.

Tier 1 Leverage Ratio considerations

The IFR limits its relief to the SLR without any corresponding adjustments to the Tier 1 Leverage Ratio. The Tier 1 Leverage Ratio includes the entirety of a firm's balance sheet assets, including Federal Reserve Bank deposits and U.S. Treasury securities. While the relative constraining effect of the SLR or Tier 1 Leverage Ratio will vary by firm, each ratio places absolute limits on a banking organization's balance sheet size.

We believe that the policy rationale in support of the IFR generally applies with equal force to the Tier 1 Leverage Ratio. Large inflows of customer deposits, or increased market-making in U.S. Treasury securities, may result in either SLR or Tier 1 Leverage Ratio constraints on particular banking organizations. While the Tier 1 Leverage Ratio has a distinct legal status, we encourage the Federal Reserve to consider extending SLR exclusions to the Tier 1 Leverage Ratio.

Conclusion

This is a unique and challenging moment. The Federal Reserve has taken a number of significant and important steps to support communities, businesses, households and individuals. Banking organizations have been a source of strength since the COVID-19 crisis began and have played a key role in extending credit, accepting deposits and marking markets. We believe that our recommendations in this letter would increase the capacity of the financial system to respond effectively to the current moment.

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[5] 12 C.F.R. § 217.32 Table 2.
[6] 85 Fed. Reg. 4569 (Jan. 27, 2020).
[7] 12 C.F.R. § 217.32(a)(1)(i).
[8] 12 C.F.R. § 217.32(a)(1)(ii).

In some areas, our comments in this letter overlap with SLR-related comments we have submitted to the Federal Reserve in recent years.[9] We believe it would be appropriate, at a future point, to consider the design and role of leverage ratios in the prudential framework, taking into account the experience and evidence of this crisis as well as broader, long-term policy objectives.

Respectfully submitted,

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President
SIFMA

[9] See, e.g., SIFMA comment letter on the calibration of the Supplementary Leverage Ratio (Oct. 21, 2013), *available at*: https://www.sifma.org/resources/submissions/sifma-and-other-associations-submit-comments-to-us-federal-regulators-on-the-proposed-leverage-ratio-rule/; SIFMA Statement on Liquidity Rules and Repo Market Volatility (Dec. 6, 2019), *available at*: https://www.sifma.org/resources/news/sifma-statement-on-liquidity-rules-and-repo-market-volatility/; SIFMA Statement on Changes to Supplemental Leverage Ratio (Nov. 19, 2019), *available at:* https://www.sifma.org/resources/news/sifma-statement-on-changes-to-supplemental-leverage-ratio/; SIFMA. Capital Markets Report—Modernizing and Rationalizing Regulation of the U.S. Capital Markets (Aug. 10, 2017), *available at*: https://www.sifma.org/wp-content/uploads/2017/08/Capital-Markets-Report-%E2%80%93-Modernizing-and-Rationalizing-Regulation-of-the-U.S.-Capital-Markets.pdf