January 16, 2024

VIA ELECTRONIC SUBMISSION

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

Re: Docket No. R–1814 and RIN 7100–AG65: Regulatory Capital Rule: Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Systemic Risk Report (FR Y-15)

Ladies and Gentlemen:

The Financial Services Forum (the "Forum") and the Bank Policy Institute[1] appreciate the opportunity to submit this letter to the Board of Governors of the Federal Reserve System (the "FRB") regarding its proposed rule on capital surcharges for global systemically important bank holding companies ("GSIBs") and the Systemic Risk Report (FR Y-15) (the "Proposal").[2] The

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1 The Financial Services Forum is an economic policy and advocacy organization whose members are the chief executive officers of the eight largest and most diversified financial institutions headquartered in the United States. Forum member institutions are a leading source of lending and investment in the United States and serve millions of consumers, businesses, investors and communities throughout the country. The Forum promotes policies that support savings and investment, deep and liquid capital markets, a competitive global marketplace and a sound financial system.

The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation's small business loans, and are an engine for financial innovation and economic growth.

2 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). The FRB, the Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency (the "OCC"; and, collectively, the "Agencies") simultaneously issued for comment a proposal on the U.S. implementation of the Basel III endgame. Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. 64028 (Sept. 18, 2023) (the "Capital Proposal").

proposed changes would apply to all of the Forum's member institutions ("member institutions"), the U.S. GSIBs.

The FRB adopted a final rule in 2015 (the "2015 Rule") to establish a methodology to identify U.S. GSIBs and assign each a risk-based capital surcharge. The 2015 Rule was designed to capture a U.S. GSIB's systemic importance, such that the U.S. GSIBs are required to hold additional capital relative to other non-GSIB banking organizations.[3] The "principal statutory impetus" for the GSIB surcharge is the Dodd-Frank Act's mandate that the FRB "adopt enhanced capital standards to mitigate the risk posed to financial stability by certain large financial institutions."[4]

Since the implementation of the Dodd-Frank Act and subsequent regulatory reforms, the U.S. GSIBs have become more resilient, liquid and resolvable than ever before, with robust levels of capital. As Chair Powell said in his most recent confirmation hearing, "capital and liquidity levels at our largest, most systemically important banks are at multi-decade highs."[5] Similarly, the 2023 Financial Stability Oversight Council Annual Report emphasized that, for GSIBs, "the Common Equity Tier 1 Capital (CET1) ratio has trended up since early 2022 and is now on par with the highest levels observed in more than 20 years."[6] The U.S. GSIBs also have continually served as a source of strength to the economy—including through COVID-19 and the spring 2023 regional bank failures.[7]

Our member institutions support certain of the changes in the Proposal that are practical and reasonable. In particular, we support the FRB's proposed change to narrow the method 2 score band ranges as well as the move to four-quarter averages rather than relying solely on a December 31 reporting date. Given the U.S. GSIBs' position of strength, however, many of the proposed changes, which are generally expected to result in increased GSIB surcharge scores and capital surcharges, are unwarranted.

Our member institutions play an essential role in providing credit, liquidity and a range of key financial services, which are fundamental to the continued growth and prosperity of the U.S. economy. The ability of our member institutions to play this role, however, critically depends on efficiently calibrated regulation. Financial regulations that do not adhere to this key principle result in an inefficient financial system that misallocates capital in a way that can have a detrimental effect on the businesses and households that our member institutions serve, and on the U.S. economy as a

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3 Regulatory Capital Rules: Implementation of Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies, 80 Fed. Reg. 49082, 49082 (Aug. 14, 2015).

4 80 Fed. Reg. at 49109.

5 Jerome Powell, "Nomination Hearing," Testimony before the United States Senate Committee on Banking, Housing, and Urban Affairs (Jan. 11, 2022), https://www.federalreserve.gov/newsevents/testimony/powell20220111a.htm.

6 Financial Stability Oversight Council, "Annual Report 2023" at 52, https://home.treasury.gov/system/files/261/FSOC2023AnnualReport.pdf.

7 In particular, based on the estimates in both the Proposal and the Capital Proposal, the disproportionate impact these proposals would have on U.S. GSIBs as compared to Category III and IV firms is inconsistent with statements from regulators explicitly citing the 2023 regional banking turmoil as an impetus for the proposed increases in capital requirements. *See, e.g.,* FRB, "Statement by Vice Chair for Supervision Michael S. Barr" (July 27, 2023), https://www.federalreserve.gov/newsevents/pressreleases/barr-statement-20230727.htm.

whole, with no clear corresponding benefit to the resilience of the financial system. As discussed further throughout this letter, the Proposal is not efficiently calibrated and unfortunately would result in precisely these detrimental effects.

I. The Proposal is based on an outdated methodology because it fails to update the fixed method 2 coefficients to account for economic growth and inflation.

A core inadequacy of the Proposal is that the GSIB surcharge is already inflated because the FRB has not addressed the impact of economic growth and inflation on the fixed coefficients in method 2 since the 2015 Rule. The Proposal fails to review the coefficients to the surcharge and make long-overdue adjustments to them, resulting in a GSIB surcharge that is unduly high. Assuming that the GSIB surcharge was originally calibrated to a level considered adequate to capture the systemic footprint of the U.S. GSIBs at the time of its adoption, with the coefficients held constant, effectively the surcharge has been materially increasing over time. Given the absence of a significant increase in the systemic risk posed by U.S. GSIBs since 2015, the GSIB surcharge is thus materially over-calibrated. In particular, we estimate that the FRB's reliance on this outdated methodology results in U.S. GSIBs unnecessarily maintaining approximately $80 billion in capital.[8]

II. The Proposal fails to adequately justify its changes, including because it fails to consider a holistic perspective of the capital framework.

A. *The Proposal fails to adequately justify its changes, empirically or otherwise.*

Many of the proposed changes are not empirically supported or adequately justified. Even when justifications are included, they are often brief and conclusory and fail to address evident counterarguments. This critical lack of justification suggests that there is inadequate evidence to support the proposed changes. The FRB also has not undertaken analysis or identified deficiencies in the U.S. GSIB surcharge framework or with regard to the capital levels of the U.S. GSIBs more generally that indicate increased capital is necessary to mitigate systemic risk. Given the insufficient justification for the proposed changes, the public is not able to fully understand or adequately respond to the Proposal.

Further, the FRB's analysis is not granular enough to provide the comprehensive, transparent and rigorous analysis that is necessary for the public to evaluate the Proposal in the comment process. Therefore, the FRB must conduct a more rigorous and comprehensive quantitative impact analysis that separately considers each of the key changes.

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[8] *Cf.* Sean Campbell, "The Federal Reserve Should Revise the U.S. GSIB Surcharge Methodology to Reflect Real Risks and Support the Economy," Forum: Banknotes Blog (Oct. 11, 2023), https://fsforum.com/news/the-federal-reserve-should-revise-the-u-s-gsib-surcharge-methodology-to-reflect-real-risks-and-support-the-economy.

B. *The Proposal fails to consider holistically the broader capital framework.*

Similarly, it is crucial that the FRB thoroughly consider and adequately justify the effect of the Proposal, the Capital Proposal and other changes to the capital framework[9] holistically and on an aggregate basis to ensure the GSIB surcharge is appropriately calibrated. Moreover, the public should have the ability to understand and respond to a holistic review of the capital framework. For example, the FRB acknowledges in the Proposal that the increase in risk-weighted assets ("RWA") in the Capital Proposal would proportionally increase the dollar amounts of the capital surcharge changes in this Proposal. This compounding effect, however, is then insufficiently considered, discussed or quantified.[10] Moreover, the fixed-coefficient methodology is not calibrated to account for these material increases in RWA and, correspondingly, the substantial overall capital increases that would result from the Capital Proposal, the bulk of which would be borne by the U.S. GSIBs.[11]

III. Many of the proposed changes would worsen disparities with foreign jurisdictions, which could harm the U.S. economy.

The Proposal and the current U.S. GSIB surcharge are inconsistent with both the Basel framework and its implementation in other jurisdictions. In particular, the U.S. GSIB surcharge already reflects more stringent standards than the framework set forth by the Basel Committee on Banking Supervision ("Basel Committee") because it includes a second calculation methodology (method 2) in addition to the methodology based on the Basel standards (method 1), and the method 2 surcharge is generally higher.[12] The excessive stringency of the U.S. standard in both the Proposal and the current approach worsen, rather than improve, international capital discrepancies, hurting U.S. economic competitiveness and undermining the Basel Committee objective of enhanced comparability.[13]

The preexisting and proposed divergences from the Basel framework are not in service of American interests—rather, they would impose additional requirements on U.S. GSIBs that would harm the

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9 For example, following the release of the Proposal and the Capital Proposal, the Agencies also released a proposed rule to require large banking organizations to hold minimum amounts of long-term debt and to make certain changes to the FRB's total loss-absorbing capacity rule that will affect capital required to be issued by U.S. GSIBs. 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).

10 88 Fed. Reg. at 60398. This multiplicative effect is discussed at further length in our letter commenting on the Capital Proposal.

11 As discussed in our letter commenting on the Capital Proposal, the Agencies should undertake a comprehensive quantitative analysis of the interactions that the Proposal would have with all of the Agencies' prudential regulatory requirements and publish the results of that analysis. The results of this analysis should inform any revision to the current capital framework.

12 Basel Committee, "Regulatory Consistency Assessment Programme (RCAP) Assessment of Basel III G-SIB framework and review of D-SIB frameworks – United States" at 5 (June 2016) ("Some aspects of the G-SIB framework in the US are more conservative than the Basel framework. This includes an alternative assessment methodology that generally results in higher minimum capital requirements and broader and more frequent disclosure requirements.").

13 Basel Committee, "Basel III: Finalising post-crisis reforms" at 1 (Dec. 2017), https://www.bis.org/bcbs/publ/d424.pdf.

American economy and the ability of U.S. GSIBs to compete internationally. Similarly, the potential increases in required capital that would result from the Proposal would exacerbate the movement of financial activity outside the regulated banking system, threatening consumers and financial stability.

Recommendations

With these considerations in mind, in the attached Annex, we wish to highlight the following key observations and recommendations:

- **The final rule should recalibrate the GSIB surcharge fixed coefficient methodology to account for economic growth since the 2015 Rule and other factors unrelated to systemic risk.** We recommend that the final rule recalibrate the fixed coefficients in method 2 of the GSIB surcharge in accordance with the FRB's commitment in the 2015 Rule that it would periodically review the coefficients to reflect economic growth. Further, we recommend that the FRB adopt a procedural mechanism to ensure that the GSIB surcharge fixed coefficient methodology is periodically reassessed every two years and, where necessary, recalibrated to better reflect the pace of economic growth, overall GSIB resiliency and other factors.

- **The weight of the short-term wholesale funding ("STWF") category should be recalibrated to 20 percent, consistent with the intention of the FRB in enacting the 2015 Rule.** In adopting the 2015 Rule, the FRB explained that a fixed conversion factor would apply to the STWF category with the intention that it would receive a 20 percent weight (equal to the other categories).[14] The weight of the STWF category within the method 2 score, however, has been approximately 30 percent since the firms began reporting this item in the FR Y-15. Accordingly, we recommend that the fixed conversion factor be updated such that the calibration equally weights the STWF category to the other categories at 20 percent.

- **The final rule should not require reporting of the average of daily values or, in some instances, the average of monthly values.** The proposed change to require averaging of daily values is unnecessary, as the move to narrower bands would remove incentives for banks to temporarily adjust their balance sheets at a reporting date in a way that is not reflective of ongoing systemic risk and so would provide no marginal benefit to measuring or reducing systemic risk. It is also inconsistent with the Basel standard and would present significant operational challenges and disadvantages. Accordingly, we recommend that the final rule not require U.S. GSIBs to report any indicator as the average of daily values of the indicator over the reporting quarter. Instead, we recommend that the majority of these indicators use the average of month-end values, except for certain indicators with particularly difficult technical challenges in using month-end values, in which case, we recommend using quarter-end, point-in-time measurements.

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[14] 80 Fed. Reg. at 49100-01.

- **The final rule should calibrate the method 2 GSIB score bands to better correspond to the current rule and not artificially inflate method 2 surcharges.** We support the FRB's proposed change to narrow the method 2 score band ranges, which is practical and reasonable. However, we do not believe the bands are appropriately reassigned. We recommend adjusting the score bands to ensure they better align with the current method 2 score bands and surcharges and to ensure this change does not inappropriately raise capital requirements.

- **The final rule should not expand the definition of "financial institution" used in the interconnectedness indicators to include exchange-traded funds ("ETFs").** The Proposal would expand the definition of "financial institution" for purposes of measuring interconnectedness to include ETFs, among other entities. However, this change is inadequately justified and would discourage U.S. GSIB interaction with ETFs, which are widely used as investment vehicles by the retail public. Accordingly, we recommend that the final rule not include ETFs in the definition.

- **The final rule should not include a firm's guarantees of client performance to a central counterparty ("CCP") with respect to client derivative clearing under the agency model in the affected indicators.** Under the Proposal, three indicators (intra-financial system assets and intra-financial system liabilities in the interconnectedness category and notional amount of over-the-counter ("OTC") derivatives in the complexity category) would include a firm's guarantees of client performance to a CCP with respect to client derivative clearing under the agency model. This proposed approach would unnecessarily discourage central clearing, harming end users with reduced access to cleared OTC derivatives and increased costs and, potentially, impairing financial stability. We recommend that the final rule not include a firm's guarantees of client performance to a CCP with respect to client-cleared derivative positions in an agency capacity in these three indicators.

- **The final rule should not include derivatives exposures in the systemic indicators for cross-jurisdictional claims and cross-jurisdictional liabilities.** Under the Proposal, the systemic indicators reported on the FR Y-15 for cross-jurisdictional claims and cross-jurisdictional liabilities would include derivatives exposures gross of collateral instead of being reported as memoranda items as they currently are. This proposed change is unnecessary and inadequately justified, particularly given the fact that derivatives exposures are already adequately captured in FR Y-15 systemic indicators in three categories and in other parts of the capital framework, such as the Standardized Approach for Counterparty Credit Risk ("SA-CCR"). Accordingly, we recommend that the final rule not add a measurement of derivatives exposures to cross-jurisdictional activity indicators. If the final rule nonetheless retains these proposed revisions, at a minimum, we recommend that the measurement of derivatives allows for netting of both cash and noncash collateral as a more accurate reflection of their risk profile.

- **The final rule and instructions to the FR Y-15 should not include the alpha factor in calculating exposure amounts for the interconnectedness indicators.** The Proposal

would specify that derivative exposures be calculated in accordance with 12 CFR 217.34(a), which for our member institutions means SA-CCR.[15] The preamble's discussion, however, is ambiguous as to how the potential future exposure ("PFE") multiplier and alpha multiplier would contribute to the calculation of PFE and replacement cost in the interconnectedness indicators. We recommend that the final rule and revised instructions to the FR Y-15 clarify that the alpha factor would not be included in the exposure calculation used for purposes of the interconnectedness indicators.

- **During the transition period, the GSIB surcharge should be determined based on a fully phased-in expanded risk-based approach ("ERBA") denominator.** We recommend that method 2 GSIB scores be calculated using fully phased-in ERBA RWA amounts, to the extent available.

- **The effective date of changes to a firm's GSIB surcharge requirement should not be changed.** The FRB seeks comment regarding "whether it would be appropriate to modify the effective date of changes to a firm's GSIB surcharge requirement following a change in its GSIB score."[16] We do not believe the effective date for an increase in the GSIB surcharge should change in the final rule. The current effective date is necessary to achieve the FRB's appropriate goals of facilitating capital planning and providing time for U.S. GSIBs to make appropriate adjustments.

- **The proposed changes should take effect at least one year after the date of adoption of a final rule.** Under the Proposal, the changes to FR Y-15 reporting would take effect relatively quickly, only two full calendar quarters after the date of adoption of the final rule.[17] Because the FRB is proposing a number of significant changes to FR Y-15 definitions and reporting methodology, we request that the proposed changes take effect at least one year after the date of adoption of a final rule in order to give banking organizations sufficient time to incorporate these changes into internal systems and processes. Moreover, if the recommendations discussed above regarding averaging for the affected indicators are not adopted, substantial additional time for compliance would be needed given the significant operational burdens associated with those changes, likely at least an additional year.

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15 FRB, "Draft Instructions for the Preparation of Systemic Risk Report: Reporting Form FR Y-15" (2023) at 30, 33, https://www.federalreserve.gov/reportforms/formsreview/20230727%20FR%20Y-15%20instructions%20NL.pdf, [hereinafter, "Proposed FR Y-15 Instructions"].

16 88 Fed. Reg. at 60390.

17 88 Fed. Reg. at 60396.

Thank you for considering these comments. Please feel free to contact Kevin Fromer (KFromer@fsforum.com) with any questions.

Respectfully submitted,

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Annex: Recommendations for the FRB

I. The final rule should recalibrate the GSIB surcharge fixed coefficient methodology to account for economic growth and other factors unrelated to systemic risk.

The Proposal neglects to include changes to the calibration of the GSIB surcharge despite the FRB's commitment in the 2015 Rule that it would periodically review the coefficients to reflect economic growth and "periodically reevaluate the framework to ensure that factors unrelated to systemic risk do not have an unintended effect on a bank holding company's systemic indicator scores."[18] Accordingly, we recommend that the final rule recalibrate the fixed coefficients in method 2 of the GSIB surcharge in accordance with the FRB's commitment. Further, we recommend that the FRB adopt a procedural mechanism to ensure that the GSIB surcharge fixed coefficient methodology is periodically reassessed every two years to ensure that the calibration of the GSIB surcharge better reflects the pace of economic growth or other factors.

A. Challenges and Concerns

1. *The current calibration does not take into account economic growth.*

In adopting the 2015 Rule, the FRB specifically acknowledged that "over time, a bank holding company's method 2 score may be affected by economic growth that does not represent an increase in systemic risk."[19] Accordingly, the FRB specifically committed that it would "periodically review the coefficients and make adjustments as appropriate" in order to "ensure changes in economic growth do not unduly affect firms' systemic risk scores."[20] In developing the fixed approach for converting a bank holding company's systemic indicator value into its method 2 score, the FRB used data from 2012 to 2013. In the full decade that has passed since that data was collected, U.S. nominal GDP has grown by approximately 61 percent.[21] Economic growth has the effect of inflating surcharge scores without any increase in systemic risk. Further, the FRB estimates the Proposal itself would also lead to an increase in method 2 GSIB scores by about 27 points across firms, corresponding to a 13-basis-point increase in the method 2 GSIB capital surcharge.[22] We believe recalibration is now necessary and long overdue to limit unintended consequences and promote continuity in both the financial sector and the economy.

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18 80 Fed. Reg. at 49085.

19 80 Fed. Reg. at 49088.

20 *Id.*

21 International Monetary Fund, "Nominal Gross Domestic Product for United States," retrieved from FRED, Federal Reserve Bank of St. Louis, https://fred.stlouisfed.org/series/NGDPSAXDCUSQ (comparing the GDP as of the third quarter of 2023 to the GDP as of the fourth quarter of 2013) [hereinafter, "Nominal GDP Data"].

22 88 Fed. Reg. at 60397.

2. *The current calibration does not take into account the compounding effect from the proposed increase in RWA in the Capital Proposal.*

Further, the fixed-coefficient methodology is not calibrated to account for the material increase in RWA and, correspondingly, overall capital that would be implemented under the Capital Proposal. The Agencies expect the bulk of this increase to be borne by the U.S. GSIBs. Specifically, the Agencies estimate that the Capital Proposal, if adopted, would increase RWA by 25 percent relative to currently binding measures of RWA for holding companies subject to Category I or II standards and "would increase binding common equity tier 1 capital requirements by an estimated 19 percent for holding companies subject to Category I or II capital standards."[23] Further, the FRB specifically acknowledges in the Proposal that "the dollar amounts of the capital surcharge changes under the proposal would be proportionally larger due to the change in risk-weighted assets" under the Capital Proposal, a compounding effect that would increase capital requirements under the GSIB surcharge despite there being no increase in systemic risk.[24] This effect is not sufficiently considered or justified by the FRB. To appropriately calibrate the GSIB surcharge, the FRB must consider the compounding effect of the increase in RWA and holistically evaluate the quantum of required capital that would result from its concurrent proposals.

3. *There is no justification for the GSIB surcharge to be materially increasing over time without any corresponding change in systemic risk.*

The method 2 fixed approach uses constants, which are "based on the average of the aggregate global indicator amounts for each indicator for year-end 2012 to 2013."[25] These fixed constants, therefore, do not account for the numerous regulatory reforms that have been implemented since those dates. These reforms have meaningfully reduced systemic risk, even while the GSIB surcharge has increased with inflation and economic growth. In particular, the calibration of the GSIB surcharge—both the Basel Committee's version and the U.S. version—does not reflect the enhancements to resiliency, liquidity and resolvability that have been achieved since the surcharge was first adopted, including: enhancements to resolution planning, minimum margin and capital requirements related to non-cleared swaps and security-based swaps, TLAC requirements, QFC contractual stay and recordkeeping requirements and enhanced supervisory practices.[26] There is nothing to suggest that U.S. GSIBs are causing increased risk to the financial system and if anything, U.S. GSIBs' resiliency during the COVID-19 pandemic and the spring 2023 bank turmoil

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[23] 88 Fed. Reg. at 64168 n.462, 64169 n.464.

[24] 88 Fed. Reg. at 60398.

[25] 80 Fed. Reg. at 49087.

[26] Minimum margin and capital requirements related to non-cleared swaps and security-based swaps were initially finalized in late 2015. Margin and Capital Requirements for Covered Swap Entities, 80 Fed. Reg. 74840 (Nov. 30, 2015). TLAC requirements for GSIBs were finalized on January 24, 2017. 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 (Jan. 24, 2017). QFC stay requirements were finalized on September 12, 2017. Restrictions on Qualified Financial Contracts of Systemically Important U.S. Banking Organizations and the U.S. Operations of Systemically Important Foreign Banking Organizations; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions, 82 Fed. Reg. 42882 (Sept. 12, 2017).

suggests the opposite—U.S. GSIBs are contributing to the overall stability of the financial system.[27] In addition, the FRB's capital planning and stress-testing programs already are designed to capture risks that are particularly acute for U.S. GSIBs, *e.g.*, the global market shock and the large counterparty default scenario.

The FRB has explained that the GSIB surcharge is based on the assumption that it is necessary to "reduce the likelihood that the failure or material financial distress of a GSIB will again pose a threat to U.S. financial stability" and to decrease the likelihood of failure in the first instance.[28] Accordingly, the GSIB surcharge must be recalibrated to reflect actual levels of systemic risk and not more.

4. *The current U.S. standard is more stringent than the Basel framework, which erodes the competitiveness of the U.S. banking sector and, when combined with other reforms, will likely weigh on the U.S. economy.*

Although ostensibly designed to implement the global standard established by the Basel Committee,[29] the U.S. GSIB surcharge is actually more stringent than the Basel Committee's standard. As discussed above, the U.S. GSIBs are generally subject to higher surcharges than their foreign counterparts, generally because of the use of method 2, which is more stringent than the Basel framework, rather than method 1. The average GSIB surcharge for our member institutions is 2.3 percent, while the asset-weighted average surcharge for their foreign peers is 1.2 percent.[30] The higher surcharge also then is applied to more stringent RWA calculations than for foreign GSIBs (both today and if the Capital Proposal were implemented), compounding the disparity. Moreover, the proposed changes would only further exacerbate the excessive stringency of U.S. requirements as compared to the Basel standard.

Because the Proposal would increase capital requirements for U.S. GSIBs relative to their foreign peers, U.S. GSIBs would be put at a disadvantage—both at home and abroad—negatively affecting the U.S. economy as a whole. U.S. GSIBs play an important and outsized role in helping U.S. companies gain access to and compete effectively in foreign markets. Moreover, equity capital is a primary cost of providing banking services. Therefore, higher surcharges would hurt the provision

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27 *See, e.g.,* FRB, "Supervision and Regulation Report" at 1 (Nov. 2020), https://www.federalreserve.gov/publications/files/202011-supervision-and-regulation-report.pdf [hereinafter, "FRB Supervision and Regulation Report"]; Alice Abboud, Elizabeth Duncan, et. al., "COVID-19 as a Stress Test: Assessing the Bank Regulatory Framework," Finance and Economics Discussion Series 2021-024. Washington: Board of Governors of the Federal Reserve System at 10 (Mar. 2021), https://www.federalreserve.gov/econres/feds/files/2021024pap.pdf; FRB, "Federal Reserve Board releases results of annual bank stress test, which demonstrates that large banks are well positioned to weather a severe recession and continue to lend to households and businesses even during a severe recession" (June 28, 2023), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20230628a.htm.

28 80 Fed. Reg. at 49092.

29 *See* Basel Committee, "Global systemically important banks: revised assessment methodology and the higher loss absorbency requirement" (July 2018), https://www.bis.org/bcbs/publ/d445.pdf.

30 Simple averages calculated using firm FFIEC 101 data and FSB data. *See* FSB, "2022 List of Global Systemically Important Banks (G-SIBs)" (Nov. 21, 2022), https://www.fsb.org/wp-content/uploads/P211122.pdf.

of banking services to U.S. companies and would ultimately be passed down to businesses and households that are seeking credit to make investments that contribute to economic growth. While estimated impacts vary, a range of studies from academics, standard-setting bodies (such as the Basel Committee) and central banks (such as the FRB and the Bank of England) all agree that higher required capital results in reduced economic output.[31]

As just one specific example, U.S. GSIBs are primary providers of foreign currency hedging products to American companies. Increased capital costs for U.S. GSIBs that result in higher hedging costs for U.S. companies operating abroad threaten the competitive standing of the entire U.S. economy. Therefore, excessive capital requirements that are more stringent than the Basel standards and the requirements of other jurisdictions hurt our economy and reduce our nation's productivity and our ability to compete internationally, with almost no marginal benefit to measuring or reducing systemic risk.

Moreover, an excessively stringent GSIB surcharge framework is unnecessary given the resilience of the U.S. GSIBs, which have robust levels of capital and have repeatedly served as a source of strength to the economy. Rather than being adversely affected by the spring 2023 bank failures, the U.S. GSIBs generally experienced deposit inflows and acted as sources of strength and support to the broader banking sector to avoid further market turmoil and cost to the economy, as they did during the COVID-19 pandemic.[32] Further, as discussed above, among all banking organizations, the U.S. GSIBs are at the forefront of regulatory reforms to reduce systemic risk.

5. *It is necessary to recalibrate coefficients to reflect any changes to related definitions or inputs.*

The Proposal would update the definitions of systemic indicators for the GSIB method 2 score without proposing any change to related coefficients. As noted above, coefficients are "based on the average of the aggregate global indicator amounts for each indicator for year-end 2012 to 2013,"

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[31] *See e.g.* Anil Kashyap, Jeremy C. Stein and Samuel G. Hanson. "An Analysis of the Impact of 'Substantially Heightened' Capital Requirements on Large Financial Institutions" (May 2010), https://scholar.harvard.edu/files/stein/files/impact_of_substantially_heightened.pdf; Federal Reserve Bank of Minneapolis, "The Minneapolis Plan To End Too Big To Fail" (Dec. 2017), https://www.minneapolisfed.org/~/media/files/publications/studies/endingtbtf/the-minneapolis-plan/the-minneapolis-plan-to-end-too-big-to-fail-final.pdf; Simon Firestone, Amy Lorenc and Ben Ranish, "An Empirical Economic Assessment of the Costs and Benefits of Bank Capital in the US, Finance and Economics," Finance and Economics Discussion Series 2017-034, Washington: Board of Governors of the Federal Reserve System, (Mar. 31, 2017), https://www.federalreserve.gov/econres/feds/files/2017034pap.pdf; Douglas Elliott, "Quantifying the Effects on Lending of Increased Capital Requirements," Brookings (Sept. 24, 2009), https://www.brookings.edu/articles/quantifying-the-effects-on-lending-of-increased-capital-requirements/; Basel Committee, "An assessment of the long-term economic impact of stronger capital and liquidity requirements" (Aug. 18, 2010), https://www.bis.org/publ/bcbs173.htm; Martin Brooke, Oliver Bush, Robert Edwards, et al., "Measuring the macroeconomic costs and benefits of higher UK bank capital requirements," Financial Stability Paper No. 35 (Dec. 2015), https://www.bankofengland.co.uk/-/media/boe/files/financial-stability-paper/2015/measuring-the-macroeconomic-costs-and-benefits-of.pdf.

[32] *See* FRB Supervision and Regulation Report at 1 ("banking organizations have been a source of strength . . . to the economy, entering the COVID event with substantial capital and liquidity and improved risk management and operational resiliency"); Abboud, *supra* note 27, at 10 ("These robust capital levels helped ensure that systemically important banks were resilient in the initial phase of the COVID-19 shock.").

which do not align with today's banking exposures.[33] If regulators update definitions for the systemic indicators within GSIB categories, then the coefficients should be updated to reflect changes in the banking system since 2013. Otherwise, there is a mismatch in the category between the basis for the coefficient and the new scoring methodology.

B. Recommendations[34]

Each of these factors suggests that the fixed coefficients of the GSIB surcharge method 2 should be recalibrated in accordance with the FRB's intention that factors unrelated to systemic risk should not have an unintended effect on a bank holding company's systemic indicator scores. Because they are incorrectly calibrated, including failing to account for the potential increase in capital due to the Capital Proposal, the current fixed coefficients are not commensurate with the firms' systemic footprints. Therefore, we recommend that the FRB recalibrate the fixed coefficients to reflect the economic growth and significant improvements to the resiliency and resolvability of our member institutions since the adoption of the GSIB surcharge in July 2015 and also to offset the compounding effect on required capital of material increases in RWA from the Capital Proposal. Because this change would further inflate the STWF factor in the method 2 score, we also recommend changes to the weighting of that factor below.

As a starting point, we recommend that the economic growth adjustment be calculated by deflating the coefficients of size, interconnectedness, complexity and cross-jurisdictional activity by 1.61 (proportionate to the increase in economic growth since the 2012-2013 data used to calibrate the fixed coefficients).[35]

Further, we request that the FRB adopt a formalized, procedural mechanism to ensure that the fixed coefficients of GSIB surcharge method 2 are periodically reassessed every two years. A fixed GSIB surcharge methodology calibrated to 2012-2013 period measurements, key aspects of which have not been updated to account for the significant economic growth and inflation since that time, is inappropriate: It introduces significant conceptual and technical frictions into the capital framework and does not reflect the strides U.S. GSIBs have made and will continue to make to increase resiliency.

II. The weight of the STWF category should be recalibrated to 20 percent, consistent with the intention of the FRB in enacting the GSIB surcharge rule.

In adopting the 2015 Rule implementing the GSIB surcharge, the FRB explained that a fixed conversion factor would apply to the STWF category with the intention that it would receive a 20

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[33] 80 Fed. Reg. at 49087.

[34] This recommendation is responsive to Question 23 and to Governor Christopher Waller's concern that "there has not been a broader comprehensive assessment of the calibration of the G-SIB surcharge since it was established in 2015 and" belief that "we should undertake such an assessment, with changes as appropriate." FRB, "Statement by Governor Christopher J. Waller" (July 27, 2023), https://www.federalreserve.gov/newsevents/pressreleases/waller-statement-20230727.htm.

[35] *See* Nominal GDP Data (taking the ratio between the GDP as of the third quarter of 2023 and the GDP as of the fourth quarter of 2013).

percent weight (equal to the other categories).[36] The weight of the STWF category within the method 2 score, however, has been approximately 30 percent since the firms started reporting this item in the FR Y-15. In addition, recalibrating the fixed coefficients to reflect the economic growth and other factors, as recommended above, would further increase the weighting of the STWF factor in the method 2 score. The risks of STWF also are already captured in many areas of the prudential framework, such as the liquidity coverage ratio and the net stable funding ratio, which only further supports the need to recalibrate downwards. Accordingly, we recommend that the fixed conversion factor be updated such that the calibration weights the STWF category at 20 percent, equal to the other categories.

A. Challenges and Concerns

In the preamble to the 2015 Rule, the FRB explained that the fixed conversion factor "was intended to weight the short-term wholesale funding amount such that the short-term wholesale funding score receives an equal weight as the other systemic indicators within method 2 (i.e., 20 percent)."[37] However, likely due to the utilization of imperfect data in the calibration, the weight of the STWF score within the method 2 score has been approximately 30 percent since the firms started reporting this item in the FR Y-15 in the fourth quarter of 2016. Therefore, the STWF category carries a disproportionate and unintended weight in the calculation of the method 2 score.

B. Recommendations

We recommend that the fixed conversion factor be updated such that the calibration equally weights the STWF category with the other categories. We note that this recommendation interacts with other recommendations in this letter and with the Capital Proposal. In particular, the calibration of the fixed coefficients for economic growth would further increase the weight of the STWF category. The FRB should consider all the final changes holistically in determining the proper conversion factor needed in order to weight STWF at 20 percent.

III. The final rule should not require reporting of the average of daily values or, in some instances, the average of monthly values.[38]

Under the Proposal, the GSIB surcharge would no longer use a December 31 point-in-time, end-of-quarter reporting date for systemic indicators that are used to calculate a firm's method 1 and method 2 GSIB score; rather, systemic indicators would be measured using an average of reported values over all four quarters of a calendar year. Further, under the Proposal, only the U.S. GSIBs

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36 80 Fed. Reg. at 49100-01.

37 80 Fed. Reg. at 49100. The FRB further explained that it calibrated "the total weighted basis points for the size, interconnectedness, complexity, and cross-jurisdictional activity systemic indicator scores for the firms currently identified as GSIBs" and then, "[g]iven that this figure is intended to comprise 80 percent of the method 2 score, the weighted basis points accounting for the remaining 20 percent of the method 2 score were determined. The fixed conversion factor was determined by dividing the aggregate estimated short-term wholesale funding amount by average risk weighted assets for the firms currently identified as GSIBs and calculating the weighted basis points that would be necessary to make the short-term wholesale measure equal to 20 percent of the firm's method 2 score." *Id.* at 49101.

38 This section is in part responsive to Questions 1-5 and 20.

would be required to report certain systemic indicators on the FR Y-15 as the average of *daily* (business-day) values of the indicator over the reporting quarter rather than quarter-end, point-in-time values, including daily averaging for intra-financial system assets, intra-financial system liabilities, securities outstanding, assets under custody, OTC derivatives, trading and available-for-sale securities, Level 3 assets, cross-jurisdictional claims and cross-jurisdictional liabilities. The U.S. GSIBs, for certain off-balance sheet items, would also be required to report the average of *month-end* values over the reporting quarter.

The proposed change to require averaging of daily values would provide no marginal benefit to measuring or reducing systemic risk, nor is it needed to prevent firms from managing their GSIB surcharge scores. It is also inconsistent with the Basel standard and would present significant operational challenges and disadvantages. Accordingly, we recommend that the final rule not require U.S. GSIBs to report any indicator as the average of daily values of the indicator over the reporting quarter. Instead, we recommend that the majority of these indicators use the average of month-end values, except for certain indicators with particularly difficult technical challenges for using month-end values, which we recommend instead use quarter-end, point-in-time measurements.

A. Challenges and Concerns

1. *Together, the proposed narrower bands to reduce cliff effects and quarter-end averaging would provide accurate measures of systemic risk and would adequately address concerns about managing scores.*

We support the FRB's proposed change to narrow the method 2 score band ranges, which is practical and reasonable, as well as the move to four-quarter averages rather than relying solely on a December 31 reporting date. These proposed changes alone would remove incentives for banks to temporarily adjust their balance sheets at a reporting date in a way that is not reflective of ongoing systemic risk and so address the FRB's concerns, and would improve sensitivity to systemic risk without significant disadvantages or challenges. By contrast, the proposed daily averaging of indicators would impose significant operational challenges and burdens on U.S. GSIBs without any clear additional purpose or incremental benefit.

The FRB justified the proposed change to daily averaging, which would apply only to U.S. GSIBs, in part by concluding that "the averaging requirement will better reflect a firm's systemic risk profile in the calculation of its GSIB surcharge requirements."[39] This simple justification for a significant operational change, however, is unsupported by any evidence shared by the FRB with the U.S. GSIBs or publicly. Moreover, any concerns the FRB may have regarding the accurate measurement of systemic risk, for instance, due to seasonal fluctuations, would be adequately addressed by the proposed move to averaging indicators with monthly or quarterly values and by narrowing the score band ranges to make the method 2 scores more sensitive.[40] Therefore, it is profoundly disproportionate and unnecessary to require averaging using daily values to address concerns around sensitivity.

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[39] 88 Fed. Reg. at 60387.

[40] *See, e.g.,* 88 Fed. Reg. at 60397.

The FRB's other justification for the change to reporting of the average of daily values of the affected indicators is that it would "reduce the effects of temporary changes to indicator values around measurement dates,"[41] or, in other words, it would "reduce opportunities to manage the values of systemic indicators in a manner that would result in a surcharge requirement that is not commensurate with the firm's systemic risk profile."[42] This is generally the same justification used to support the proposed narrower method 2 score band ranges, which are designed to reduce cliff effects, and the move to an average of reported values over all four quarters of a calendar year.[43] The FRB has not explained why daily averages are needed notwithstanding these two other changes designed to address the same concern.

2. *Temporary changes to indicator values, if any, have been minor, and, therefore, given the move to smaller band sizes, limited adjustments to the averaging approach are sufficient to address the FRB's concerns.*

Although the Proposal suggests that daily averaging is necessary, in part, to counteract concerns of end-of-year balance sheet management that could alter the measured systemic score of a GSIB in a way that is not representative of its systemic profile,[44] it is important to recognize that any potential temporary changes to indicator values have been modest, as demonstrated by the data below, which compares current GSIB scores to hypothetical GSIB scores using a four-quarter average. The small differences between the actual scores (which could include the potential effect of temporary changes) and hypothetical scores (which would not be expected to show temporary changes) show that the effect of any balance sheet management activities has been small.

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41 88 Fed. Reg. at 60385.

42 88 Fed. Reg. at 60387.

43 *See, e.g.,* 88 Fed. Reg. at 60389 (noting the narrower method 2 score band ranges would address the FRB's observation "that firms' method 2 scores tend to cluster close to the upper limit of a score band range, especially at year-end").

44 *See, e.g.,* 88 Fed. Reg. at 60396-97.

Impact of High-Frequency Averaging on GSIB Scores: 2017-2022				
Year	**GSIB Score Based on...**			**# Firms with Score Decrease**
	Q4 Data	**Q1-Q4 Avg.**	**Difference**	
2017	474	480	6	2
2018	464	479	15	1
2019	471	479	9	4
2020	508	500	(8)	7
2021	536	544	7	2
2022	514	532	18	1
Average	**494**	**502**	**8**	**3**

The table above first presents data on non-weighted averages of actual GSIB scores across each of the eight U.S. GSIBs from 2017 through 2022, using fourth quarter data from the FR Y-15. Further, the table presents an average hypothetical score that results from taking a simple average of quarter-end data in each quarter of the year for each U.S. GSIB and then averaging those values across the U.S. GSIBs—this represents hypothetical GSIB scores if a four-quarter average were used.

As shown in the table, from 2017-2022, scores based on fourth quarter data are roughly eight points lower than scores based on an average of first quarter through fourth quarter data. These results suggest that the impact of any potential capital management activities is modest. GSIB score bands are presently 100 score points wide, indicating that in most circumstances, the difference between the fourth quarter score and the score based on an average of first quarter through fourth quarter data would have no impact on GSIB surcharges. Further, results of individual banks vary from the average.

The final column of the table reports the number of U.S. GSIBs that would have experienced a decline (or no change) in their GSIB score had the four-quarter average approach been used. From 2017-2022, between one and seven GSIBs would have experienced a decline in their GSIB score had the four-quarter approach been used instead of the approach based on fourth quarter data. Finally, it should be noted that across all U.S. GSIBs, the average GSIB score was actually lower than the fourth quarter score in 2020, though this result may be an outlier given the unusual circumstances surrounding the COVID pandemic in 2020. Overall, the data presented in the table suggest that the impact of any potential balance sheet management activities is likely to be modest.

In addition to gauging the magnitude of any capital management impacts, these data are also useful for assessing the potential benefits of moving to high-frequency averaging as presented in the Proposal. As shown in the table above, a simple four-quarter average would have the impact of modestly increasing GSIB scores by roughly eight points and would present a better reflection of the underlying systemic profile of each GSIB over the course of a full year.

The Proposal would, however, require higher frequency averaging at either the daily or monthly frequency, depending on the systemic indicator in question. The data presented above are useful for evaluating the relative costs and benefits of such an approach. Because GSIB surcharges were not based on first-quarter through third-quarter scores from 2017 through 2022, there is no basis to expect that there would be any systematic quarter-end management of scores in the first three quarters of each year. Accordingly, if daily data were available, then it would be expected that the result of computing daily averaged GSIB scores would be similar to that computed from quarter-end data.

At the same time, as discussed further below, the operational burdens and costs associated with daily data production across a variety of systemic indicators are substantial. Such complexities include dependencies on third-party data providers, situations in which the required data is simply not available at a daily frequency and the substantial IT management and systems costs associated with daily data collection. Accordingly, the additional benefits of a daily data collection are clearly limited given the introduction of the 10 basis point surcharge bands and are outweighed by the substantial costs. Effectively, much the same result can be achieved by using a lower-frequency averaging approach such as an average of quarterly or monthly systemic indicators.

Because the effect of the potential issue is minimal, only moderate changes would be needed to address it. Accordingly, as discussed above, we believe that the other proposed changes would adequately remove incentives for banks to temporarily adjust their balance sheets at a reporting date in a way that is not reflective of ongoing systemic risk. Because of the proposed narrower method 2 score band changes, which we support, transitioning from one band to a higher band would increase the GSIB surcharge by only 10 rather than 50 basis points. Accordingly, the incentives to engage in end-of-period management would be substantially reduced as the cost of transitioning to a higher surcharge would be significantly smaller.

Finally, and crucially, the data underpinning each of the systemic indicators must be viewed in the context of the ongoing business relationships and practices it represents. As the FRB alludes to, any temporary changes to indicator values would represent frictions for a firm and its participation in the market, making management of systemic indicator values generally undesirable and costly for banks.[45] Making substantial changes to the balance sheet for reasons wholly unrelated to a legitimate business or client need would be highly disruptive to regular business practices and existing client relationships that are often cultivated over months and years. As a result, regular and ongoing balance sheet adjustments at the end of each month or quarter would risk a measurable diminution in a bank's reputation for service and quality. Accordingly, both because of the significant costs of any potential balance sheet management and the appropriate changes elsewhere in the Proposal addressing the same concern, there is no significant risk of excessive balance sheet

[45] *See* 88 Fed. Reg. at 60396-97.

management from adopting a monthly or quarterly averaged GSIB score rather than a score based on a daily average.

3. *Daily averaging would be inconsistent with the Basel standard.*

The Basel standard generally advises using data for the GSIB surcharge based on an institution's position at financial year-end.[46] Consistent with the Basel standard, the European Union (the "EU") also generally determines indicator values based on year-end data.[47] Accordingly, the proposed approach would be another instance of inexplicably departing from the Basel standard and international norms that would harm the international competitiveness of U.S. GSIBs. The U.S. GSIB surcharge is already significantly more stringent than the Basel standard—for example, through the application of a U.S.-specific method 2. Requiring the proposed daily and monthly data averaging beyond the Basel standard would further harm U.S. economic competitiveness unnecessarily by imposing a significant, disproportional operational burden on U.S. GSIBs for doing the same activities that carry the same risks as peer institutions abroad.

4. *Averaging using daily or monthly values would pose significant operational challenges.*

While the FRB has not provided any data to demonstrate the incremental benefit of using daily averaging, what is clear is that data averaging using daily values would pose a number of significant or, in some instances, unsurmountable operational challenges. Challenges result because data must be transformed to be fit for purpose for external regulatory reporting and because of other complications, including reliance on third-party providers for certain inputs.

Any change to the current approach would require major reengineering across multiple platforms and new levels of review, controls and governance to ensure the processes are rigorous enough for a CFO-level attestation. Although banking organizations may track data similar to that reported on the FR Y-15 for risk-management purposes, to transform the data to be fit for purpose for external regulatory reporting would face substantial hurdles and require numerous additional controls, reconciliations and approvals.

In particular, certain regulatory reporting requires reliance on third-party providers of inputs, which inputs may be impossible to obtain on a daily basis. For example, with respect to measuring "preferred shares and other forms of subordinated funding not captured in item 13" in the measurement of "securities outstanding," banking organizations regularly engage external dealers to

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[46] *See* Basel Committee, "Instructions for the end-2022 G-SIB assessment exercise" at 5 (Jan. 2023), https://www.bis.org/bcbs/gsib/instr_end22_gsib.pdf ("In general, all data should relate to the financial year-end closest to end-December 2022").

[47] *See* European Banking Authority ("EBA"), "Guidelines on the specification and disclosure of systemic importance indicators" at 4 (Nov. 4, 2020), https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Guidelines/2020/Guidelines%20on%20the%20specification%20and%20disclosure%20of%20systemic%20importance%20indicators/935707/Final%20report%20-%20EBA%20GLs%20on%20disclosure%20of%20G-SIIs%20indicators.pdf ("Indicator values are to refer to 31 December, unless a relevant entity using a financial year-end other than 31 December agrees with its relevant authority on a different reference date.").

provide an arm's-length approach to the valuations of these unlisted securities. A daily requirement would present significant operational challenges because of the dependence on the timely delivery of information from third parties to report accurate data. Given this dependency, there is virtually no ability to ensure that daily valuations can be accommodated. Finally, because an unlisted securities portfolio is granular and comprised of many tranches, to provide a daily valuation across all the capital instruments would require a substantial operational burden for third parties and internal stakeholders to attest to the accuracy. The operational challenges of ensuring processes are rigorous enough for a CFO-level attestation are also particularly difficult where current processes often require manual data submissions from lines of business or where position-level data sourcing may be required.

Moreover, the operational challenges and inefficiencies are even greater because some of the information that populates directly from other reports under the current approach, such as the Country Exposure Report (FFIEC 009) and the Consolidated Financial Statements for Bank Holding Companies (FR Y-9C), which are reported quarterly, no longer could be used as a source of certain affected indicators. These indicators would now need to be calculated using new systems built expressly for this purpose.

As another example of the substantial operational difficulties that would be raised by more frequent data averaging, the interconnectedness indicators all rely on the definition of "financial institutions" that is unique to the FR Y-15 and explicitly differs from the definition of "financial institutions" used in other Federal Reserve and FFIEC reports. For example, finance companies are non-bank financial institutions on the FFIEC 009 and nondepository financial institutions on the FR Y-9C but are not financial institutions on the FR Y-15 and may be financial institutions under the capital rules, depending on whether the reporting bank owns a certain amount of equity in the company and the percentage of the finance company's assets and revenues that are related to financial activities. The complexity associated with tracking these overlapping but distinct definitions of financial institution places significant limits on banks' ability to automate reporting processes and still achieve accurate reporting.

Further, data averaging using even monthly values is not possible for a small subset of the affected indicators due to significant systems limitations and data sourcing issues, including the indicators in the cross-jurisdictional activity category, one line item reported in the interconnectedness category ("funds deposited with or lent to unaffiliated financial institutions") and the Level 3 assets indicator reported in the complexity category.

For example, cross-jurisdictional balances currently leverage the Country Exposure Report (FFIEC 009). The Country Exposure Report, however, is only reported quarterly. Similar to the FR Y-9C discussed above, banks are given 45 days (or 50 days for the December 31 as of date) to report the FFIEC 009 data due to the complexities and challenges involved in producing the data, and it is not feasible for the U.S. GSIBs to adjust to a daily or even a monthly report with the same level of controls necessary for CFO-level attestation.[48]

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[48] FFIEC, Country Exposure Report: Reporting Form FFIEC 009, "General Instructions" (Dec. 2022), https://www.ffiec.gov/PDF/FFIEC_forms/FFIEC009_202212_i.pdf.

Moreover, Level 3 assets are currently derived from the FR Y-9C, Schedule HC-Q.[49] Under the Proposal, Level 3 assets would move from a quarterly, point-in-time measure to one based on daily averages. This change, however, would present numerous difficulties given the difficulty of valuing and categorizing Level 3 assets. In particular, Level 3 assets are valued based on "unobservable inputs" and reflect a bank holding company's "assumptions about the assumptions that a market participant would use in pricing an asset or liability and should be based on the best information available in the circumstances."[50] Level 3 assets are therefore more difficult to value than assets based on observable prices or inputs, making a daily valuation considerably more onerous (and also less beneficial, as the price is less volatile). Currently, in the FR Y-9C, banks are given 40 days (or 45 days for the December 31 as of date) to report this data due to the complexities and challenges involved in sourcing, validating, aggregating and approving the data.[51] It would be implausible for U.S. GSIBs to go from quarterly reporting with a 40- to 45-day lag to a daily report while maintaining the same level of controls, review and governance to allow for CFO-level attestation.

Simply put, the significant costs of daily averaging vastly outweigh any small potential benefit. As discussed above, quarterly or, where possible, monthly averaging would address the concerns of the FRB without the immense and, in certain instances, impossible operational challenges for both banks and service providers that daily averaging would present.

B. Recommendations

We recommend that the final rule not require an average of daily values for any indicators over the reporting quarter. Specifically, we recommend that the majority of the affected indicators average values as of month-end rather than daily values. However, for the cross-jurisdictional activity indicators, the interconnectedness line item "funds deposited with or lent to unaffiliated financial institutions" and the Level 3 assets indicator in the complexity category, which create particularly difficult technical challenges for even month-end averaging, we recommend instead using quarter-end, point-in-time measurements.

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[49] FRB, "Instructions for the Preparation of Systemic Risk Report: Reporting Form FR Y-15" at GEN-6 (Sept. 2021), https://www.federalreserve.gov/apps/reportingforms/Download/DownloadAttachment?guid=ba9b1d68-3a2a-4472-84e6-0130d5c8a601 [hereinafter, "FR Y-15 Instructions"].

[50] FRB, "Instructions for Preparation of Consolidated Financial Statements for Bank Holding Companies: Reporting Form FR Y-9C" at GL-43 (Dec. 2023), https://www.federalreserve.gov/apps/reportingforms/Download/DownloadAttachment?guid=81d24d2b-870d-4e43-98c2-3ca4983678f1 [hereinafter, "FR Y-9C Instructions"].

[51] FR Y-9C Instructions at GEN-3.

IV. The final rule should calibrate the method 2 GSIB score bands to better correspond to the current rule and not artificially inflate method 2 surcharges.[52]

We support the FRB's proposed change to narrow the method 2 score band ranges, which is practical and reasonable. However, we do not believe the bands are appropriately reassigned; as proposed, the score bands do not properly correspond to the current method 2 score bands and surcharges and would worsen the unwarranted increase in capital requirements under the Proposal and the Capital Proposal.

A. Challenges and Concerns

The Proposal would narrow the method 2 GSIB score bands from 100 basis point score band ranges that correspond to 0.5-percentage point increments for the GSIB surcharge to 20 basis point ranges corresponding to 0.1-percentage point increments.[53] Under the Proposal, the lowest score band range would be scores of 189 basis points or less, corresponding to a 1.0 percent surcharge.[54] Although this approach would provide a more gradual transition between surcharge percentages, it would penalize banking organizations that currently fall in the upper range of the score band. For example, under the current rule, a GSIB with a score of 310 would have a 1.5 percent surcharge; under the Proposal, however, a GSIB with a score of 310 would have a 1.7 percent surcharge.

B. Recommendations

We recommend that the FRB neutralize, at least in part, the improperly punitive effect of the Proposal by setting the surcharge to maintain the same upper end of each current score band (such as 310-329 for the 1.5 percent surcharge). We further recommend that the FRB reduce the punitive "cliff effect" of falling into a higher band by beginning with a method 2 surcharge of 0.6 percent for a method 2 score between 130-149, with the assigned surcharge then increasing by 0.1 percent for every 20-basis-point band. For instance, a score of 330-349 under this approach would represent a GSIB surcharge of 1.6 percent.

V. The final rule should make certain changes to the systemic indicators.

The Proposal would also make changes to certain systemic indicators that are used in the GSIB surcharge framework and reported on the FR Y-15. Below, we discuss our recommendations relevant to certain of these proposed changes.

The final rule should not expand the definition of "financial institution" used in the interconnectedness indicators to include ETFs.[55]

The Proposal would expand the definition of "financial institution" for purposes of measuring interconnectedness to include ETFs, among other entities. However, this change is inadequately

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52 This section is in part responsive to Questions 5 and 23.

53 88 Fed. Reg. at 60389.

54 88 Fed. Reg. at 60390.

55 This section is in part responsive to Question 20.

justified and risks discouraging U.S. GSIB interaction with ETFs, which are widely used as investment vehicles by the retail public. Accordingly, we recommend that the final rule not include ETFs in the definition.

A. Challenges and Concerns

The GSIB surcharge framework uses three systemic indicators to measure interconnectedness: intra-financial system assets, intra-financial system liabilities and securities outstanding, which measure relationships with other "financial institutions." For these indicators, the FR Y-15 instructions currently define "financial institutions" as depository institutions, bank holding companies, securities brokers, securities dealers, insurance companies, mutual funds, hedge funds, pension funds, investment banks and central counterparties.

The Proposal fails to adequately justify the significant expansion of the definition, particularly with regard to ETFs. The FRB did not provide any data or other findings to support its contention that a position with ETFs or other similar entities can act as a "channel for transmission of distress."[56] In fact, in the context of the capital rule, investment funds registered with the Securities and Exchange Commission under the Investment Company Act of 1940 are specifically excluded from the definition of "financial institution" because the FRB and the OCC acknowledged "that such funds create risks of systemic interconnectedness largely through their investments in the capital of financial institutions,"[57] which are separately addressed. This same dynamic is true in this context, as capturing ETFs broadly would not be an accurate measure of systemic interconnectedness, which really should be limited to true financial institutions.

In developing capital rules, the FRB is prohibited from "[taking] into account the activities, operations, or investments of" registered investment companies, subject to limited exceptions.[58] The inclusion of ETFs in the definition of a "financial institution" in the FR Y-15 could have an improperly punitive effect on banking organization interactions with ETFs, which are appropriately subject to their own regulatory framework. In view of Congress's intent to exclude registered investment companies from capital requirements, the FRB should not penalize banking organizations for their interactions with ETFs.[59]

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56 *See, e.g.,* 88 Fed. Reg. at 60391.

57 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, 78 Fed. Reg. 62018, 62063 (Oct. 11, 2013).

58 12 U.S.C. § 1844(c)(3)(C).

59 The legislative history of this provision reflects recognition by Congress that regulated U.S. funds have their own appropriately tailored regulatory framework. For example, the Report from the U.S. House of Representatives Committee on Banking and Financial Services stated that "[i]nvestment companies are regulated entities that must meet diversification, liquidity and other requirements specifically suited to their role as investment vehicles." H.R. Rep. No. 106-74, pt. 1, at 130 (1999). In view of the existing regulatory framework for U.S. funds, the Committee noted that "it was important to ensure that the [U.S. Federal Reserve] Board not indirectly regulate these entities through the imposition of capital requirements at the holding company level, except in the very limited circumstances noted above." *Id.* This suggests that

Further, the addition of ETFs is problematic, as it would be inconsistent with the Basel and EU standards, which would hurt U.S. economic competitiveness and unjustifiably penalize the U.S. GSIBs. The FR Y-15 reporting instructions for Schedule B—Interconnectedness Indicators, line item 3, ask banks to "not report products where the issuing institution does not back the performance of the asset."[60] The Basel Committee standard includes the same instruction for item 3.c but further clarifies that certain ETFs should be excluded ("Do not report products where the issuing institution does not back the performance of the asset (e.g. asset-backed securities) … Do not include … bond exchange traded funds (ETFs)").[61]

In addition to providing no evidence to support the view that the addition of ETFs is needed to better reflect financial interconnectedness, the FRB neglects to consider the costs of this proposed expansion. For example, the change may discourage U.S. GSIBs from interacting with ETFs, which are widely used as investment vehicles by the retail public. Discouraging interaction with ETFs, which provide important diversification both for individuals and the market as a whole, would increase concentration risk in the market and could hurt ordinary retail investors.

B. Recommendations

We recommend that the final rule exclude ETFs from the definition of "financial institution."

The final rule should not include a firm's guarantees of client performance to a CCP with respect to client derivative clearing under the agency model in the affected indicators.[62]

As Chair Powell has said, regulators "have a responsibility to ensure that bank capital standards and other policies do not unnecessarily discourage central clearing."[63] The proposed approach, however, would do exactly that. Under the Proposal, three indicators (intra-financial system assets and intra-financial system liabilities in the interconnectedness category and notional amount of OTC derivatives in the complexity category) would include a firm's guarantees of client performance to a CCP with respect to client derivative clearing under the agency model. We recommend that the final rule not include a firm's guarantees of client performance to a CCP with respect to client-cleared derivative positions in an agency capacity in these three indicators.

Congress intended to create a regulatory structure that would preclude the use of capital requirements by the FRB in a way that would restrict bank holding company interaction with U.S. regulated funds.

60 FR Y-15 Instructions at B-2. This instruction is retained in the Proposed FR Y-15 Instructions.

61 *See* Basel Committee, "Instructions for the end-2022 G-SIB assessment exercise" at 13 (Jan. 2023), https://www.bis.org/bcbs/gsib/instr_end22_gsib.pdf. EBA, Guidelines on the specification and disclosure of systemic importance indicators (Nov. 4, 2020), https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Guidelines/2020/Guidelines%20on%20the%20specification%20and%20disclosure%20of%20systemic%20importance%20indicators/935707/Final%20report%20-%20EBA%20GLs%20on%20disclosure%20of%20G-SIIs%20indicators.pdf. *See also* EBA, "Global Systemically Important Institutions (G-SIIs)," https://www.eba.europa.eu/risk-analysis-and-data/global-systemically-important-institutions (last visited Dec. 21, 2023) (referencing and linking to the Basel Committee instructions).

62 This section is responsive to Questions 12, 14 and 20.

63 Jerome Powell "Central Clearing and Liquidity" (June 23, 2017), https://www.federalreserve.gov/newsevents/speech/powell20170623a.htm.

Under the current approach, each of these three indicators includes client-cleared derivative positions under the principal model but not under the agency model. Because the agency model is the only model used in the United States, the true effect of the Proposal is to subject OTC derivatives clearing businesses to the complexity and interconnectedness indicators essentially for the first time, a major change in approach that is inadequately justified and contrary to the central clearing mandate. The exclusion of transactions under the agency model is appropriate given the significant benefits, long acknowledged by regulators worldwide, that central clearing provides. In particular, central clearing of OTC derivatives makes financial markets less complex, ensures that fewer parties are exposed to or interconnected with GSIBs and promotes financial stability.

A. Challenges and Concerns

1. *The proposed changes would disincentivize central clearing, in contrast to the FRB's intent.*

The proposed changes would disincentivize central clearing, contrary to the intent of regulators following the global financial crisis.[64] For example, this intent was memorialized in the Pittsburgh G20 commitments of 2009, which affirmed that mandatory clearing of certain derivatives is essential to improve risk management and promote financial stability. These commitments support the view that cleared derivatives should be subject to lower capital requirements.[65]

It is critical that the FRB consider the potential harm to the clearing market that could result from these changes. The proposed changes would discourage clearing market participation, potentially even causing exits from the market, all of which would harm end users by reducing access to cleared OTC derivatives and increasing costs (particularly for end users with trades with large notional values of OTC derivatives or that are "financial institutions").[66] Moreover, any discouragement of U.S. GSIB clearing would have an outsized impact on this market because the

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64 For instance, at the G-20 meeting in Pittsburgh in 2009, the G-20 Leaders declared that "[a]ll standardized OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties by end-2012 at the latest." G20 Leaders, "Leaders' Statement: The Pittsburgh Summit" at 9 (Sept. 24, 2009), https://www.oecd.org/g20/summits/pittsburgh/G20-Pittsburgh-Leaders-Declaration.pdf. The Dodd-Frank Act included a "clearing mandate," which amended the Commodity Exchange Act and Security Exchange Act to require mandatory clearing through a CCP for certain products.

65 The G20 commitments provide that "[n]on-centrally cleared contracts should be subject to higher capital requirements," implying that centrally cleared derivatives contracts should be subject to *lower* capital requirements. *Id.*

66 The number of FCMs that provide OTC clearing has already shrunk from 22 to 12, in part because of the disproportionately high capital charge on OTC derivatives clearing activities that had been imposed by the Supplementary Leverage Ratio ("SLR"). *See* Commodity Futures Trading Commission, "Financial Data for FCMs," https://www.cftc.gov/sites/default/files/2023-12/01%20-%20FCM%20Webpage%20Update%20-%20October%202023.pdf (last visited Dec. 21, 2023); *see also* FSB, Basel Committee, Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions "Incentives to centrally clear over-the-counter (OTC) derivatives: A post-implementation evaluation of the effects of the G20 financial regulatory reforms" (Aug. 7, 2018) at 5 [hereinafter, the "FSB Report"], https://www.fsb.org/wp-content/uploads/P070818.pdf.

top six futures commission merchants ("FCMs") that clear swaps and the top five FCMs that clear futures are U.S. GSIBs.[67]

2. *The proposed changes could harm financial stability.*

As Chair Powell has explained, central clearing "serves to address many of the weaknesses exposed during the crisis by fostering a reduction in risk exposures through multilateral netting and daily margin requirements as well as greater transparency through enhanced reporting requirements."[68] As the Financial Stability Board (the "FSB") has acknowledged, if capital requirements for clearing are disproportionately high, a major provider could withdraw, increasing concentration risk because fewer remaining clearing members might be able and willing to step in and accept a book of cleared derivatives.[69] Given the importance of the U.S. GSIBs to this market, it is not clear whether other clearing members would be able to make up for the loss in capacity if U.S. GSIBs exited or scaled back their clearing businesses.

In fact, proposed changes that would disincentivize central clearing are contrary to both the mandate of the complexity category and the wider goal of the GSIB surcharge itself, which is designed both to measure potential sources of systemic risk and to provide opportunity for a firm to decrease its systemic risk profile according to those measures.[70] Clearing provides more standardization of derivative transactions and enhances transparency, both of which reduce complexity and systemic risk. The Proposal would also substantially increase the capital required for another banking organization clearing member to take on a substantial book of new business, making the transfer (or "port") of the positions (and collateral) of a defaulting clearing member's clients more difficult.

The proposed changes are also inconsistent with central clearing's reduction of interconnectedness risk. The FRB has explained that the interconnectedness category should capture the likelihood that "financial distress at a GSIB may materially raise the likelihood of distress at other firms."[71] Client clearing, then, should in fact decrease interconnectedness risk because it reduces the number of counterparties that are exposed to a clearing member since, in a cleared OTC derivative transaction, the client's primary counterparty is the CCP. Client clearing also results in each banking

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67 *See* Commodity Futures Trading Commission, "Financial Data for FCMs," https://www.cftc.gov/MarketReports/financialfcmdata/index.htm (last visited Dec. 21, 2023). These figures are based on the amount of customer funds held in FCM accounts.

68 Jerome Powell "Central Clearing and Liquidity" (June 23, 2017), https://www.federalreserve.gov/newsevents/speech/powell20170623a.htm ("Central clearing also enables a reduction in the potential cost of counterparty default by facilitating the orderly liquidation of a defaulting member's positions, and the sharing of risk among members of the CCP through some mutualization of the costs of such a default.").

69 FSB Report at 3, 54-55, 59.

70 *See, e.g.,* 88 Fed. Reg. at 60390.

71 Risk-Based Capital Guidelines: Implementation of Capital Requirements for Global Systemically Important Bank Holding Companies, 79 Fed. Reg. 75473, 75485 (Dec. 18, 2014).

organization being less interconnected with other firms, as compared to banking organizations entering into bilateral derivatives with clients.[72]

3. *The capital framework already counts exposures from clearing activity, which is a low-risk activity for the clearing member.*

Even though OTC derivatives clearing activity is low risk (for example, because a client is subject to clearinghouse-imposed initial and variation margin requirements, which protect the clearing member as well as the clearinghouse), it is already substantially accounted for in the capital framework, such that U.S. GSIBs maintain robust capital levels to support their OTC derivatives clearing businesses. In fact, exposures from clearing activity are extensively measured under the current GSIB surcharge requirements and in the wider capital framework.[73] The operational risk provisions in the Capital Proposal would also capture clearing activity risk in the proposed business indicator component because clearing activity is also compensated through fees, the impact of which is not considered in this Proposal.[74] The FRB fails to justify the need to expand this measurement any further, particularly because of the low risk posed by central clearing.

4. *The proposed increase in capital requirements for client OTC clearing activities of U.S. GSIBs could decrease access to clearing services and increase prices for end users.*

The proposed increases in capital would disincentivize U.S. GSIBs from clearing OTC derivatives, which, in turn, would harm end-user clients that use cleared OTC derivatives to hedge their risks. In particular, some of the biggest clients that tend to clear their derivative transactions through banks are agricultural and food producers, insurance companies and pension funds. These clients use these derivatives to hedge against commodity price fluctuations and long-term interest rate and inflation risks. These clients are not members of clearing organizations and do not want to be members of a CCP because, for example, they do not want to be subject to the risks of default fund contributions. These main street end users are likely to be disproportionately affected by the proposed increase in capital requirements for client OTC clearing activities for U.S. GSIBs through this Proposal.

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72 Any possible interconnectedness that could result from the mutualization of losses in the central clearing model is substantially mitigated by a waterfall of risk mitigants and safeguards including, for example, initial margin, pre-funded default fund contributions and CCP capital. This significantly reduces the chance that other clearing members would suffer losses from a clearing member's default and mitigates the potential impact of any such losses.

73 For example, the size category captures systemic risk that could result from a clearing member's guarantee of its client's obligation to a CCP in an OTC derivatives transaction. Numerous other aspects of the capital framework also impose requirements relating to derivatives clearing activities, including SA-CCR, the SLR and the enhanced supplementary leverage ratio.

74 88 Fed. Reg. at 64084.

5. *Adding transactions conducted under the agency model would be unnecessary, contrary to the FRB's prior position and a divergence from international standards.*

The FRB specifically justifies the proposed changes by explaining that they would "promote consistent treatment" of the agency and principal models.[75] However, this justification ignores the FRB's own prior reasoning on this point, which ultimately reached the opposite conclusion. In 2017, the FRB proposed to make the same changes included in the Proposal, but the changes were not included in the final rule. In discussing the changes to the complexity category, the FRB explained that these changes were in part to ensure that "no one model receives significantly more or less representation with respect to the GSIB indicators."[76]

However, the FRB did not finalize such changes, reasoning that the predominance of the agency model mitigated concerns about relative treatment between the two models.[77] The FRB acknowledged at the time that it may address this issue in the future "if the principal model again becomes more common."[78] However, even today, the agency model is the only model used in the United States and is the predominant model for clearing of OTC derivatives globally. The principal model has not become more common and therefore, by the FRB's own reasoning, there is no justification for adding OTC derivative transactions cleared under the agency model to the complexity and interconnectedness categories. Further, because the agency model is the only model used in the United States, the true effect of the Proposal is to subject OTC derivatives clearing businesses to the complexity and interconnectedness indicators essentially for the first time.

Inclusion of transactions under the agency model also would be out of step with international standards, potentially harming the competitiveness of the U.S. GSIBs. In particular, the Basel framework excludes from the complexity category cleared OTC derivative transactions in which the GSIB, acting as agent, does not guarantee the performance of a CCP to its client. Competitive imbalance between U.S. and international GSIBs could distort the OTC derivatives clearing markets and potentially increase systemic risk by moving clearing activity to banks that may not be regulated in the same manner or to the same extent as the U.S. GSIBs.

B. Recommendations

We recommend that the final rule not include a firm's guarantees of client performance to a CCP with respect to client-cleared derivative positions in an agency capacity in intra-financial system assets and intra-financial system liabilities in the interconnectedness category and notional amount of OTC derivatives in the complexity category, as doing so would directly contravene regulators' goals of encouraging central clearing and decreasing systemic risk.

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75 88 Fed. Reg. at 60392.

76 Agency Information Collection Activities: Announcement of Board Approval Under Delegated Authority and Submission to OMB, 83 Fed. Reg. 31144, 31145 (July 3, 2018).

77 *Id.*

78 *Id.*

The final rule should not include derivative exposures in the systemic indicators for cross-jurisdictional claims and cross-jurisdictional liabilities.[79]

Under the Proposal, the systemic indicators reported on the FR Y-15 for cross-jurisdictional claims and cross-jurisdictional liabilities would include derivative exposures gross of collateral instead of being reported as memoranda items as they currently are. This proposed change is unnecessary and unjustified, as derivatives exposures are already adequately captured under the current framework. Accordingly, we recommend that the final rule not add a measurement of derivative exposures to cross-jurisdictional activity indicators. If the final rule nonetheless retains these proposed revisions, at a minimum we recommend that the measurement of derivatives allow for netting of both cash and noncash collateral as a more accurate reflection of their risk profile, as collateral mitigates risk of the exposure.

A. Challenges and Concerns

The Proposal fails to explain why the proposed derivatives metric should be measured gross of collateral, other than making the conclusory statement that this would "measure the underlying scale of a banking organization's cross-jurisdictional derivatives activity."[80] There is no explanation as to why this approach is needed here when it is inconsistent with how the FRB measures derivatives in other indicators, where they are measured net of both cash and noncash collateral, consistent with their risk.[81] The FRB and other financial regulators have long acknowledged the risk-mitigating benefits of both cash and noncash collateral, particularly where legally enforceable collateral agreements or qualifying master netting agreements are in place, because the collateral necessarily reduces the risk of the transaction by providing a right of recourse to assets that can be sold in the event of a default.[82] Acknowledging the risk-mitigating benefits of netting would align with both the legal certainty of the transaction and sound risk management practices.

Moreover, the FRB justifies the inclusion of derivative exposures in the systemic indicators for cross-jurisdictional claims and cross-jurisdictional liabilities, without providing data or specifics, by explaining that not including derivatives in these indicators would "present opportunities for a banking organization to use derivatives to structure its exposures in a manner that reduces the value of its systemic indicators without reducing the risks the indicator is intended to measure" and noting

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79 This section is in part responsive to Questions 19 and 20.

80 88 Fed. Reg. at 60394.

81 For instance, derivatives are measured net of cash and noncash collateral in other indicators measured on the FR Y-15. *See, e.g.,* Proposed FR Y-15 Instructions at 29. The FRB also nets derivatives for other measures, for instance, under the liquidity coverage ratio. *See generally* 12 CFR part 249. *See also* 12 U.S.C. §4401 (Congress finds that the efficient processing of transactions between financial institutions "is essential to a smoothly functioning economy" and that "such transactions can be processed most efficiently if, consistent with applicable contractual terms, obligations among financial institutions are netted" and "such netting procedures would reduce the systemic risk within the banking system and financial markets").

82 *See generally* 12 CFR part 217. *See also* Liquidity Coverage Ratio: Liquidity Risk Measurement Standards, 79 Fed. Reg. 61440 (Oct. 10, 2014); Regulatory Capital Rules, Liquidity Coverage Ratio: Interim Final Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions, 79 Fed. Reg. 78287 (Dec. 30, 2014).

that including derivatives "would provide a more accurate and comprehensive measure of a banking organization's cross-jurisdictional activity and the associated risks."[83]

The FRB fails to acknowledge or address, however, that derivative exposures are already triple-counted through the FR Y-15 systemic indicators in the size, interconnectedness and complexity categories, as well as in ancillary schedules.[84] The FRB does not explain why adding derivatives to yet another systemic indicator would incrementally improve the accuracy of measuring systemic risk, nor does it support its assertion that banking organizations are using derivatives to reduce their indicator values. Accordingly, the Proposal fails to justify the need to add additional derivatives metrics to the already comprehensive reporting and regulation of derivative exposures.

Second, derivatives are already well capitalized and accounted for beyond FR Y-15 reporting. For instance, a firm's derivatives risk is accounted for in standardized counterparty risk weights, SA-CCR, the Credit Valuation Adjustment ("CVA") framework revisions and the Fundamental Review of the Trading Book ("FRTB"). The FRB fails to address these overlapping regulatory regimes to explain how this proposed change is not duplicative and is necessary in the context of the overall regulatory framework. Accordingly, the Proposal fails to justify the need to add additional derivatives metrics to the already comprehensive reporting and regulation of derivative exposures.

B. Recommendations

We recommend that the final rule not include the proposed requirement to include derivative exposures in the systemic indicators for cross-jurisdictional claims and cross-jurisdictional liabilities. Instead, measurements of these exposures should remain as memoranda items.

If the final rule nonetheless retains the proposed revisions to the cross-jurisdictional activity indicators, at a minimum we recommend that the measurement of derivatives be aligned with the other indicators to allow for netting of both cash and noncash collateral where legally enforceable collateral agreements or qualifying master netting agreements are in place, consistent with their risk. Further, if the FRB retains these proposed revisions to the cross-jurisdictional activity indicators and continues to over count derivatives in these categories, it should at least recalibrate the GSIB surcharge fixed coefficient methodology to account for the duplicative treatment of derivatives, among other factors discussed in greater detail above.

VI. The final rule and instructions to the FR Y-15 should not include alpha in calculating exposure amounts for the interconnectedness indicators.[85]

The Proposal would remove reference to the current exposure method in the proposed instructions to Form FR Y-15 and instead specify that derivative exposures be calculated in accordance with 12

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83 88 Fed. Reg. at 60394.

84 Derivatives are measured in Schedule A—Size: Item 1 (Derivative Exposures); Schedule B—Interconnectedness Indicators: Intra-Financial System Assets, Item 5 (Over-the-counter (OTC) derivative contracts with other financial institutions that have a net positive fair value); Schedule D—Complexity: Notional Amount of Over-the-Counter (OTC) Derivative Contracts; Schedule F—Ancillary Indicators: Gross positive fair value of over-the-counter (OTC) derivative contracts.

85 This section is in part responsive to Question 20.

CFR 217.34(a), which for our member institutions means SA-CCR.[86] The Proposal goes on to explain that the change "would align with the measurement of derivatives in the interconnectedness category with that used in the size category, as well as in the calculation of standardized total risk-weighted assets and total leverage exposure in the capital rule."[87]

A. Challenges and Concerns

The preamble's explanation raises ambiguity as to how the PFE multiplier and alpha multiplier would contribute to the calculation of PFE and replacement cost in the interconnectedness indicators. We do not believe it is appropriate to include the alpha factor in the interconnectedness indicators' exposure calculation because it is not relevant to interconnectedness and thus would inaccurately inflate the indicators.

The alpha factor is justified in the SA-CCR final rule release as a way to "instill an appropriate level of conservatism and further support the use of SA-CCR as a broadly applicable and standardized methodology … [and] capture certain risks (*e.g.,* wrong-way risk, non-granular risk exposures, etc.) that are not fully reflected under either [internal models methodology] or SA-CCR."[88] The quoted risks the alpha factor is meant to address are not related to interconnectedness between financial institutions, so including the alpha in the exposure calculation of the interconnectedness indicators would only serve as a punitive measure, overstating a GSIB's interconnectedness.

B. Recommendations

The final rule and instructions to the FR Y-15 should not include the alpha factor in calculating exposure amounts for the interconnectedness indicators.

VII. During the transition period, the method 2 GSIB scores should be determined based on a fully phased-in ERBA denominator.

As discussed in greater detail in our letter on the Capital Proposal, we recommend that, during the transition period, the Agencies use fully phased-in ERBA to calculate the method 2 GSIB scores (which include a weighted STWF component that references RWA amounts), to the extent available. In particular, the December 31, 2025 GSIB score used to calculate the applicable GSIB surcharge effective on January 1, 2027 should be calculated using the limited, fully phased in ERBA RWA amounts from 4Q2025. Using fully phased-in ERBA for purposes of the GSIB surcharge would result in a smoother transition to ERBA under the Capital Proposal.

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86 Proposed FR Y-15 Instructions at 30, 33; *see also* 88 Fed. Reg. at 60392.

87 88 Fed. Reg. at 60392.

88 Standardized Approach for Calculating the Exposure Amount of Derivative Contracts, 85 Fed. Reg. 4362, 4372 (Jan. 24, 2020).

VIII. The effective date of changes to a firm's GSIB surcharge requirement should not be changed.[89]

Currently, an increase in the GSIB surcharge takes effect on January 1 of the year that is one full calendar year after the increased GSIB surcharge was calculated. As the FRB correctly notes, this facilitates capital planning and allows a U.S. GSIB to make appropriate adjustments such that it may be subject to a lower GSIB surcharge.[90] The FRB does not propose changes to this approach but seeks comment regarding "whether it would be appropriate to modify the effective date of changes to a firm's GSIB surcharge requirement following a change in its GSIB score."[91] The FRB specifically suggests alternatives in which an increase in the GSIB surcharge could take effect more quickly.

We do not believe the effective date for an increase in the GSIB surcharge should change in the final rule. The current effective date is necessary to achieve the FRB's appropriate goals of facilitating capital planning and providing time for U.S. GSIBs to make appropriate adjustments.

A. Challenges and Concerns

As the FRB notes, U.S. GSIBs need sufficient time to appropriately make adjustments based on their expected GSIB surcharge and engage in capital planning. The current approach providing for the GSIB surcharge to take effect on January 1 of the year that is one full calendar year after the increased GSIB surcharge was calculated provides sufficient time to meet these goals.

Moreover, the FRB's suggestion that other elements of the Proposal, such as averaging of indicators and the narrower method 2 score band ranges, would justify a shorter lag period is misplaced.[92] Although averaging over four quarters would marginally improve predictability of the applicable GSIB surcharge, it would not allow for enough of an increase in predictability such that any lag period of less than a year would allow sufficient time for U.S. GSIBs to appropriately make adjustments based on their expected GSIB surcharge and engage in appropriate capital planning. The GSIB surcharge is a complex calculation with dozens of variables, making predictions difficult. Additionally, capital planning is a holistic process that considers all applicable constraints, some of which (such as the stress capital buffer requirement) are inherently unpredictable for large banking organizations.

In fact, a firm's capital planning itself is subject to specific expectations from the FRB. The FRB has explained that "a firm's processes for managing and allocating its capital resources are critical to its financial strength and resiliency, and also to the stability and effective functioning of the U.S.

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89 This section is in part responsive to Questions 7 and 9.

90 88 Fed. Reg. at 60390.

91 *Id.*

92 *Id.*

financial system."[93] These expectations are particularly high for the U.S. GSIBs subject to Category I standards.[94]

To meet these expectations, large banking organizations, especially the U.S. GSIBs, need sufficient time to engage in sound capital planning. Reducing the amount of time a U.S. GSIB has before an increase in its surcharge becomes effective would be in tension with the FRB's capital planning expectations for U.S. GSIBs. Even a 10 basis point increase in a U.S. GSIB's surcharge (the new increment under the Proposal) would represent a substantial increase in the dollar amount of a U.S. GSIB's capital requirements, and U.S. GSIBs need time to plan around these potential increases.

B. Recommendations

We recommend that the final rule maintain the effective date for an increase in the GSIB surcharge–*i.e.*, January 1 of the year that is one full calendar year after the increased GSIB surcharge was calculated.

IX. The proposed changes should take effect at least one year after the date of adoption of a final rule.[95]

Under the Proposal, the changes to FR Y-15 reporting would take effect relatively quickly, only two full calendar quarters after the date of adoption of the final rule.[96] Because the FRB is proposing a number of significant changes to FR Y-15 definitions and reporting methodology, we request that the proposed changes take effect at least one year after the date of adoption of a final rule in order to give banking organizations sufficient time to incorporate these changes into internal systems and processes. Moreover, if the recommendations discussed above regarding averaging for the affected indicators are not adopted, substantial additional time for compliance would be needed given the significant operational burdens associated with those changes, likely at least an additional year.

A. Challenges and Concerns

For the reasons discussed above, it would be extremely difficult if not impossible for our member institutions to implement daily (or even, in some instances, monthly) averaging within two quarters of the final rule's adoption. The frequency of data averaging required under the Proposal would require our member institutions to build new systems, processes and departments, which would take far more than two quarters. As discussed above, banking organizations foresee significant challenges with building out the systems, processes and departments to comply with the more frequent data averaging in the Proposal. As noted above, in some cases, the reported data is reliant on third parties, which poses particularly significant challenges for calculating daily valuations.

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93 FRB, "Federal Reserve Guidance on Supervisory Assessment of Capital Planning and Positions for Firms Subject to Category I Standards," SR 15-18 (Dec.18, 2015) (rev. Jan. 15, 2021), https://www.federalreserve.gov/supervisionreg/srletters/sr1518.htm.

94 *Id.*

95 This section is responsive to Question 21.

96 88 Fed. Reg. at 60396.

This is particularly relevant to the extent that our recommendations regarding frequency of averaging are not adopted.

Even beyond the proposed changes regarding the frequency of data averaging, the other changes contemplated by this Proposal also would require significant operational changes, requiring banking organizations to build new systems and processes to comply with the proposed requirements. Accordingly, banking organizations will require more than two quarters to comply with the proposed changes.

B. Recommendations

We recommend that the final rule (including the amendments to the FR Y-15 and FR Y-15 instructions) take effect at least one year after the date of adoption of a final rule. Moreover, if the recommendations discussed above regarding frequency of averaging are not adopted, we recommend that the final rule (including the amendments to the FR Y-15 and FR Y-15 instructions) take effect at least two years after the date of adoption of a final rule to account for the significant systems development that banking organizations would need to undertake to comply.