U.S. Chamber of Commerce

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January 16, 2024

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

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

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

Re: Comments on Regulatory Capital Rule: Large Banking Organizations and to Banking Organizations with Significant Trading Activity [R-1813] / Docket ID OCC-2023-0008 / RIN 3064-AF29

Dear Ladies and Gentlemen:

The U.S. Chamber of Commerce ("Chamber") Center for Capital Markets Competitiveness submits these comments in response to the Board of Governors of the Federal Reserve System's ("FRB"), the Federal Deposit Insurance Corporation's, and the Office of the Comptroller of the Currency's ("Agencies") joint proposed rulemaking entitled Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity ("Proposal").

As U.S. capital standards are traditionally stricter than international counterparts, the Chamber believes that the Proposal's implementation of the Basel Committee on Banking Supervision ("BCBS") recommendations lacks a rationale for a problem it seeks to solve. Failure by the agencies to adhere to procedures in the Administrative Procedure Act ("APA") make the proposal arbitrary and fails to provide a basis for moving forward. Furthermore, the Chamber has serious concerns with the Proposal and its impacts upon banks, consumers, businesses, and the broader U.S. economy.

In the wake of the global financial crisis in 2008 and 2009, the BCBS introduced a series of reforms to increase the quality and quantity of capital in the global banking system including the Basel III capital standards. In 2017, the BCBS finalized revisions to those capital standards, which are generally referred to as the Basel III Endgame. The purpose of these

standards is to achieve more consistency and comparability among the global risk-based capital requirements. Since 2019, regulators from the U.K. and other major banking centers began the process of introducing these revised standards in their capital rules. However, the Agencies took nearly six years to introduce their Proposal and provided little data or other rationale to support the necessity of their proposed capital requirement increases nor how it would impact banks, businesses, consumers, or the U.S. economy.

In fact, a significant increase in capital requirements was not the goal of the Basel III Endgame. Mario Draghi (at the time, Chair of the Group of Governors and Heads of Supervision) highlighted that point at the press conference announcing the agreement, "The focus of the exercise was not to increase capital. As a matter of fact, the Group of Central Bank Governors and Heads of Supervision almost a year ago endorsed this review by the Basel Committee, provided it would not create a significant capital increase in the aggregate of the banking system." [1]

Lack of Necessity

The Agencies have not adequately explained why the Proposal is necessary nor provided evidence as to why a rule that would dramatically increase bank capital should be implemented. In their own comments to Congress, the Agencies have consistently stated that U.S. banks are strong and resilient. Moreover, in his statement releasing the Proposal, FRB Chair Jerome Powell, said that U.S. banks have "strong levels of capital and liquidity." [2] Chair Powell correctly points out that U.S. banks are well capitalized. In fact, the aggregate capital ratio of the largest U.S. banks has increased by roughly a factor of three since 2008 (4% to 12%). [3]

A recent study from the Federal Reserve Bank of New York underscored the strength and resilience of the U.S. banking system in finding that, "the largest [U.S.] banks tend to be less exposed to capital shortfalls, fire sales, liquidity, and run risk relative to smaller institutions." [4] The FRB's 2023 stress test produced similar results, finding that the 23 large banks subject to the stress testing "have sufficient capital to absorb more than $540 billion in losses and continue lending to households and businesses under stressful conditions." [5]

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[1] Basel Committee on Banking Supervision, "Basel III: Finalising post-crisis reforms", December 2017, https://www.bis.org/bcbs/b3/ghos_20171207_2.htm

[2] Powell, J. (2023, July 27). Statement by Chair Powell on the Federal Reserve's monetary policy actions. Retrieved from https://www.federalreserve.gov/newsevents/pressreleases/powell-statement-20230727.htm

[3] Board of Governors of the Federal Reserve System (2022). Financial Stability Report, November 2022. Retrieved from https://www.federalreserve.gov/publications/2022-november-financial-stability-report-leverage.htm

[4] Banking System Vulnerability: 2023 Update. Liberty Street Economics. https://libertystreeteconomics.newyorkfed.org/2023/11/banking-system-vulnerability-2023-update/

[5] Board of Governors of the Federal Reserve System (2023). Dodd-Frank Act Stress Test 2023: Supervisory Stress Test Results. Retrieved from https://www.federalreserve.gov/publications/files/2023-dfast-results-20230628.pdf

Furthermore, the significant increase in capital is not designed to manage risk in the banking sector. Ironically, the Proposal, which purports to mitigate risk, could actually increase risk. While appropriately calibrated capital requirements are critical for the stability in the banking sector, requiring banks to hold more capital for its own sake is imprudent and would have downstream negative impacts upon the U.S. economy. Given the wealth of evidence indicating that banks already have the optimal level of capital, the Chamber respectfully requests that the Agencies to further explain their rationale behind the Proposal.

The short-lived crisis caused by the collapse of Silicon Valley Bank ("SVB") is an example. SVB was well capitalized, but it had a liquidity issue. This underscores that the economic and financial situation is much different today than when the BCBS did its initial releases that led to the proposal. Accordingly, other issues, such as liquidity and failure by agencies to conduct appropriate oversight, may be of greater importance than increased capital standards.

Adherence to Regulatory Tailoring Requirements

The Proposal fails to adhere to the tailoring regulations required by the Economic Growth, Regulatory Relief, and Consumer Protection Act ("The Economic Growth Act"). [6] The law, enacted in 2018 with bipartisan support, instructed federal banking regulators to adjust the prudential Dodd-Frank regulations for banks according to their size and other factors. Following enactment, the Agencies created a framework that segmented large banking organizations into five categories subject to different correlated risk, and subject to different regulations. However, the Proposal undermines the size-specific tailoring and imposes many of the same rules that were designed for the largest and most complex banks on all banks with more than $100 billion in assets.

FDIC Vice Chair, Travis Hill expressed concerns on the Proposal's impact to tailoring in July 2023 saying, "For purposes of the capital rules, the proposal effectively collapses Categories II, III, and IV into one category. The proposal undoes almost all of the tailoring of the capital framework for large banks and is a repudiation of the intent and spirit of S. 2155. It is further a troubling sign for future policymaking, a signal that regulators intend to treat all large banks alike, in defiance of Congressional directives..." [7]

The reversal of this tailoring would have serious negative impacts for the economy. It would significantly increase the regulatory costs for Category II, III, and IV banks. This could contribute to more consolidation in the banking sector as smaller banks struggle to cope with increased regulatory expenses, leading to a loss of the healthy diversity in the banking sector from which American consumers currently benefit.

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[6] U.S. Congress. 2018. Economic Growth, Regulatory Relief, and Consumer Protection Act. S. 2155, 115th Cong. https://www.congress.gov/bill/115th-congress/senate-bill/2155

[7] Travis Hill, "Statement by Travis Hill, Vice Chairman, FDIC, on the Proposal to Revise the Regulatory Capital Requirements for Large Banks", July 27, 2023, https://www.fdic.gov/news/speeches/2023/spjul2723b.html.

Lack of Sufficient Evidence

Setting aside the yet unanswered question of necessity, the Chamber is concerned that the Agencies have not conducted adequate research on the negative economic impacts of the Proposal. The lack of a robust cost-benefit analysis, subject to public comment, of the Proposal's impact on the banks and the broader U.S. economy, is a grave oversight. According to a survey of 300 corporate treasures, 68% of respondents believe that proposed net increases in capital requirements under the Proposal would be damaging to their business. [8] If adopted as proposed, the Proposal will have predictable and harmful outcomes for markets, businesses of all sizes, and American households. The Chamber urges the Agencies to show the public that they have undertaken the necessary research and analysis to ensure that the Proposal will not hurt the nation's economy.

The Agencies should have undertaken an updated quantitative impact study ("QIS") *before* issuing the Proposal. The failure to undertake an updated QIS prior to issuance of the Proposal potentially violates the Administrative Procedure Act. It has been over six years since the BCBS issued the 2017 post-crisis reform and four years since the market risk (fundamental review of trading book) reform Basel III: A global regulatory framework for more resilient banks and banking systems. Since issuance of the Basel III standard, there was adequate time for the Agencies to commission a study prior to the issuance of the Proposal. The result is a proposal that is unvetted and arbitrarily modifies the U.S. capital standards in a way that could create significant harms to the U.S. financial system.

Not only has a comprehensive economic analysis not taken place, but the basis of the Proposal is flawed. The Proposal is primarily based on an outdated QIS conducted by BCBS from 2017 that comprised a total of 248 banks, only 12 of which were US-based. [9] U.S. banks represent less than 5 percent of the banks that participated in the exercise. Undue reliance on data that fails to adequately represent U.S. banks could explain why the Proposal stands to create so many harmful downstream consequences for the American economy. Additionally, the study, which was published in December of 2017, is based on end-2015 data. The Proposal is relying on eight-year-old data that does not consider changes to the U.S. banking system and the broader economy. This data fails to capture the current economic landscape that has been shaped by the COVID-19 pandemic and recovery, disruptions in the labor market and supply chain, increased inflation, and challenges in the geopolitical landscape. The BCBS QIS is outdated and unrepresentative of U.S. banking institutions yet is the core data set underpinning the Proposal.

[8] U.S. Chamber of Commerce, Financial Challenges Facing Small Businesses in 2023, accessed December 18, 2023, https://www.uschamber.com/assets/documents/CCMC_Survey-FinancialChallenges_Fall2023.pdf.
[9] Basel Committee on Banking Supervision, Basel III Monitoring Report - Results of the cumulative quantitative impact study, https://www.bis.org/bcbs/publ/d426.pdf.

As noted in a letter dated October 13, 2023, from a group of bank industry groups, [10], the Agencies acknowledged that the data which estimates the impact of the Proposal suffers from at least three severe limitations:

> "First, these estimates heavily rely on banking organizations' Basel III QIS submissions. The Basel III QIS was conducted before the introduction of a U.S. notice of proposed rulemaking, and therefore is based on banking organizations' assumptions on how the Basel III reforms would be implemented in the United States. For market risk, the impact of the proposal further depends on banking organizations' assumptions on the degree to which they will pursue the internal models versus the standardized approach and their success in obtaining approval for modeling.
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> "Second, for banking organizations that do not participate in Basel III monitoring exercises, the agencies' estimates are primarily based on banking organizations' regulatory filings, which do not include sufficient granularity for precise estimates. In cases where the proposed capital requirements are difficult to calculate because there is no formula to apply (in particular, the proposed market risk rule revisions), impact estimates are based on projections of the other banking organizations that submitted QIS reports.
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> "Third, estimates are based on banking organizations' balance sheets as of yearend 2021, and do not account for potential changes in banking structure, banking organization behavior, or market conditions since that point."

The Agencies relied on outdated and unrepresentative data in the formulation of the Proposal. Not until October 20th, 2023, did the FRB announce they are undertaking data collection from the affected banks to determine the impact of the Proposal. It is important to note that it is unclear if the FRB will make this data collection submission available to the public. Even if the submission is made publicly available, it is due the same day as the comment period deadline, so the public is unable to respond to the results. This work should have been undertaken and published prior to the issuance of the Proposal so the public could review and respond to the data. The Chamber urges the FRB to make publicly available the results of the data collection from the affected banks. The Chamber also requests that the Agencies conduct a holistic QIS on the impacts of the Proposal on the broader U.S. economy. A comprehensive study is necessary to assess the potential effects of the Proposal on any number of sectors including, but not limited to, access to and availability of credit, mortgage lending, derivatives markets, and renewable energy projects.

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[10] Center for Capital Markets Competitiveness. (2023). Letter to Agencies re QIS. Retrieved from https://www.centerforcapitalmarkets.com/wp-content/uploads/2023/11/Letter-to-Agencies-re-QIS-2023.10.13-4877-2461-6327-v1-1.pdf

Specific Areas of Negative Impact

The Chamber believes the Proposal will have significant negative impacts upon a wide range of bank customers and clients. Vice Chair Barr stated in October 2023 that, "The proposal is projected to raise capital for large banks. This may result in higher funding costs." [11] The Proposal will make mortgages, business loans, government infrastructure projects, and any number of other bank-offered credit products such as credit cards more expensive. Below, we highlight just some of the consumers and business sectors that would be negatively impacted by the Proposal.

First, the Proposal will make it harder and costlier for consumers to obtain mortgages, especially those who are buying their first home or who have low or moderate incomes ("LMI") and smaller downpayments. Increasing required bank capital requirements will increase the cost of making and holding these loans for banks, non-banks, and government agencies.

The Proposal would particularly hurt LMI borrowers, LMI communities, and Black and Hispanic borrowers the most, as they tend to rely on high loan-to-value (LTV) loans that would face higher capital charges. This contradicts the Agencies' goals of promoting more lending to underserved groups under the Community Reinvestment Act and other programs. The Proposal would discourage banks from making mortgage loans in general and especially to LMI borrowers and communities and borrowers of color. [12]

The Proposal would also adversely impact consumer loan products. While BCBS recognized that consumer loans are inherently less risky and assigned lower risk weights to them, the Proposal would not adopt the risk-weights proposed by BCBS. Instead, the Proposal would add a 10 to 20 percentage point surcharge on the regulatory retail and residential mortgage risk-weights proposed by BCBS, thereby unjustifiably inflating the capital requirements for these loans. The surcharge, combined with other aspects of the Proposal, such as the additional burden from the standardized operational risk requirement and new capital charge for unconditionally cancellable unused credit line, would increase the effective risk-weights of these consumer credit exposures and inflate the capital needs for these products. Many startup entrepreneurs use consumer financial products as seed money to start a business. Accordingly, the unnecessary tightening of consumer financial products could have negative downstream effects on business startups that regulators need to assess and take into account when considering higher capital standards.

[11] Barr, Michael S. (2023). "Financial Innovation and Regulation: Balancing Risks and Rewards". Speech at the Brookings Institution, Washington, D.C., October 9.
https://www.federalreserve.gov/newsevents/speech/barr20231009a.htm
[12] Bank Capital Notice of Proposed Rulemaking, https://www.urban.org/sites/default/files/2023-09/Bank%20Capital%20Notice%20of%20Proposed%20Rulemaking.pdf

Additionally, many entities, such as governments at different levels and various institutions like Community Development Financial Institutions, depend on Global Systemically Important Banks (GSIBs) to access the U.S. capital markets that finance their projects. The Proposal would increase the capital requirements for capital markets activities of the GSIBs by more than 55%. [13] This means that the entities that rely on the capital markets to fund job creation, invest in innovation, and build public infrastructure, such as hospitals, roads, and bridges, would face higher costs. This includes the infrastructure and green energy projects that are part of the Inflation Reduction Act ("IRA").

A new proposed charge for operational risk would account for nearly 90 percent of the increase in banks' capital requirements under the Proposal. It would amount to a tax on all bank intermediation activities, but it would have a particularly punitive impact on capital markets and other fee-income activities (including brokerage, advisory, clearing and custody services) that brokers, asset managers, money market funds and pension funds use daily to manage securities and other financial instruments for American investors. As the costs of bank services and products increase, that cost will be passed on to customers. This includes higher costs and lower returns for retirement accounts, college funds and other long-term savings.

The Proposal will also impact derivatives trading and, in turn, have negative consequences for American companies that use derivatives to safely hedge their non-financial business risk – including farmers, airlines, utility companies, and consumers. The Proposal would increase the cost and complexity for end-users to hedge their non-financial business risk. It is critical to ensure a robust and competitive derivatives market, as it is a key source of risk management, liquidity, and innovation for the economy. U.S. banks are among the largest and most active participants in the global derivatives market.

The Proposal will create an environment that discourages international banks from investing in U.S. operations. Notably, the Proposal's disproportionate impact on foreign banks will inhibit U.S. investment and negatively impact the diversity and competitiveness of the U.S. financial system. This would disincentivize investment from foreign banks into the derivatives market because any investment into a U.S. operation would come with increased capital requirements. [14] The result would be less investment from foreign banking organizations which would lead to further concentration and consolidation of activities, affecting the cost and range of products available to American consumers and businesses.

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[13] SIFMA. (2021, October 21). Identifying an Optimal Level of Capital and Evaluating the Impact of Higher Bank Capital Requirements on US Capital Markets. Retrieved from https://www.sifma.org/resources/news/identifying-an-optimal-level-of-capital-and-evaluating-the-impact-of-higher-bank-capital-requirements-on-us-capital-markets/
[14] U.S. Chamber of Commerce (2024). "Endgame" for Main Street Lending: Understanding how the Basel III bank capital rules will harm American businesses and the U.S. economy [White paper].

Under the Proposal, banks will have to use a new method, standardized approach for counterparty credit risk ("SA-CCR"), to calculate how much capital they need for derivative transactions. The transition from the current exposure methodology ("CEM") and internal models methodology to SA-CCR methodology would likely increase expenses and capital requirements for banks. Businesses that use banks to hedge their commercial risk will then face higher costs, and they may pass them on to their customers by increasing the prices of their products and services. This could drive down the profits of businesses and reduce consumer spending power, slowing down the economy.

This capital requirement increase to derivative transactions will reduce banks' ability to provide credit and hedging services to the agricultural sector, which is already facing challenges from climate change, trade disputes, and supply chain disruptions. This would increase the cost of borrowing and risk management for farmers and agribusinesses, which would ultimately be passed on to consumers in the form of higher food prices. These tools that help companies manage risk in order to keep prices stable and low for consumers will also become more costly. In turn, Americans will have to pay more for their groceries, travel, and other manufactured or retail goods.

The Proposal will affect banks' ability and willingness to invest in clean energy projects. Banks use tax equity as a financing mechanism that allows clean energy developers to monetize tax credits and incentives by partnering with investors who have tax liabilities. Tax equity is a vital source of funding for the clean energy sector, especially for solar and wind projects, and any disruption or decline in the tax equity market could jeopardize the growth and competitiveness of the industry.

Under the current regulatory capital rule, tax equity has a risk weight of 100% as long as the total amount of equity investments by a bank is less than 10% of its capital. Under the Proposal the risk weight for many tax equity investments would be 400%, meaning that the capital requirement would quadruple. This will cause large banks to increase their tax equity investment pricing and would, in turn, make the costs too high for developers. The Proposal is already having unintended impacts on the tax equity market as some investors are already holding back new investments, while others are trying to rework new and existing deals that are not fully funded yet. [15]

The IRA provides tax benefits for reducing greenhouse gas emissions in the U.S. economy by supporting technologies such as clean energy production. Experts in energy finance estimate that the tax equity market, which is currently around $20 billion per year, needs to grow to more than $50 billion to achieve the objectives of the IRA and meet the

[15] Project Finance Law, "Proposed Basel III Rules Could Be Catastrophic for the Traditional Tax Equity Market", September 2023, https://www.projectfinance.law/tax-equity-news/2023/september/proposed-basel-iii-rules-could-be-catastrophic-for-the-traditional-tax-equity-market/

demand generated by the new tax incentives. [16] According to major tax equity providers, the annual tax equity investments in the clean energy sector could drop by up to 90%, and many banks could withdraw from the renewable tax equity marketplace altogether. [17] The Proposal would make it challenging to maintain the current status quo, much less achieve a 150% increase to the tax equity market. Simply put, reduction in the availability and affordability of tax equity financing would dramatically slow the implementation of new renewable energy projects.

Re-propose the Rule

As described in this letter, the Proposal is unnecessary and arbitrary as it fails to adhere to procedures required by law. The Agencies have not explained the need for bank capital to increase nor have they provided the appropriate analysis of the potential economic impacts should the Proposal take effect. The Chamber believes that if the Proposal is finalized as proposed, it will restrict access of loans and credit to small businesses and low- and medium-income Americans, hurt businesses of all sizes in all sectors, and slow the growth of the U.S. economy. The Proposal must be withdrawn and rewritten in a transparent and justified manner that considers the impacts to American businesses and consumers.

Sincerely,

Tom Quaadman
Executive Vice President
Center for Capital Market Competitiveness
U.S. Chamber of Commerce

[16] ACORE, Expectations for Renewable Energy Finance in 2023-2026, June 2023, https://acore.org/wp-content/uploads/2023/06/ACORE-Expectations-for-Renewable-Energy-Finance-in-2023-2026.pdf.
[17] ACORE, "Letter on the Impact of Proposed Bank Regulatory Capital Requirements on Tax Equity Investment in Clean Energy", August 2023, https://acore.org/wp-content/uploads/2023/08/ACORE-Letter-on-the-Impact-of-Proposed-Bank-Regulatory-Capital-Requirements-on-Tax-Equity-Investment-in-Clean-Energy.pdf