By Electronic Mail

January 11, 2024

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

Chief Counsel's Office
Attention: Comment Processing
Office of the Comptroller of the Currency
400 7th Street, SW, Suite 3E-218
Washington, DC 20219

James P. Sheesley, Assistant Executive Secretary
Attention: Comments/Legal OES RIN 3064–AF29
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Re: Notice of Proposed Rulemaking: Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions; Federal Reserve Docket No. R–1815, RIN 7100–AG66; OCC Docket ID OCC-2023-0011; FDIC RIN 3064-AF86

Ladies and Gentlemen,

The Securities Industry and Financial Markets Association ("SIFMA"),[1] together with the Asset Management Group of SIFMA ("SIFMA AMG"),[2] appreciates the opportunity to comment on the above-captioned proposal to extend long-term debt ("LTD") and clean holding company requirements to non-GSIB large banking organizations ("LBOs"), certain intermediate holding companies ("IHCs") of foreign banking organizations ("FBOs"), and large insured depository institutions ("covered IDIs," and collectively with LBOs and IHCs, "covered entities") issued by the Board of Governors of the Federal Reserve System ("Federal Reserve"), Office of the Comptroller of the Currency ("OCC") and Federal Deposit

[1] 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 for 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.

[2] SIFMA AMG brings the asset management community together to provide views on policy matters and to create industry best practices. SIFMA AMG's members represent U.S. and multinational asset management firms whose combined global assets under management exceed $45 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds.

Insurance Corporation ("FDIC," and collectively with the Federal Reserve and the OCC, the "agencies").[3]

Executive Summary

SIFMA and SIFMA AMG support efforts to ensure there is adequate loss-absorbing capacity in the U.S. banking system. However, the agencies' LTD proposal threatens to materially impede investor demand for LTD securities, while simultaneously increasing the supply of these instruments to the market. As a result, the proposal as currently written would have significant adverse effects on bank funding costs and on the liquidity of bank funding markets. We recommend that the agencies consider and address the following issues before finalizing the proposal:

I. **LTD Minimum Denomination: The agencies should not introduce the proposed minimum denomination requirement for newly issued eligible debt securities, as it would change the industry's current LTD issuance practices in ways that reduce the diversity of the institutional investor base and liquidity in LTD markets. If, however, the agencies continue to believe that a mechanism is necessary to maintain low direct ownership of LTD securities by retail investors, they should consider using other, less disruptive approaches that would maintain the current industry practice of primarily issuing directly to institutional investors.**

The agencies propose amending the term "eligible debt security" in the proposal to specify that new LTD must be issued in minimum denominations of $400,000 to be considered eligible external LTD in an effort to disincentivize retail investors from directly investing in LTD. We are concerned that this proposed change to the definition of eligible debt security will drastically reduce the institutional investor base for bank debt, given the current standard for issuance is a $2,000 denomination. As proposed, this change will not only exclude the few retail investors that may invest directly in these types of securities,[4] but also large swathes of institutional investors in both the primary and secondary LTD markets. The reduced size of the institutional investor base would, in turn, reduce the depth of liquidity in the markets for bank-issued LTD at a time when covered entities may have to increase their external LTD issuances. Decreased liquidity would increase costs for issuers.

We strongly recommend that the minimum denomination requirement be eliminated from the final rule. A minimum denomination at any level above the current industry standard could have significant, unintended consequences for LTD markets. While SIFMA and SIFMA AMG do not believe that the agencies need to consider any alternative approaches in light of the very small number of direct retail investors in the LTD markets, we would welcome the opportunity to discuss less disruptive approaches with the agencies should they deem action necessary, including through supplementary materials that may be shared after the closing date for comments on this proposal. Such approaches would be designed to preserve the current state of low direct retail holdings of LTD.

II. **Interaction with the Basel III Endgame and Other Proposals: The proposal does not account for the impact of the Basel III Endgame proposal on the amount and costs of LTD that covered entities would need to issue. A final version of the proposal should consider the effects of the final Basel III Endgame rule—and the impact of other outstanding proposals—on the amount and costs of LTD.**

The proposal over-calibrates the LTD requirement for covered entities, in part because of its interaction with the far-reaching risk-based capital reforms that the agencies have proposed in their Basel

[3] See Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System and Federal Deposit Insurance Corporation, Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions, 88 Fed. Reg. 64524 (Sept. 19, 2023).

[4] Only about 1 percent of U.S. households directly invest in debt securities of any kind. See Board of Governors of the Federal Reserve System, Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances (Sept. 2020), https://www.federalreserve.gov/publications/files/scf20.pdf.

III Endgame proposal.[5] The Basel III Endgame proposal would significantly increase risk-weighted assets ("RWAs") for covered entity banking organizations, which would "lead mechanically to increased requirements for LTD under the LTD proposal."[6] Yet the agencies acknowledge that their estimates of the LTD needs and costs presented in the proposal do not account for the impact of the Basel III Endgame proposal.[7] Until the agencies can fully consider the relationship between the two proposals, they should refrain from finalizing any new LTD requirements.

In addition, there are a number of other outstanding proposals that may impact the LTD proposal, including the GSIB surcharge and resolution planning proposals.[8] The plethora of proposals that are currently under review make it difficult to assess with certainty how they may interact and compound on one another. The agencies should therefore remain receptive to receiving supplemental comments on the LTD proposal as these impacts become more apparent. The agencies should further wait to finalize the LTD proposal until they and the industry can take into account how the final version of the Basel III Endgame rule—as well as the other proposals noted above—will impact the amount and cost of LTD that will need to be issued by covered entities.

III. Internal LTD Requirement: The proposed "internal LTD" requirement would significantly contribute to the over-calibration of the "external LTD" requirement, which would increase bank funding costs and negatively impact firms' ability to provide credit and capital markets services. The agencies should therefore not adopt an internal LTD requirement, and instead permit covered holding companies to comply with any LTD requirement at either the holding company or insured depository institution ("IDI") level. If, however, the agencies believe internal LTD is necessary, the agencies should recalibrate it downwards and allow it to be satisfied through other loss-absorbing instruments and exempt certain firms. The agencies should also retain the exemption from the internal LTD requirement for U.S. GSIBs contained in the proposal and extend it to foreign GSIB IHCs and non-GSIB LBO retail broker-dealers.

The creation of an "internal LTD" requirement applicable at the IDI level is also a major driver of the over-calibration of the proposed LTD requirement. Internal LTD would create a two-level LTD requirement for covered entity holding companies—one at the holding company level and one at the IDI level—which would force many covered entities to issue significantly larger volumes of "external LTD" than reflected in the agencies' estimates in the proposal. In the aggregate, this requirement would lead to levels of LTD that are far greater than needed to ensure adequate loss-absorbing capacity and could prove difficult for the markets to absorb in a short period of time.

Given these issues with the internal LTD requirement, the agencies should not adopt it as a requirement in the final LTD rule, and instead should permit a covered holding company or IHC to comply with any LTD requirement at either the holding company level (which would allow for flexible deployment of resources where needed) or the IDI level. If, however, the agencies believe an internal LTD requirement is necessary, they should recalibrate the requirement for those firms that remain subject to it to more appropriately reflect the impact it will have on holding company liquidity requirements and its

[5] See Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System and Federal Deposit Insurance Corporation, Regulatory Capital Rule: Large Banking Organizations and to Banking Organizations with Significant Trading Activity, 88 Fed. Reg. 64028 (Sept. 18, 2023).

[6] 88 Fed. Reg. 64524, 64551 n.97.

[7] *Id.*

[8] See Board of Governors of the Federal Reserve System, Regulatory Capital Rule: Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Systemic Risk Report (FR Y-15), 88 Fed. Reg. 60385 (Sept. 1, 2023); Federal Deposit Insurance Corporation, Resolution Plans Required for Insured Depository Institutions With $100 Billion or More in Total Assets; Informational Filings Required for Insured Depository Institutions With at Least $50 Billion But Less Than $100 Billion in Total Assets, 88 Fed. Reg. 64579 (Sept. 19, 2023); Board of Governors of the Federal Reserve System and Federal Deposit Insurance Corporation, Guidance for Resolution Plan Submissions of Domestic Triennial Full Filers, 88 Fed. Reg. 64626 (Sept. 19, 2023); Board of Governors of the Federal Reserve System and Federal Deposit Insurance Corporation, Guidance for Resolution Plan Submissions of Foreign Triennial Full Filers, 88 Fed. Reg. 64641 (Sept. 19, 2023).

broader impacts on market capacity. The agencies should specifically consider replacing the internal LTD requirement with a more flexible internal "gone-concern loss-absorbing capacity" requirement that could be met through various types of internal loss-absorbing resources and re-calibrating the internal requirement to at a minimum 2 percent of total RWAs (and revise any leverage-based LTD requirements commensurately). A lower calibration of the internal LTD requirement for Categories III and IV holding companies would also be appropriate and consistent with the letter and spirit of the requirement to tailor enhanced prudential standards under the Economic Growth, Regulatory Relief and Consumer Protection Act ("EGRRCPA").[9]

Even under a recalibrated approach, the internal LTD requirement would be inappropriate for many firms. We support the agencies retaining an exclusion for the IDIs of U.S. GSIBs from this requirement. As the agencies acknowledge, U.S. GSIBs are already subject to both total loss absorbing capacity ("TLAC") and external LTD requirements and have in place resolution frameworks for maintaining and then distributing internal loss-absorbing resources to their material subsidiaries. An exemption would also be appropriate for IDIs of foreign GSIB IHCs, given that the foreign parent and U.S. IHC of such institutions are subject to robust home jurisdiction and U.S. resolution planning requirements that are substantively similar to U.S. GSIBs and TLAC (or similar) requirements. In addition, we believe the agencies should further exempt from the proposed internal LTD requirement for IDIs of non-GSIB LBOs that operate primarily as retail broker-dealers, given the low-risk profiles of the consolidated firm and that they are already subject to enhanced prudential standards, can be resolved effectively under existing frameworks and would be subject to external LTD at the full "capital refill" calibration.

IV. Covered Debt Instrument Definition: The agencies should clarify that the definition of "covered debt instrument" only applies to an IDI subject to a LTD requirement.

Any final rule should be revised to provide that, for purposes of the deduction framework under the capital rule, the definition of "covered debt instrument" only applies to an IDI that is subject to a LTD requirement (*i.e.*, unsecured debt issued by an IDI that is not subject to a LTD requirement is not included). Specifically, clause (1)(i) of the proposed revised definition of covered debt instrument should refer to a subsidiary subject to a LTD requirement under proposed new Part 54, 216, or 374, instead of any subsidiary of a depository institution holding company subject to a LTD requirement under Part 238 or Part 252. As currently drafted, the proposed definition of covered debt instrument would appear to scope in certain unsecured exposures to subsidiaries of covered companies that do not count as capital or eligible LTD.

V. LTD Implementation: The transition period for the LTD proposal should follow sequentially after the transition period for the Basel III Endgame proposal to facilitate capital accretion and ensure that the market can absorb new LTD issuances.

Because LTD is "generally more expensive than" other forms of short-term funding, the LTD proposal is likely to "raise funding costs in the long run."[10] This cost would likely impact the ability of covered entities to accrete additional capital in advance of any final Basel III Endgame rule. As a result, banking organizations may need to substantially change their lending activity to comply with the new rules, which could reduce credit availability and raise costs for borrowers. To mitigate these concerns, and for other reasons discussed below, the agencies should consider sequencing the transition period of any new LTD requirement. Sequencing the LTD requirement's transition period to follow the transition period for any final rule implementing the Basel III Endgame proposal would help facilitate the accretion of capital at banking organizations and minimize detrimental impacts to borrowers.

VI. Clean Holding Company Requirements: The proposal's limited exemptions to the prohibition on covered entity holding companies entering qualified financial contract ("QFC") arrangements with third parties should be expanded to cover normal course

[9] See Economic Growth, Regulatory Relief, and Consumer Protection Act, Pub. L. No. 115-174, sec. 401, 132 Stat. 1296 (2018).

[10] 88 Fed. Reg. 64524, 64552.

transactions that do not conflict with the agencies' underlying policy objectives. The agencies should also clarify that since clean holding company requirements are primarily designed to facilitate a single-point-of-entry ("SPOE") resolution, the same requirements should not be applied to firms with alternative resolution strategies.

We welcome the agencies' decision to provide limited exemptions to the prohibition under the clean holding company requirements on covered entity holding companies entering into normal course QFC arrangements with third parties. We recommend that the agencies further extend the exemptions on QFC arrangements with third parties to additional normal course QFC transactions that similarly would not interfere with an orderly SPOE resolution or cause financial stability risks. Despite the agencies' positive step forward with respect to the QFC exemptions, we are not supportive of their proposal to extend the clean holding company requirements to holding companies that rely on a multiple-point-of-entry ("MPOE") resolution strategy, for the reasons discussed below.

VII. Changes to the Existing TLAC Rule: The proposed changes to the calculation of TLAC should not be adopted. However, if they are adopted, they should only apply to newly issued LTD.

The proposal would amend the calculation of the minimum TLAC requirement for those firms subject to the TLAC rule by allowing only 50 percent of eligible LTD with a maturity of one year or more, but less than two years, to count toward a firm's TLAC requirement (at present, this haircut applies only to these firms' minimum LTD requirement). This change is unnecessary given that firms subject to the existing TLAC rule overwhelmingly call LTD instruments prior to the last year before they mature, in large part because of the impact of the existing LTD haircut. Amending the current treatment would moreover needlessly impair firms' funding plans and business strategies without yielding any significant benefit.

We recommend that the current TLAC rule's approach to LTD with a maturity of one year or more but less than two years should be retained. However, if the proposed haircut change is adopted, it should only apply to newly issued LTD and not to existing eligible LTD that was issued under the assumption of the prior calculation method. The treatment of already-issued LTD should not suddenly change, especially as the change in the calculation method would affect firms' funding plans.

VIII. Uninsured Deposits: The agencies have asked about the different types of uninsured deposits and are urged to recognize the differing levels of risks posed by different types of these deposits.

We believe that the agencies have missed key nuances in making broad statements in the proposal about the risks posed by uninsured deposits that do not distinguish between different types of these deposits.[11] In fact, as the agencies have recognized in the past, some types of uninsured deposits are observably stable even in stressed periods. We therefore urge the agencies to acknowledge and consider the important distinctions among different types of uninsured deposits.

[11] 88 Fed. Reg. 64524, 64525.

SIFMA and SIFMA AMG Comments on the Proposal

I. LTD Minimum Denomination: *The agencies should not introduce a minimum denomination requirement for newly issued eligible debt securities, as it would change the industry's current LTD issuance practices in ways that reduce the diversity of the institutional investor base and liquidity in LTD markets. If, however, the agencies continue to believe that a mechanism is necessary to maintain low direct ownership of LTD securities by retail investors, they should consider using other, less disruptive approaches that would maintain current industry practice of primarily direct issuance to institutional investors.*

The agencies propose amending the term "eligible debt security" in the proposal to specify that new LTD issued after finalizing the LTD proposal must be issued in minimum denominations of $400,000 to be considered eligible external LTD. The agencies' stated objective for doing so is described as follows:

> *The purpose of this requirement is to limit direct investment in eligible LTD by retail investors. Significant holdings of LTD by retail investors may create a disincentive to impose losses on LTD holders, which runs contrary to the agencies' intention that LTD holders expect to absorb losses in resolution after equity shareholders. Imposing requirements that will tend to limit investments in LTD to more sophisticated investors will help ensure that LTD holders will monitor the performance of the issuer and thus support market discipline. These more sophisticated investors are more likely to appreciate that LTD that satisfies the requirements of the proposed rule may present different risks than other types of debt instruments issued by covered entities, covered IDIs, or other firms.*[12]

SIFMA and SIFMA AMG view this provision as not only unnecessary to achieving these policy objectives, but also a deleterious change to primary and secondary LTD market practices, especially given the current industry standard denomination is $2,000. If included in the final LTD rule, the proposed minimum denomination requirement would dramatically shrink the investor base for high-quality bank debt by excluding a large swathe of institutional investors from primary market purchases, and secondary market trading, of LTD. These impacts, in turn, would reduce market depth and liquidity for bank-issued LTD, increasing costs for issuers and creating a greater concentration in the ownership base of LTD. This minimum denomination requirement should therefore be removed from the final rule. If the agencies' objective is to maintain the *status quo*—extremely low direct ownership of eligible LTD by retail investors—they can achieve this objective through less disruptive approaches, to the extent deemed necessary. We would welcome the opportunity to discuss alternative approaches with the agencies that would preserve the current low level of direct retail ownership, including through supplementary materials that may be shared after the closing date for comments on this proposal.

A Minimum Denomination Amount Would Negatively Impact Institutional Investors' Ability to Invest in LTD.

SIFMA's and SIFMA AMG's members are concerned that the most meaningful effect of the minimum denomination requirement would be to prevent a wide range of institutional investors from purchasing these types of bonds, as reflected in the bullets below. Retail investors generally only have exposures to LTD indirectly through professionally managed investment accounts and/or vehicles that are part of a broader investment portfolio, such as mutual funds and exchange traded funds ("ETFs"). Institutional investors that manage these accounts and/or funds are highly sophisticated professionals that understand credit risks and make investment decisions in their clients' best interest.

- Member estimates indicate that a fixed income portfolio managed to a corporate bond index would need at least $200 million in total assets to be able to make a $400,000 investment in the LTD of a single banking organization. The reason for this is because U.S. banks comprise about 15 percent of the corporate bond index, and within a specific sector, portfolio managers

[12] 88 Fed. Reg. 64524, 64537.

commonly make investments across issuers for diversification and risk management purposes. Mutual funds and ETFs are among the largest pools of institutional investments, yet the $400,000 threshold is so large that many of them could be precluded from investing in LTD. According to Morningstar, 41 of 83 corporate bond mutual funds and ETFs have less than $200 million in assets.[13]

- Similarly, member estimates indicate that a fixed income portfolio managed to the U.S. Aggregate Bond Index (which tracks corporate bonds and also a broader spectrum of instruments including U.S. Treasuries, agency mortgages and other securitized products) would need at least $800 million in total assets to make an investment in LTD with a $400,000 denomination. According to Morningstar, 355 of 557 mutual funds and ETFs with a U.S. Aggregate Bond Index benchmark have less than $800 million in assets under management.
- Many other institutional investors will have fewer assets than these thresholds, effectively preventing them from buying LTD. It would not be unusual, for example, for a moderately-sized separate account for a pension fund, endowment, or trust to be in the range of $20-100 million. Similarly, a newly seeded mutual fund or ETF might have as little as $3-5 million in assets when first launched. These types of accounts would effectively be excluded from this market because it would cause them to have an overweight exposure to a single debt security.

As demonstrated above, the minimum denomination requirement would likely exclude a wide range of institutional investors from the markets for banking organizations' LTD. As such, the requirement would, perhaps unintentionally, prevent professionally managed vehicles from widely investing in LTD.

A Minimum Denomination Amount Would Reduce Market Liquidity and Increase LTD Funding Costs for Banking Organizations.

A $400,000 minimum denomination for LTD instruments would be significantly larger than the denominations that the holding companies of the eight U.S. GSIBs have already issued in the primary markets. As Figure 1 below illustrates, a minimum denomination threshold of $400,000 would render more than 90 percent of the U.S. GSIBs' principal notional amount ineligible. Even if the minimum denomination amount were lowered to $100,000, as the agencies indicated that they actively considered,[14] this threshold would still exclude 80 percent of the outstanding principal amount of LTD securities (i.e., the specified denomination less the aggregate amount of all principal payments in respect of such LTD securities) issued in the primary markets. In fact, the vast bulk of outstanding eligible LTD issued by the U.S. GSIBs has a principal amount of $10,000 or less, with the industry standard being a denomination of just $2,000.

[13] Figures obtained from the Morningstar Direct database.

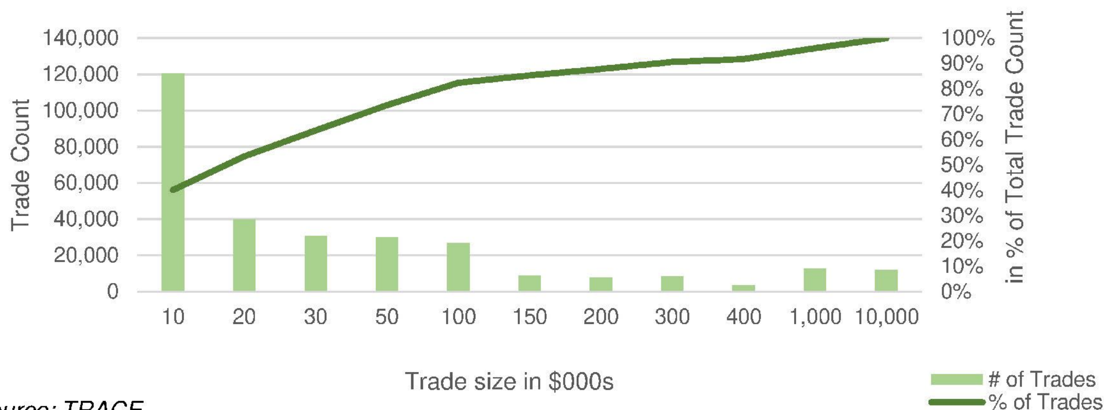
[14] 88 Fed. Reg. 64524, 64537.

Figure 1: Outstanding Principal Amount of Debt Securities Issued by U.S. GSIBs by Minimum Denomination

Source: TRACE

A $400,000 minimum denomination would also likely result in a reduction in liquidity in the secondary LTD markets, as seen in the below analysis of trading activity of debt securities issued by the holding companies of the eight U.S. GSIBs via TRACE. As shown in Figure 2, over 90 percent of trading activity occurs in relation to trade sizes of less than $400,000, with the overwhelming bulk of trading occurring in denominations under $100,000 (particularly under $10,000). Moreover, even when large institutional managers transact in substantial sizes, such as $100,000 or greater, they often do so on behalf of various funds in their complex. It is common for managers to make a large purchase, and then distribute bonds across a series of eligible bond funds, thus requiring lower denominations. This dynamic is also true in the primary markets, where an institutional investor may purchase a large block allocation of LTD, and then distribute bonds across appropriate funds. Those funds, in turn, will need bonds in smaller denominations for portfolio and risk management purposes.

Figure 2: Number of Trades of Debt Securities issued of US GSIB Holding Companies over 4 Weeks by Trade Size



Source: TRACE

As the above figures suggest, a large minimum denomination requirement would likely result in a significant reduction in the number and type of investors that hold LTD. That in turn would affect the liquidity of these markets. The link between maintaining a broad and diverse investor base and market liquidity has long been established as a key ingredient of market depth. In fact, one of the requirements of the "liquid and readily marketable" definition under the agencies' liquidity coverage ratio ("LCR")

requirement is that "the security is traded in an active secondary market with . . . a large number of non-market maker participants on both the buying and selling sides of transactions."[15] A smaller investor base is thus likely to reduce LTD market liquidity and conversely increase both market volatility and the cost of LTD funding for banking organizations. The Private Resales of Securities to Institutions or 144A market may provide insight on how the proposed LTD minimum denomination requirement could impact market liquidity and the cost of issuing LTD, given analogous restrictions on who can purchase 144A securities and the minimum denomination requirements for such securities. Sell-side research has found that the average spread on 144A bonds is currently 25 bps wider compared to registered bonds. This kind of spread would ultimately increase the cost of debt for bank issuers.

Very Few Retail Investors Directly Invest in Debt Markets.

Very few retail investors seek out bank holding company debt securities directly.[16] The small number of retail investors directly investing in debt instruments tend to be sophisticated and have a higher net worth, given the difficulty of purchasing individual bonds; even then, in most instances these investments are managed by a professional fiduciary making the investment decision. These instruments are not exchange traded and require the transaction to proceed through a broker and a prospectus to be delivered. Moreover, direct investors in bank-issued LTD are made aware of the risks associated with these instruments, as debt security prospectuses are already required to disclose that a resolution of the issuing bank could materially affect the debt security's value. The minimum denomination requirement would therefore simply serve to reduce choice for sophisticated retail investors looking to gain exposure to high-quality debt securities in bank holding companies that are subject to rigorous prudential oversight.

For the Reasons Cited Above, the Minimum Denomination Requirement Should Not Be Included in the Final Rule. However, if the Agencies Believe Action is Required to Maintain the Status Quo of Low Direct Retail Investment in LTD, SIFMA and SIFMA AMG Would Welcome the Opportunity to Discuss Less Disruptive Approaches.

In conclusion, a minimum denomination requirement is unnecessary, given very low levels of direct retail holdings of LTD securities, and would have a wide range of adverse impacts by excluding a large swath of institutional investors and secondary market participants, thereby reducing market liquidity and increasing the cost of financing bank LTD. The agencies should therefore not include any minimum denomination requirement in the final LTD rule, as it could be contrary to long-standing market practice and have a destabilizing effect as a result.

While SIFMA and SIFMA AMG do not believe that action is needed in light of the small number of direct retail investors engaging in the primary or secondary LTD markets, we would welcome the opportunity to discuss and submit supplementary materials on less disruptive approaches with the agencies that would preserve the current low level of direct retail ownership.

II. Interaction with the Basel III Endgame and Other Proposals: *The proposal does not account for the impact of the Basel III Endgame proposal on the amount and costs of LTD that covered entities will need to issue. Any finalized version of the LTD proposal should consider the effects of the finalized Basel III Endgame rule—and the impact of other outstanding proposals, including the GSIB surcharge proposal—on the amount and costs of LTD.*

The LTD proposal over-calibrates the LTD requirement for covered entities, in part because of its interaction with the far-reaching risk-based capital reforms that the agencies have proposed in their Basel

[15] 12 CFR § 249.3.

[16] Approximately 1 percent of U.S. households invest in corporate bonds. See Board of Governors of the Federal Reserve System, Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances (Sept. 2020), https://www.federalreserve.gov/publications/files/scf20.pdf.

III Endgame proposal. The Basel III Endgame proposal would significantly increase RWAs for covered entity banking organizations, with the agencies' own estimates suggesting that the RWAs for Categories I-IV banking organizations would rise by approximately $2.2 trillion. This RWA increase would, as the agencies acknowledge, "lead mechanically to increased requirements for LTD under the LTD proposal."[17] Yet, the agencies also acknowledge that their estimates of the LTD needs and costs presented in the proposal do not account for the impact of the Basel III Endgame proposal.[18]

The clear implication is that the LTD shortfall estimates included in the proposal[19] are based on the calculation of RWAs under the existing U.S. standardized approach to banking organizations' capital requirements, rather than the significantly higher RWAs that are expected to result from the implementation of the proposed expanded risk-based approach under the Basel III Endgame proposal. As a result, the LTD shortfall could be much greater than the agencies' current estimates indicate purely as a result of the higher RWAs that would result from the implementation of the Basel III Endgame proposal.[20] While the agencies suggest that the increased capital required under the Basel III Endgame proposal could "reduce the cost of various forms of debt for impacted firms due to the increased resilience that accompanies additional capital," they provide no empirical evidence to support this claim.[21] They also do not appear to have considered the impacts on costs of issuing LTD that might accompany the paradoxical result of increasing supply, while simultaneously reducing demand because of the minimum denomination requirement,[22] that the proposal could have.

Until the agencies can fully consider the relationship between the two proposals—and particularly how the Basel III Endgame proposal could affect the costs and amounts of LTD that would need to be issued—they should refrain from finalizing any new LTD requirements. Given that the agencies are in the midst of conducting a quantitative impact study on the Basel III Endgame proposal and have yet to receive results, neither they nor the public are yet able to fully assess the impact of the Basel III Endgame proposal in general or specifically on the proposed LTD requirement. In addition to the Basel III Endgame proposal, there are a number of other outstanding proposals that may impact the LTD proposal, including the GSIB surcharge and resolution planning proposals. For instance, proposed changes to the GSIB surcharge could impact the calculation and calibration of the external LTD requirement for the covered holding companies of U.S. GSIBs under the TLAC rule. The plethora of proposals that are currently under agency and industry review make it difficult to assess with any certainty how these proposals may interact and compound on each other.

In light of this fact, the agencies should remain receptive to receiving supplemental comments on the LTD proposal as compounding impacts become more apparent over time. The agencies should wait to finalize the LTD proposal only once they, the industry and the public can take into account how the final version of the Basel III Endgame proposal and the other proposals will impact the amount and cost of LTD that would need to be issued.

III. Internal LTD Requirement: ***The proposed "internal LTD" requirement would significantly contribute to the over-calibration of the "external LTD" requirement, thereby increasing bank funding costs and negatively impacting firms' ability to provide credit and capital markets services. The agencies should therefore not adopt an internal LTD requirement, and instead permit covered holding companies to comply with any LTD requirement at either the holding company or IDI level. If, however, the***

[17] 88 Fed. Reg. 64524, 64551.

[18] *Id.*

[19] The agencies estimate that the LTD shortfall is approximately $70 billion in the aggregate. Categories II and III firms would need to issue about $20 billion of such shortfall amount, while Category IV firms would need to issue about $50 billion. *Id.* at 64552.

[20] As discussed below in Section III, the actual shortfall amount is likely also significantly higher as a result of the internal LTD requirement.

[21] 88 Fed. Reg. 64524, 64551.

[22] See discussion in Section I above.

agencies believe internal LTD is necessary, the agencies should recalibrate it downwards and allow it to be satisfied through other loss-absorbing instruments. The agencies should also retain the exemption from the internal LTD requirement for U.S. GSIBs and extend it to foreign GSIB IHCs and non-GSIB LBO retail broker-dealers.

The Internal LTD Requirement Contributes to Over-Calibration of the External LTD Requirement, Which Would Contribute to the Oversupply of LTD in the Markets.

The proposal would require covered entity holding companies to downstream the proceeds of external LTD to certain IDI subsidiaries with assets of $100 billion or more. These covered IDIs would then issue internal LTD back to their parent holding company. This new concept of an internal LTD requirement would create a two-tiered LTD requirement for covered entity holding companies that would ultimately force them to issue significantly larger volumes of external LTD than reflected in the agencies' estimates in the proposal. In the aggregate, this requirement would also lead to levels of LTD that would be far greater than needed to ensure adequate loss-absorbing capacity in the system and may prove difficult for the markets to absorb, given the significant spike in the supply of LTD that would result.

As noted above in Section II, the agencies have estimated that the total LTD shortfall amount resulting from the proposal (under their incremental shortfall approach)[23] would be approximately $70 billion in the aggregate, representing a 15 percent increase in annual LTD issuance. In the proposal, the agencies make clear that this estimate assumes that it "will be costless to substitute external holding company-issued debt for external IDI-issued debt, as well as to downstream resources from holding companies to IDIs through eligible internal debt securities, to fulfill the requirements of the proposed rule and general funding needs. It is assumed, in other words, that there are no additional costs for IDIs to maintain eligible internal debt securities to holding companies beyond those attributable to any external holding company LTD that may be passed through to IDIs."[24]

The agencies' assumption under the incremental shortfall approach is that the internal LTD requirement would be "costless" and have no bearing on the overall level of external LTD is incorrect. Estimates suggest that, even leaving aside the impact of the Basel III Endgame proposal, the external LTD shortfall could be closer to $186.6 billion[25] in the aggregate, more than double the agencies' own estimates under the incremental shortfall approach, driven in large part by the constraints of maintaining an adequate level of internal LTD at the IDI level. The Bank Policy Institute also released estimates showing that the LTD shortfall would be approximately $83 billion for Categories II and III banking organizations and approximately $104 billion for Category IV banking organizations, approximately $60 billion and $50 billion more, respectively, than the agencies' estimates of $20 billion and $50 billion under

[23] The agencies' economic impact analysis includes two approaches for analyzing the costs for the banking organizations that would become newly subject to LTD requirements: (i) a lower-end estimate ("incremental shortfall approach"), which assumes the current reported principal amounts of LTD issuance at covered entities is a "reasonable proxy for the levels of such debt that would be maintained in future periods in the absence of the [LTD proposal]," and (ii) a higher-end estimate ("zero baseline approach"), which assumes that covered entities would, in the absence of the LTD proposal, "choose to maintain no instruments that satisfy the [LTD proposal's] requirements in future periods." 88 Fed. Reg. at 64,549. The agencies state that "the funding cost impact of the proposal is likely between the lower-end estimate from the incremental shortfall approach and the higher-end estimate from the zero baseline approach," while adding that "the incremental shortfall approach may provide a more accurate near-term perspective on funding cost impact." 88 Fed. Reg. at 64,553. Under the incremental shortfall approach, the Agencies estimate that the aggregate LTD shortfall would be approximately $70 billion and pre-tax annual funding costs would increase by approximately $1.5 billion, which would represent a three-basis-point decline in net interest margins. See *id.* at 64,552. Under the zero baseline approach, the agencies estimate that the total principal value of external LTD required of these banking organizations, irrespective of existing LTD, would be approximately $250 billion and pre-tax annual funding costs would increase by approximately $5.6 billion, which would represent an 11-basis-point decline in net interest margins. See *id.* at 64,551. The zero-baseline approach estimate is that pre-tax annual funding costs would increase by approximately $9.4 billion, which would represent a 19-basis-point decline in net interest margins.

[24] 88 Fed. Reg. 64524, 64551–52.

[25] Bank Policy Institute, "The Long-Term Debt Proposal and Bank Profitability," Bank Policy Institute, Dec. 7, 2023, https://bpi.com/wp-content/uploads/2023/12/The-Long-Term-Debt-Proposal-and-Bank-Profitability.pdf.

the incremental shortfall approach. This significant increase in shortfall would again be driven in large part by the internal LTD requirement.[26]

There are several reasons why the internal LTD requirement may force covered entity holding companies to issue significantly higher levels of external LTD. First, while the holding company may be able to raise sufficient external LTD to meet the proposal's requirements, it may not have enough liquid assets to downstream proceeds to its covered IDI subsidiary and also fund the operations of a broker-dealer or other non-bank subsidiary. As a result, the holding company would be forced to issue more external LTD. Second, and more particularly, a covered entity holding company may need to issue additional external LTD because of the impact that downstreaming liquid assets to its covered IDI subsidiary would have on the holding company's LCR. If the holding company also needs to use debt to fund the operations of the broker-dealer or other non-bank subsidiaries, it would need to issue more external LTD to maintain adequate LCR levels. Additionally, under the proposed internal LTD requirement, an IDI would not be able to substitute its holding company's overnight deposits held at the IDI with internal LTD without reducing the high-quality liquid asset ("HQLA") amount counted toward the holding company's LCR. This outcome would reduce the holding company's LCR, which could force the holding company to issue additional external LTD. Firms would also need to factor in management buffers, which could further add to over-calibration and costs. The internal LTD requirement would therefore effectively be doubling the required amount of LTD estimated under the incremental shortfall approach—due in large part to firms' need to comply with the LCR requirements.

As a result, covered entity holding companies—many of which are already facing higher funding costs in light of current economic conditions—would likely see costs increase as they would be forced to issue significant amounts of new external LTD at the holding company level rather than at the IDI level (where spreads would typically be lower). As a result of this increase in external LTD issuances, the market would have to absorb much larger volumes of LTD at more frequent intervals, which could generally impact market capacity in the secondary markets. Indeed, the agencies explicitly recognize this issue in the proposal, noting that "due to the considerable scope of the proposal, there is a risk that efforts by covered entities and covered IDIs to issue a large volume of LTD over a limited period could strain the market capacity to absorb the full amount of such issuance if issuance volume exceeds debt market appetite for LTD instruments."[27] The supply of LTD would therefore increase at a time when the agencies, through the minimum denomination requirement, seek to narrow the pool of potential buyers of such debt.

In addition to these broader market-level impacts, the agencies should consider that, for many types of firms, the impacts of the internal LTD requirement would be particularly harmful, duplicative or unnecessary, which should preclude the need for an internal LTD requirement more generally:[28]

- For instance, the above impacts would be felt most acutely by smaller issuers of LTD. These issuers may face higher credit spreads, not because of concerns with their underlying credit risk, but because of concerns about illiquidity in the secondary market for their debt. This outcome could not only affect the cost of funding, but also restrict access to the markets, making it difficult for these issuers to raise new external LTD.

- Many of the above issues with the internal LTD requirement would also be particularly harmful to non-GSIB LBO firms that are leverage-bound due to the low-risk nature of their assets, such as LBOs that operate primarily as retail broker-dealers.[29] Leverage ratios, particularly LTD leverage ratios, should be a backstop and not a binding constraint, as the

[26] *Id.*

[27] 88 Fed. Reg. 64524, 64553.

[28] As discussed below in this Section, we have proposed, in many cases, to specifically exempt these firms from the internal LTD requirement in the event that the agencies determine that they will retain the internal LTD requirement in the finalized version of the LTD proposal.

[29] The low-risk nature of these firms' assets further mitigates the need to have LTD at both the holding company and the IDI level.

agencies intended.[30] As SIFMA noted in its January 2023 letter[31] to the Federal Reserve's and FDIC's advance notice of proposed rulemaking ("ANPR") on this issue,[32] these leverage-bound non-GSIB LBOs generally have a simple organizational structure and low-risk profile relative to GSIBs and other non-GSIB LBOs and can be effectively resolved under existing frameworks,[33] especially with a layer of external LTD at the full "capital refill" level at the holding company. Furthermore, such firms are already subject to other enhanced prudential standards established by the agencies in the aftermath of the last financial crisis under the Dodd-Frank Act, including capital, stress testing and liquidity requirements.[34] The internal LTD requirement would therefore seem particularly unnecessary for these firms.

- Finally, IDI subsidiaries of U.S. GSIB firms are already subject to various requirements under the 165(d) resolution planning framework, including Resolution Capital Adequacy and Positioning ("RCAP"), that obviates the need for an internal LTD requirement as this LTD requirement would essentially be duplicative.[35]

In short, the internal LTD requirement would significantly increase the overall amount of external LTD that covered holding companies, including smaller issuers, would need to raise and would do so unnecessarily and to the detriment of many firms. In all cases, the increase in external LTD issuances would negatively affect the ability of firms to provide credit and engage in capital markets intermediation on behalf of clients. The LTD proposal would therefore exacerbate the expected impacts and costs on retail customers, businesses, and other end-users of the Basel III Endgame proposal, which is similarly expected to strain banking organizations' lending and capital markets activities.

Given the Issues Highlighted Above, the Agencies Should Not Adopt the Internal LTD Requirement or, in the Alternative, Should Consider Two Methods for Reconfiguring the Internal LTD Requirement.

In light of the issues with the internal LTD requirement highlighted above, the agencies should not adopt the internal LTD requirement as part of the final LTD rule and should instead permit a covered holding company or IHC to comply with any LTD requirement at either the holding company level or the IDI level.

If, however, the agencies believe internal LTD is necessary in certain cases, the agencies should recalibrate the internal LTD requirement to appropriately reflect the impact this requirement would have on covered entity holding company liquidity requirements as well as its broader impacts on market

[30] Any leverage-based LTD requirements would need to be revised commensurately, reflecting the fact that leverage capital requirements are intended to be a backstop and not a binding requirement. See, e.g., Jerome H. Powell, "Central Clearing and Liquidity" (June 23, 2017), https://www.federalreserve.gov/newsevents/speech/powell20170623a.htm ("A risk-insensitive leverage ratio can be a useful backstop to risk-based capital requirements. But such a ratio can have perverse incentives if it is the binding capital requirement because it treats relatively safe activities, such as central clearing, as equivalent to the most risky activities.").

[31] SIFMA comments on Advanced Notice of Proposed Rulemaking, Resolution-Related Resource Requirements for Large Banking Organizations, Jan. 23, 2023, https://www.sifma.org/wp-content/uploads/2023/01/Advanced-Notice-of-Proposed-Rulemaking-Resolution-Related-Resource-Requirements-for-Large-Banking-Organizations.pdf.

[32] See Board of Governors of the Federal Reserve System and Federal Deposit Insurance Corporation, Resolution-Related Resource Requirements for Large Banking Organizations, 87 Fed. Reg. 64170 (Oct. 24, 2022).

[33] A retail broker-dealer subsidiary could be sold or wound down under a proceeding pursuant to the Securities Investor Protection Act ("SIPA"), which is designed to protect retail investors. The main insolvency imperative would be to transfer customer accounts to another broker-dealer, and the Securities Investor Protection Corporation has a well-established and proven process for executing such a resolution.

[34] In this respect, SIFMA and SIFMA AMG notes that non-GSIB LBOs affiliated with a retail broker-dealer are already subject to full (100 percent) standardized liquidity requirements (liquidity coverage ratio and net stable funding ratio).

[35] As discussed further below in this Section, the agencies have correctly exempted such IDIs from the internal LTD requirement in the proposal, and we believe that they should continue to do so going forward in the event that the agencies decide to impose an internal LTD requirement for some firms.

capacity and liquidity. This recalibration would require the agencies to re-estimate the impacts of the internal LTD requirement and complete a thorough cost-benefit analysis, prior to finalizing the rule. As discussed above in Section II, the agencies should also take into account the impacts of the Basel III Endgame final rule on overall LTD levels. A lower calibration of the internal LTD requirement for Categories III and IV holding companies would also be appropriate and consistent with the letter and spirit of the requirement to tailor enhanced prudential standards under the EGRRCPA, as Federal Reserve Chair Powell recently highlighted in testimony before Congress.[36]

Although the above impact and cost-benefit analysis should ultimately guide the recalibration of the internal LTD requirement, we recommend that the agencies consider two potential approaches to reconfiguring the requirement. First, the agencies should consider replacing the internal LTD requirement with a more flexible internal "gone loss-absorbing capacity" requirement. Any of the following internal loss-absorbing resources would satisfy this alternate requirement:

- Eligible LTD (with any minimum composition requirement relating to internal LTD at a reduced calibration for IDIs whose parent holding companies have external LTD satisfying any LTD requirement in full);
- Any Level 1 HQLA of a covered entity holding company, covered IHC or funding affiliate, or any internal demand deposit/other short-term debt instruments issued by its IDI, so long as these instruments are pledged to secure the holding company's obligation to use those financial assets to provide capital support to its covered entity IDI subsidiaries, without any such internal deposit or other short-term extension of credit being required to satisfy the conditions of eligible internal debt securities;[37] or
- Any other means jointly approved by the agencies as part of the 165(d) resolution planning process or otherwise.

Second, at a minimum, the internal LTD requirement for covered entities should be recalibrated downwards to 2 percent of RWAs. Under the proposal, the internal LTD requirement is currently calibrated to the "greater of 6 percent of the covered IDI's total [RWAs], 3.5 percent of its average total consolidated assets and 2.5 percent of its total leverage exposure if the covered IDI is subject to the supplementary leverage ratio." According to the agencies, the proposed calibration is intended to "be sufficient to capitalize a newly formed bridge depository institution with an amount necessary to comply with the minimum leverage capital requirements and common equity tier 1 risk-based capital requirements plus buffers applicable to ordinary non-bridge IDIs . . . ."[38] SIFMA and SIFMA AMG believe that this proposed calibration and the agencies' rationale is unrealistic and overly conservative for the following reasons.

As contemplated by the prompt corrective action ("PCA") framework under section 38 of the Federal Deposit Insurance Act ("FDIA"), a covered entity is almost certain to have going-concern leverage capital of at least 2 percent of its average total assets at the time it reaches its point of non-viability.[39] In

[36] See Economic Growth, Regulatory Relief, and Consumer Protection Act, Pub. L. No. 115-174, sec. 401, 132 Stat. 1296 (2018). See also Federal Reserve's Semi-Annual Monetary Policy Report: Hearing Before the H. Comm. on Fin. Servs., 118th Cong. (Mar. 8, 2023) (testimony of Chair Powell in response to a question regarding a potential LTD requirement for Categories I-IV banking organizations) ("We believe strongly and always have in tailoring to address the different size and risk characteristics of financial institutions and certainly nothing like that for the regionals. They won't have anything like what the very large, most systemically important banks have in terms of overall regulation . . . We're required by the law now and we're doing this [tailoring]. Dodd-Frank actually required us, suggested that we should tailor, and then S. 2155 required it. And anything that we do will reflect appropriate tailoring.").

[37] These intercompany deposits or other debt instruments would not, however, be required to meet the definition of eligible internal LTD.

[38] 88 Fed. Reg. 64524, 64533.

[39] See 12 U.S.C. § 1831o; see also 12 CFR § 6.4(b)(5); 12 CFR § 208.43(b)(5); 12 CFR § 324.403(b)(5). The PCA framework generally requires the appropriate Federal banking agency to promptly close a critically undercapitalized IDI and appoint a receiver or conservator. See 12 U.S.C. § 1831o(h).

addition, unlike a resolution strategy involving the recapitalization of material subsidiaries so they can continue to operate as going concerns outside their own resolution proceedings, a bridge-bank, purchase and assumption transaction or other alternative resolution strategy does not require enough LTD to fully recapitalize the IDI subsidiary. It is therefore not reasonable for the agencies to assume that there should be enough internal LTD to fully recapitalize the IDI subsidiary at the requisite capital level, *plus* buffers, applicable to ordinary non-bridge IDIs—even with some balance sheet depletion. The minimum common equity tier 1 ("CET1") capital level of 4.5 percent of RWAs,[40] without any applicable buffers, should be a sufficient recapitalization target. Indeed, the FDIA expressly provides that a bridge bank is not subject to capital requirements.[41] It is unclear why, especially in light of the statutory exemption, the agencies would believe that a bridge bank must be recapitalized at the same level as the pre-failure IDI—that is, at a level able to satisfy both the minimum CET1 capital and buffer requirements.

The agencies should revise these overly conservative assumptions by (1) assuming a starting point of 2 percent of RWAs, as contemplated by the PCA framework, instead of zero capital for full depletion of capital; (2) using an ending point of 4.5 percent of RWAs, reflecting the CET1 capital requirement necessary to be considered adequately capitalized under the agencies' regulations without any buffers; and (3) in light of the revised assumptions, provide for a balance sheet depletion allowance of 0.5 percentage points. These revised assumptions would result in an internal LTD requirement equal to 2 percent of RWAs rather than the proposed 6 percent of RWAs. The agencies should also revise any leverage-based LTD requirements commensurately.

SIFMA and SIFMA AMG Support the Agencies' Proposal to Continue to Exclude U.S. GSIBs from the Internal LTD Requirement. An Internal LTD Requirement Would Also Be Inappropriate for Foreign GSIBs' IHCs and non-GSIB LBOs That Operate Primarily as Retail Broker-Dealers.

To the extent that the agencies retain the internal LTD requirement in the final LTD rule, they should exempt certain firms from this requirement. First, consistent with the LTD proposal, the agencies should abstain from extending internal LTD requirements to IDI subsidiaries of U.S. GSIBs because they are already subject to considerable gone-concern loss-absorbing capacity requirements under the 165(d) resolution planning process. Specifically, as the agencies recognize, U.S. GSIBs (i) are "subject to the most stringent capital, liquidity, and other prudential standards in the United States" and (ii) have adopted resolution plans reflecting guidance from the Federal Reserve and the FDIC that establishes a capital and liquidity framework for resolution.[42] This guidance includes RCAP, which is designed to provide adequate maintenance of loss-absorbing resources at the parent level of material subsidiaries such that all material subsidiaries, including IDIs, could be recapitalized in the event of resolution under the SPOE resolution strategies adopted by U.S. GSIBs. Accordingly, the agencies should continue to not extend the internal LTD requirements to IDI subsidiaries of U.S. GSIBs, and instead should continue to implement gone-concern loss-absorbing requirements through the 165(d) resolution planning process.

The agencies should also exempt IHCs of foreign GSIBs from complying with the internal LTD requirement for their U.S. IDI subsidiaries as these institutions and their parent companies are already subject to sufficiently stringent capital, liquidity and prudential standards. The IHCs of foreign GSIBs are already subject to LTD, TLAC and clean holding company requirements under the TLAC rule as well as 165(d) resolution planning requirements. In addition, the top-tier parent entities of these IHCs are subject to home-country loss-absorbing capacity and resolution-related requirements. In many cases, the supervision and regulation of foreign GSIBs by their home country supervisors is comparable to that for U.S. GSIBs (e.g., home country regulators apply comparable capital and liquidity allocation requirements to foreign GSIBs). Considering these requirements together, foreign GSIBs' IHCs are subject to a level of

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[40] See 12 CFR § 6.4(b)(2)(iii); 12 CFR § 208.43(b)(2)(iii); 12 CFR § 324.403(b)(2)(iii).

[41] See 12 U.S.C. § 1821(n)(5).

[42] 88 Fed. Reg. 64524, 64526.

consolidated regulation that should exempt them from the internal LTD requirement for their U.S. IDI subsidiaries.

Beyond the U.S. GSIBs and IHCs of foreign GSIBs, an internal LTD requirement at the IDI level would be inappropriate for covered entity non-GSIB LBOs that operate primarily as retail broker-dealers. As SIFMA noted in its January 2023 letter[43] to the ANPR on this issue,[44] non-GSIB LBOs whose primary business model involves the operation of a retail broker-dealer should be given special consideration in the application of any enhanced resolution-related resource requirements, such as internal LTD requirements. This special consideration first stems from the fact that these firms generally have a simple organizational structure and low-risk profile relative to GSIBs and other non-GSIB LBOs. SIFMA's response to the ANPR contains a more detailed discussion of the relatively low risk that these firms pose to U.S. financial stability and the enhanced prudential standards to which they are already subject (including, in certain cases, full (100 percent) standardized liquidity requirements), as well as potential mechanisms for categorizing such organizations.

In addition, these non-GSIB LBOs that operate primarily as retail broker-dealers can be effectively resolved under existing frameworks without adverse consequences for U.S. financial stability. The resolution of these firms may proceed in an especially smooth and orderly manner, in part because their retail broker-dealer and registered investment adviser subsidiaries can be sold to a wide range of possible acquirers without transferring an affiliated IDI as part of the sale since an affiliated IDI is not necessary to operate a retail broker-dealer business. Any large IDI affiliated with a non-GSIB LBO broker-dealer could be separately resolved under existing IDI resolution planning regimes. There are also existing separate and effective resolution mechanisms for retail broker-dealer firms, such as the SIPA framework. Requiring pre-positioning of resources at the IDI would also generally constrain flexibility for LBO retail broker-dealers to deploy resources where they are most needed, including to their broker dealer subsidiaries, during business-as-usual and times of stress, thus undermining their resiliency in a manner inconsistent with statutory source of strength requirements.[45] Finally, these firms would also be subject to a full external "capital refill" LTD calibration that would already supply the necessary resources to be deployed flexibly, mitigating the need for a separate internal LTD requirement.

For these reasons, we recommend that covered entity non-GSIB LBOs that operate primarily as retail broker-dealers be exempt from an internal LTD requirement, assuming they can meet a full external "capital refill" LTD calibration at the holding company level.

IV. Definition of Covered Debt Instrument: *The agencies should clarify that the definition of "covered debt instrument" only applies to an IDI subject to a LTD requirement.*

Any final rule should be revised to provide that, for purposes of the deduction framework under the capital rule, the definition of "covered debt instrument" only applies to an IDI that is subject to a LTD requirement (*i.e.*, unsecured debt issued by an IDI that is not subject to a LTD requirement is not included). Specifically, clause (1)(i) of the proposed revised definition of covered debt instrument should refer to a subsidiary subject to a LTD requirement under proposed new Part 54, 216, or 374, instead of any subsidiary of a depository institution holding company subject to a LTD requirement under Part 238 or Part 252.

Under the existing definition of a covered debt instrument, only instruments issued directly by a globally systemically important BHC or Covered IHCs are included. The Agencies indicate in the proposal that the amendments to the definition of covered debt instrument are intended to reflect the wider scope

[43] SIFMA, Comments on Advanced Notice of Proposed Rulemaking, Resolution-Related Resource Requirements for Large Banking Organizations (Jan. 23, 2023), https://www.sifma.org/wp-content/uploads/2023/01/Advanced-Notice-of-Proposed-Rulemaking-Resolution-Related-Resource-Requirements-for-Large-Banking-Organizations.pdf.

[44] See Board of Governors of the Federal Reserve System and Federal Deposit Insurance Corporation, Resolution-Related Resource Requirements for Large Banking Organizations, 87 Fed. Reg. 64170 (Oct. 24, 2022).

[45] Dodd-Frank Wall Street Reform and Consumer Protection Act, Title VI, § 616, 12 USC 1831o–1 (2021).

of organizations (i.e. "covered companies") subject to LTD requirement but do not provide any rationale for the inclusion of instruments issued by subsidiaries of covered companies. The stated intent of these deductions is to "reduce interconnectedness and contagion risk among financial institutions by discouraging banking organizations from investing in the capital [and eligible LTD] of other financial institutions".[46] However, as currently drafted, the proposed definition of covered debt instruments would appear to scope in certain unsecured exposures to subsidiaries of covered companies that do not count as capital or eligible long-term debt.

V. LTD Implementation: ***The transition period for the LTD proposal should follow sequentially after the transition period for the Basel III Endgame proposal to facilitate capital accretion and ensure that the market can absorb new LTD issuances.***

As the agencies acknowledge, because LTD is "generally more expensive than the short-term funding banking organizations could otherwise use, the [LTD proposal] is likely to raise funding costs in the long run."[47] This rise in cost would likely impact the ability of covered entities to accrete additional capital to prepare for any final rule to implement the Basel III Endgame proposal. As a result, banking organizations would need to make more extensive changes to their lending activity to comply with the new rules, which could reduce credit availability and raise costs for borrowers.

To mitigate these concerns, the agencies should consider sequencing the transition period of any new LTD requirement with the transition period for any final rule to implement the Basel III Endgame proposal, which would help to facilitate the accretion of capital at banking organizations and minimize detrimental impacts to borrowers. Specifically, the transition periods for the finalized LTD and Basel III Endgame proposals should run sequentially, rather than concurrently, to allow banking organizations to prioritize capital accretion without increased funding costs related to the issuance of new LTD. In other words, the first year of the transition period for any new LTD requirements should begin following the end of the transition period for any final rule to implement the Basel III Endgame proposal. This approach would appropriately prioritize the accretion of capital. It would also (1) ensure that banking organizations could meet any new LTD requirements in a timely manner; and (2) provide more time for the market to absorb the large volume of expected LTD issuances and for smaller banks to build their investor bases and debt marketing programs.

VI. Clean Holding Company Requirements: ***The proposal's limited exemptions to the prohibition on covered entity holding companies entering QFC arrangements with third parties should be expanded to cover normal course transactions that do not conflict with the agencies' underlying policy objectives. The agencies should also clarify that since clean holding company requirements are primarily designed to facilitate a SPOE resolution, the same requirements should not be applied to firms with alternative resolution strategies.***

We welcome the agencies' decision to provide limited exemptions to the prohibition on covered entity holding companies entering normal course QFC arrangements with third parties, such as underwriting agreements. As the agencies note, these normal course transactions would not pose a material risk to the orderly resolution of covered entities, nor would they affect the stability of the U.S. banking or financial system.[48]

However, we recommend that the agencies extend the exemptions on QFC arrangements with third parties to additional normal course QFC transactions that similarly would not interfere with an orderly

[46] 88 Fed. Reg. 64545.

[47] 88 Fed. Reg. 64524, 64552.

[48] 88 Fed. Reg. 64524, 64547.

SPOE resolution or cause financial stability risks. The exemptions in the proposal should be extended to include the following transactions:

- Any securities contract entered into by a covered entity holding company to execute a cash tender offer, exchange offer, consent solicitations or open market or bilaterally negotiated repurchase transaction to redenominate, amend, exchange, replace or retire debt or equity securities;
- Any agreement for the spot purchase or sale of securities; and
- Any swap contract entered into by a covered entity holding company to hedge exposures related to an employee deferred compensation plan.

Despite the agencies' positive steps forward on the QFC exemptions to the clean holding company requirement, we are not supportive of the extension of the clean holding company requirements to holding companies that rely on a non-SPOE resolution strategy. The clean holding company requirements were originally put in place to facilitate the orderly resolution of a bank holding company using a SPOE strategy, and the preamble to the TLAC rule focuses extensively on the purported benefits of such a requirement in SPOE strategies to enable the continued operation of a covered entity holding company's operating subsidiaries in the event of a resolution.[49] Applying these same requirements to a covered entity holding company relying on a non-SPOE resolution strategy, which presupposes that the covered entity holding company's subsidiaries would also enter resolution proceedings (rather than continue to operate), would not serve the purpose of advancing an orderly resolution of the firm to the same extent.

Indeed, the agencies have already recognized the limited utility of the clean holding company requirements by exempting covered IDIs from these requirements. While the agencies have noted that "[i]n the case of an MPOE resolution . . . the [clean holding company requirements] would limit the extent to which a subsidiary of a covered entity would experience losses or disruptions in its operations as a result of the failure of the covered entity prior to and during resolution," the costs of limiting the funding source of the holding company outweighs any such potential benefits. In fact, the agencies explicitly recognize that "the benefits of these [clean holding company] requirements . . . may be more significant for covered entities with an SPOE resolution strategy" compared to those relying on a non-SPOE strategy.[50]

In addition, the agencies' justification that banking organizations relying on an MPOE resolution strategy in their resolution plans should be subject to clean holding company requirements because they may switch to an SPOE strategy in the future or ultimately be resolved under such a strategy seems weak.[51] If a firm switches from a MPOE to SPOE strategy in the future, it could instead become subject to clean holding company requirements at that time. Imposing clean holding company requirements in advance of such a switch appears to undermine the legitimacy of the MPOE strategy as a valid alternative strategy to SPOE. The agencies should therefore not apply clean holding company requirements to holding companies that rely on a non-SPOE strategy.

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[49] See, e.g., Board of Governors of the Federal Reserve System, 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, 82 Fed. Reg. 8266, 8298 (Jan. 24, 2017). ("The covered holding companies themselves would be prohibited from relying on short-term funding, reducing the run risk associated with the failure of such an entity. This goal is particularly important in light of the likely liquidity needs of a GSIB during SPOE resolution, because a short-term funding run on a covered holding company would drain liquidity that may be needed to support the group's operating subsidiaries."); see also 88 Fed. Reg. 64524, 64541 ("In the case of SPOE resolution, these provisions support the goal of that resolution strategy to achieve the rapid recapitalization of the material subsidiaries of a covered entity with minimal interruption to the ordinary operations of those subsidiaries. The proposed clean holding company restrictions would advance this goal by prohibiting transactions that would distribute losses that should be borne solely by a covered entity to the covered entity's subsidiaries.").

[50] 88 Fed. Reg. 64524, 64541.

[51] *Id.*

VII. Changes to the Existing TLAC Rule: *The proposed changes to the calculation of TLAC should not be adopted. However, if they are adopted, they should only apply to newly issued LTD.*

The proposal would amend the calculation of the TLAC requirement for those firms subject to the TLAC rule (i.e., U.S. GSIBs and foreign GSIBs' IHCs) by allowing only 50 percent of eligible LTD with a maturity of one year or more, but less than two years, to count toward a firm's minimum TLAC requirement (at present, this haircut applies only to these firms' minimum LTD requirement). In the proposal, the Federal Reserve Board states that this amendment is intended both to simplify the rule and to "incentivize firms to reduce reliance on eligible LTD with maturities of less than two years,"[52] thus reducing the vulnerability of their LTD loss-absorbing capacity to potential runs.

Although the proposed change may simplify the rule, it would do little to advance the second objective. Firms subject to the existing TLAC rule already overwhelmingly call LTD instruments prior to the last year before they mature because of the existing LTD haircut and prevailing market practices. There is no evidence provided in the proposal to suggest that there is an over-reliance on debt maturing within one-to-two years amongst this group of firms; indeed, the Federal Reserve Board acknowledges that the potential effects of the proposed change "appear to be modest," raising the question as to why the change is necessary in the first place. Moreover, these firms have developed their funding plans and business strategies based on the current TLAC rule's treatment of LTD. Even if the overall impact is "modest," modifying the TLAC calculation method, particularly at a time when significant RWA increases are likely to result from the implementation of the Basel III Endgame proposal, would needlessly impair firms' funding plans and business strategies without yielding any significant benefit.

Given the above, the current TLAC rule's approach to LTD with a maturity of one year or more but less than two years should be retained in the final rule. In the event that the proposed treatment is adopted in the final rule, then the haircut change should only apply to newly issued LTD and not existing eligible LTD that was issued in reliance on the prior calculation method. As a general matter, impacted firms should have an opportunity to plan and not be subject to such a sudden shift in the treatment of already-issued LTD.

VIII. Uninsured Deposits: *The agencies have asked about the different types of uninsured deposits. We urge them to recognize the differing levels of risks posed by different types of these deposits.*

As reflected in the proposal, the agencies continue to focus on the "rise to vulnerabilities" and amplified systemic contagion risks at banking organizations that increasingly rely on uninsured deposits.[53] We believe that the agencies have missed key nuances in making such broad statements that do not distinguish between different types of uninsured deposits. In evaluating risks associated with uninsured deposits, the agencies should consider that some types of uninsured deposits are observably stable even in periods of financial stress, which they have recognized in the past. For example, the agencies have stated that operational deposits related to the clearing, custody, and cash management services "present less liquidity risk during a stress period" and "are more stable than non-operational funding."[54] We therefore urge the agencies to acknowledge and consider the important distinctions among different types of uninsured deposits and the reasons why many customers place deposits at a bank that exceed the federal deposit insurance limit. For example, deposits associated with payment, settlement, and payroll administration are generally more stable, and must meet requisite criteria under liquidity regulations which recognize such deposit stability.

[52] 88 Fed. Reg. 64547.

[53] 88 Fed. Reg. 64524, 64525-26.

[54] Liquidity Coverage Ratio: Liquidity Risk Measurement Standards, 79 Fed. Reg. 61439, 61498, 61502 (Oct. 10, 2014). Under the agencies' liquidity coverage ratio rules, operational deposits are assigned outflow rates far lower than other uninsured wholesale deposits. Compare 12 CFR § 329.32(h)(4) (25 percent outflow rate for uninsured operational deposits) with 12 CFR § 329.32(h)(1), (5) (40 to 100 percent outflow rates for uninsured, non-operational unsecured wholesale funding).

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SIFMA and SIFMA AMG appreciate the agencies' consideration of these comments and would be pleased to discuss any of these views in greater detail if it would assist with their deliberations. Please contact Peter Ryan at pryan@sifma.org or at (202) 962-7452 if you wish to discuss the points raised in this letter further.

Sincerely,

Kenneth E. Bentsen, Jr.
CEO and President
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