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January 16, 2024

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, D.C. 20551
Attention: Docket No. R–1813, RIN 7100–AG64

Federal Deposit Insurance Corporation
550 17th Street NW
Washington, D.C. 20429
Attention: RIN 3064–AF29

Office of the Comptroller of the Currency
400 7th Street, SW, Suite 3E-218
Washington, D.C. 20219
Attention: Docket ID OCC–2023–0008

Re: Regulatory Capital Rule: Large Banking Organizations and Banking Organizations with Significant Trading Activity

Ladies and Gentlemen,

The Bank of New York Mellon Corporation (BNY Mellon) appreciates the opportunity to comment on the above-mentioned proposal to revise capital requirements applicable to large banking organizations and to banking organizations with significant trading activity (the Proposal).[1]

Established in 1784, BNY Mellon is a global company that delivers wealth management and investment services to institutions, corporations, and individual investors in 35 countries. BNY Mellon plays a critical role as a central orchestrator in the global financial ecosystem, touching more than 20% of investable assets globally. We are the world's largest custodian, with $48 trillion in assets under custody and/or administration (AUC/A). We clear about $10 trillion of securities and process over $2 trillion of payments per day, and we manage $2 trillion of assets on behalf of our Investment and Wealth Management clients.[2] Additionally, BNY Mellon's balance sheet is liabilities-driven and expands through the development of fee-based client-servicing relationships, not through asset growth like most consumer and commercial banks. Deposit liabilities and the related funding that come on to our balance sheet are driven by customer-related needs and not by our financing decisions or risk taking, and we currently have central bank placement assets that equal approximately one-third of our deposit liability levels. As a global systemically important bank (G-SIB), BNY Mellon would be subject to the proposed rule, and it is through this system-wide lens that we view the Proposal and form our comments.

We understand the importance of a well-capitalized banking system that works for all Americans. We also acknowledge that, following the 2008-2009 global financial crisis, regulators appropriately focused on implementing rules that increased both the quantity and quality of bank capital. As a result of the post-crisis Basel 3 framework and related measures, large US banking organizations hold sufficient capital to absorb losses under supervisory, idiosyncratic, and real-life stress scenarios.

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1 Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. 64028 (September 18, 2023).

2 Bank of New York Mellon Corporation. (January 12, 2023). *4Q23 Financial Results*. Retrieved from https://www.bnymellon.com/content/dam/bnymellon/documents/pdf/investor-relations/earnings-press-release-january-2024.pdf.

As Federal Reserve Board Chair Powell noted in his July 27, 2023 statement, the Federal Reserve Board (FRB), Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) (US federal prudential banking regulators, collectively the Agencies) are expected to "achieve an effective and efficient regulatory regime that keeps our financial system strong and protects our economy, while imposing no more burden than is necessary."[3] BNY Mellon's ability to provide essential financial services to US consumers, businesses, institutions, government agencies, and communities is dependent on well-calibrated regulation. To strike a more balanced approach, we believe that elements of the Proposal noted in this letter should be reconsidered.

I. US Banks are Strong, Resilient, and Well Capitalized

Since the 2008 financial crisis, US banks have more than doubled their common equity tier 1 capital (CET1) ratios, from 6.2% in 1Q 2009 to 12.9% in 2Q 2023.[4] Additionally, US G-SIBs have tripled their CET1 capital amounts over the same time period, from $297 billion to $914 billion.[5] Finally, since 2011 large US banks have been subject to annual supervisory capital stress testing, the "most risk-sensitive and dynamic component of the regulatory capital framework".[6] Results have consistently shown that large banks maintain capital well in excess of amounts required by the stress tests.[7]

In addition to minimum capital and stress capital requirements, large US banks comply with multiple additional post-crisis prudential requirements, including capital and liquidity stress testing; liquidity and resolution planning requirements; and rigorous governance, controls, risk management, and technology enhancements that have improved banks' operational resiliency and risk management. These measures complement the Agencies' regulatory capital framework and together strengthen banks' safety and soundness, and reduce systemic risk and threats to financial stability across the banking system.

US G-SIBs are already subject to the highest capital standards beyond Basel requirements and those of peer jurisdictions such as the EU and UK.[8] Further, during and after recent stress periods including the COVID pandemic and March 2023 regional bank failures FRB Vice Chair for Supervision Barr, FDIC Chair Gruenberg, and Acting Comptroller Hsu repeatedly acknowledged the stability and resiliency of the banking industry, with strong capital and liquidity.[9]

II. The Agencies Should Address Differences with the Basel Standard to Improve International Comparability and US Bank Competitiveness

The super-equivalency of the US Proposal to the Basel Committee on Banking Supervision's Basel III standard (Basel standard)[10] will drive larger increases in capital requirements for US banks and result in uneven

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[3] Joint Press Release, "Statement by Chair Jerome H. Powell," Board of Governors of the Federal Reserve (July 27, 2023). Retrieved from https://www.federalreserve.gov/newsevents/pressreleases/powell-statement-20230727.htm.

[4] Federal Reserve Bank of New York. (2023, Second Quarter). *Quarterly Trends for Consolidated U.S. Banking Organizations*. Retrieved from https://www.newyorkfed.org/research/banking_research/quarterly_trends.

[5] According to FRB data, US GSIBs maintained $297 billion in "common equity" on December 31, 2008. According to FR Y-9C data as of 2Q 2023, aggregate US GSIB CET1 capital is $914 billion.

[6] Dodd-Frank Act Stress Test 2023: Supervisory Stress Test Results June – 2023. ("While stress tests are one of many supervisory tools, they are the most risk-sensitive and dynamic component of the regulatory capital framework. They help ensure banks can withstand acute financial stress and still be able to lend to households and businesses."). Retrieved from https://www.federalreserve.gov/publications/2023-june-dodd-frank-act-stress-test-executive-summary.htm.

[7] Ibid.; 12 CFR Part 252, Appendix A, §3.1.

[8] Joint Press Release, "Statement by Chair Jerome H. Powell," Board of Governors of the Federal Reserve (July 27, 2023). Retrieved from https://www.federalreserve.gov/newsevents/pressreleases/powell-statement-20230727.htm.

[9] *See* e.g. Oversight of Financial Regulators: Protecting Main Street Not Wall Street. (November 14, 2023). Retrieved from https://www.banking.senate.gov/hearings/oversight-of-financial-regulators-protecting-main-street-not-wall-street.; Barr, Michael S. "Why Bank Capital Matters," Board of Governors of the Federal Reserve (December 1, 2022) ("We have strong capital levels today, and generally higher bank capital requirements in the United States after the Dodd-Frank Act have corresponded with healthy economic growth and have supported the competitiveness of U.S. firms in the global economy . . . We're starting from a good place because capital today is strong."), retrieved from https://www.federalreserve.gov/newsevents/speech/barr20221201a.htm ; Joint Press Release, "Statement by Chair Jerome H. Powell," Board of Governors of the Federal Reserve (July 27, 2023) ("The U.S. banking system is sound and resilient, with strong levels of capital and liquidity."), retrieved from https://www.federalreserve.gov/newsevents/pressreleases/powell-statement-20230727.htm.

[10] Basel Committee on Banking Supervision. (2017). *Basel III: Finalising post-crisis reforms*. December 2017. Retrieved from https://www.bis.org/bcbs/publ/d424.htm.

implementation of capital standards across regions, without evidence of improving financial stability.[11] The likely knock-on impact will be increased costs and less access to financial services for American consumers and companies, as well as incentives to move essential financial services outside of the regulated banking sector. Accordingly, we recommend the Agencies align more closely to the Basel standard generally, and specifically in the areas noted in this letter.

III. The Agencies Should Revise the Operational Risk Components within SCB, CCAR, and DFAST

The Proposal results in duplicative capture of operational risk from the combination of stress capital requirements and minimum capital requirements. The Stress Capital Buffer (SCB) includes projected operational risk losses based on the FRB's Dodd-Frank Act Stress Test (DFAST) methodology, which is calibrated on the Basel 3 Standardized (B3S) approach. The SCB is currently applied only to B3S, which does not include an operational risk capital requirement. However, the proposed Expanded Risk-Based Approach (ERBA) includes credit risk, *operational risk*, market risk, and credit valuation adjustment (CVA), and is also subject to the SCB instead of the fixed 2.5% Capital Conservation Buffer (CCB). As a result, the SCB and the ERBA include overlapping projected operational losses. As Governor Waller noted in his July 27, 2023 statement, "there is no discussion on why operational risk capital needs to be an additional charge as opposed to just using the existing capital stack to absorb operational losses."[12]

We recommend retaining the current B3S approach as the base for the SCB in DFAST and the Comprehensive Capital Analysis and Review (CCAR) process.

IV. The Agencies Should Revise the Services Component of the Operational Risk Business Indicator

The Proposal introduces a standardized operational risk capital approach to replace the current Advanced Measurement Approach (AMA) based on a banking organization's internal models. The Business Indicator Component of the proposed methodology is based on the sum of three elements: interest, lease, and dividend component (ILDC), services component, and financial component. The services component of the proposed approach is intended to capture fee and commission-based activities.

We acknowledge that operational risk is inherent across many banking products, activities, processes, and systems. However, we believe the services component should be amended to better reflect the risks associated with such activities.

The ILDC is calculated as the absolute value of the net difference between total interest income and total interest expense and subject to a cap equal to 2.25% of a banking organization's total interest-earning assets. In contrast, the services component is calculated as a gross amount (higher of income *or* expense) and is uncapped. This structural "overcapitalisation" issue was acknowledged by the Basel Committee on Banking Supervision (BCBS) in two prior consultations (2014, 2016) but, without explanation, was not adopted in the final standard.[13]

The proposed gross amount calculation and uncapped amount of services component operational risk capital disproportionately impacts banks predominantly engaged in fee-based activities. Many of these activities have observably lower historical operational losses than non-fee-based activities. Further, the proposed services component calculation does not differentiate between various fee-based activities, among which there are apparent differences in operational loss rates.

We recommend that the Agencies consider modifying the calculation to reflect the 2016 BCBS consultation:

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[11] Basel Committee on Banking Supervision. *Regulatory Consistency Assessment Programme Jurisdictional Assessments: regulatory implementation consistency* (Updated 13 December 2023). Retrieved from https://www.bis.org/bcbs/implementation/rcap_jurisdictional.htm.

[12] Joint Press Release, "Statement by Governor Christopher J. Waller," Board of Governors of the Federal Reserve (July 27, 2023). Retrieved from https://www.federalreserve.gov/newsevents/pressreleases/waller-statement-20230727.htm.

[13] Basel Committee on Banking Supervision. *Consultative Document: Operational risk – Revisions to the simpler approaches* (October 2014), retrieved from https://www.bis.org/publ/bcbs291.pdf; Basel Committee on Banking Supervision. *Consultative Document: Standardised Measurement Approach for operational risk* (March 2016), ("In response to comments received during the first consultation, the Committee adjusted the structure of the BI to address the following issues: […] (c) Overcapitalisation of banks with high fee revenues and expenses: banks with a high fee component in respect to the overall BI amount have a very high BI value which results in capital requirements that are too conservative relative to the operational risk faced by these banks). Retrieved from https://www.bis.org/bcbs/publ/d355.pdf.

$$\begin{aligned} Services\ Component \\ &= Max[Other\ operating\ income, Other\ operating\ expenses] \\ &+ Max[|Fee\ Income - Fee\ Expenses|, Min\{Max(Fee\ Income, Fee\ Expense), 0.5 \\ &\cdot unadjusted\ BI + 0.1 \cdot (Max(Fee\ Income, Fee\ Expense) - 0.5 * unadjusted\ BI\ )\}] \end{aligned}$$

As a result, “high fee banks” (banks with a share of fees greater than 50% of their unadjusted Business Indicator) would account for only 10% of fees greater than 50% of the unadjusted Business Indicator, with net fee income as a floor.

Alternatively, we recommend simply capping the services component as a percentage of the unadjusted business indicator. This would be consistent with the 2.25% ILDC cap noted above, and it would reduce the disproportionate impact to US banks predominantly engaged in fee-revenue based activities.

V. The Agencies Should Retain the Non-Significant Equity Exposures Category

The current US Basel 3 capital rule’s simple risk-weighted approach for equity exposures includes a 100% risk weight category for non-significant equity exposures. This category, which was eliminated in the Proposal, is generally defined to include an equity exposure to the extent that the aggregate adjusted carrying value of the exposures does not exceed 10% of a banking organization’s total capital.

As a result of the elimination, various equity exposures would be re-classified to higher risk weight categories without evidence that such exposures warrant materially higher risk weights. We understand the Agencies’ intention to increase the risk sensitivity of the equity framework by requiring application of a risk weight based on the characteristics of each equity exposure, rather than only for those less than 10% of a bank’s total capital. However, the increase in risk weights for some categories of equity exposures would disincentivize or eliminate banks’ ability to make critical investments that expand important public policy objectives and promote capital formation. We highlight two examples below.

Renewable Energy Tax Credit Investments

US banks are the predominant investors in clean energy tax equity investments, providing more than 80% of the $20 billion in annual financing for renewable energy project development.[14] Federal tax credits have been an essential catalyst for the development and expansion of the US renewable energy sector, providing necessary financial incentives for banks to invest in these large scale, low risk projects.

Elimination of the non-significant equity exposure category would increase the risk weight of these investments from 100% to 400%. The quadrupling in risk weight for these investments would severely reduce or eliminate banks’ capacity to invest in renewable energy projects; The American Council on Renewable Energy estimates that annual tax equity investments in the renewable energy sector could decrease 80%-90%, and the resulting increase in project cost would render many projects unviable.[15]

Accordingly, the Agencies should consider establishing a 100% risk weight applicable to banks’ equity investments in renewable energy projects that qualify for Federal tax credits. This would be consistent with the low risk profile of these investments, as well as the Basel standard which allows national supervisors to assign a 100% risk weight to “equity holdings made pursuant to national legislated programmes that provide significant subsidies for the investment to the bank and involve government oversight and restrictions on the equity investments.”[16]

Equity Exposures to Investment Funds

The Proposal would require banks to treat an equity exposure to an investment fund as a market risk covered position under Subpart F if the bank has access to the investment fund’s prospectus and is able to either (1) use

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[14] American Council on Renewable Energy. *The Risk Profile of Renewable Energy Tax Equity Investments* (December 2023). Retrieved from https://acore.org/wp-content/uploads/2023/12/ACORE-The-Risk-Profile-of-Renewable-Energy-Tax-Equity-Investments.pdf.

[15] American Council on Renewable Energy. *Letter to Dr. Lael Brainard* (August 22, 2023). Retrieved from https://acore.org/wp-content/uploads/2023/08/ACORE-Letter-on-the-Impact-of-Proposed-Bank-Regulatory-Capital-Requirements-on-Tax-Equity-Investment-in-Clean-Energy.pdf.

[16] Basel Committee on Banking Supervision. *Basel III: Finalising post-crisis reforms* §A.8.52 (December 2017). Retrieved from https://www.bis.org/bcbs/publ/d424.htm.

the look through approach to calculate a market risk capital requirement for its proportional ownership share of each exposure held by the investment fund or (2) obtain daily price quotes for the investment fund.[17]

As a result, the Proposal would require banks to use the revised market risk framework to measure all equity exposures to investment funds, including seed investments in support of client-facing asset management activities. To date, banks have measured seed capital investments under banking book rules due to the lack of trading intent for these investments. The proposed change would materially increase the capital requirements without actual changes in the underlying economic risk, or explanation from the Agencies. In addition, the large increase in risk weight could have a material impact on the ability of US banks to support the growth and innovation of asset management products for their clients.

We recommend the Agencies allow banks that can prove lack of trading intent for seed investments to continue to use banking book rules to calculate the appropriate capital requirement.

VI. The Agencies Should Eliminate the Publicly Traded Security Requirement for Corporate Exposures

The Proposal maintains the 100% B3S corporate exposure risk weight and includes a 65% risk weight for a corporate exposure that is (1) investment grade (as defined in the current Basel 3 capital rule[18]) *and* (2) has a publicly traded security outstanding or is controlled by a company that has a publicly traded security outstanding. We understand the Agencies' desire to incorporate a "simple, objective criterion that would provide a degree of consistency across banking organizations."[19] However this standard fails to appropriately capture the risk sensitivity and creditworthiness of myriad non-public corporate exposures. Less than 1% of US companies are public.[20] As a result, the publicly traded security requirement would prevent nearly all US corporate borrowers from a lower risk weight, regardless of creditworthiness. Further, regulated investment funds are less likely to have a publicly traded security outstanding and can be more creditworthy than corporate borrowers.[21]

The Proposal's additional assertion that "publicly traded corporate entities are subject to enhanced transparency and market discipline as a result of being listed publicly on an exchange"[22] fails to acknowledge that banks require access to prospective borrowers' financial statements, among many additional diligence requirements, and engage in extensive credit review prior to lending and at frequent, regular intervals throughout the life of a credit-based relationship.

Therefore, we recommend eliminating the publicly traded security criterion. This would also be consistent with peer jurisdictions such as the EU and UK, both of whom elected not to include this requirement in their standards. It would also be consistent with the proposed methodology to determine bank exposure risk weights, which does not rely on the existence of a publicly listed security.

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[17] *See* Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. at 64232 (September 18, 2023).

[18] *See* Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Risk weighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule, and Market Risk Capital Rule (October 11, 2013). *("Investment grade* means that the entity to which the [BANK] is exposed through a loan or security, or the reference entity with respect to a credit derivative, has adequate capacity to meet financial commitments for the projected life of the asset or exposure. Such an entity or reference entity has adequate capacity to meet financial commitments if the risk of its default is low and the full and timely repayment of principal and interest is expected.").

[19] *See* Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. at 64054 (September 18, 2023).

[20] United States Census Bureau, Longitudinal Business Database. *As cited in* David, Steven J.; Haltiwanger, John; Jarmin, Ron; Miranda, Javier (June 2006). Volatility and Dispersion in Business Growth Rates: Publicly Traded versus Privately Held Firms. Retrieved from https://www.nber.org/digest/apr07/changing-business-volatility#:~:text=Publicly%20traded%20companies%20constitute%20less.the%20non%2Dfarm%20business%20sector.

[21] Covas, Francisco, and Barbora Stepankova. Working paper. Consistency in Risk Weights for Corporate Exposures Under the Standardized Approach. Washington, DC: Bank Policy Institute, 2022. Retrieved from https://bpi.com/wp-content/uploads/2022/01/Consistency-in-Risk-Weights-for-Corporate-Exposures-Under-the-Standardized-Approach.pdf.

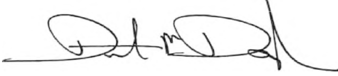
[22] *See* Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. at 64054 (September 18, 2023).

Thank you again for the opportunity to comment on this important Proposal.

We encourage the agencies to consider these changes, which we believe will more appropriately calibrate the final rule to capitalize risks and better align the US capital framework with the Basel standard.

We would be happy to provide further information regarding the comments contained in this letter. Should you have any questions, please contact Rick Gambs (rick.gambs@bnymellon.com).

Sincerely,



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