



## INSTITUTE OF INTERNATIONAL BANKERS

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August 5, 2016

Office of the Comptroller of the Currency  
Legislative and Regulatory Activities  
Division  
400 7th Street, SW., Suite 3E-218  
Mail Stop 9W-11  
Washington, D.C. 20219  
Docket ID OCC-2014-0029  
[regs.comments@occ.treas.gov](https://www.regulations.gov/comment/OCC-2014-0029)

Robert de V. Frierson  
Secretary  
Board of Governors of the Federal Reserve  
System  
20th Street & Constitution Avenue, NW.  
Washington, D.C. 20551  
Docket No. R-1537; RIN 7100-AE51  
[regs.comments@federalreserve.gov](https://www.regulations.gov/comment/R-1537)

Robert E. Feldman  
Executive Secretary  
Attention: Comments/Legal ESS  
Federal Deposit Insurance Corporation  
550 17th Street, N.W.  
Washington, D.C. 20429  
FDIC RIN 3064-AE44  
[comments@FDIC.gov](https://www.regulations.gov/comment/FDIC-2014-0029)

Re: Net Stable Funding Ratio: Liquidity Risk Measurement Standards and Disclosure Requirements

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Ladies and Gentlemen:

The Institute of International Bankers (“IIB”) appreciates the opportunity to comment on the proposed rulemaking referenced above.<sup>1</sup> The IIB’s membership is comprised of banks headquartered outside the United States which engage in a variety of banking and other financial activities in the United States. The IIB and its members are committed to strengthening the liquidity of internationally active banking organizations as a means to enhance their resiliency and mitigate risks to financial system stability.

The Proposal applies to those IIB member banks which conduct operations in the United States through newly-established U.S. intermediate holding company (“IHC”) subsidiaries that

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<sup>1</sup> 81 Fed. Reg. 35124 (June 1, 2016) (the “Proposal”). Capitalized terms used in this letter have the meanings ascribed in either the Proposal or the definitions applicable to the Proposal, except as otherwise indicated or required by the context.



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are themselves Covered Depository Institution Holding Companies (“Covered DIHCs”; and any such IHC, a “Covered IHC”<sup>2</sup>). We have co-signed with The Clearing House Association L.L.C., the Securities Industry and Financial Markets Association, the American Bankers Association, the Financial Services Roundtable and the Commercial Real Estate Finance Council a separate letter on the Proposal (the “Joint Trade Associations Letter”) and are submitting this letter on our own behalf to focus specifically on the following two aspects of the Proposal that are uniquely relevant to foreign banking organizations (“FBOs”):

- As applied to Covered IHCs, the methodology for calculating the \$10 billion foreign exposure threshold will result in overstatement of their international activities and thereby result in more IHCs having to comply with the “full” NSFR requirements prescribed in Subparts K, L and N of Regulation WW than is warranted by their “international” profile, which, for such IHCs, otherwise is closer to that of U.S.-headquartered bank holding companies (“U.S. BHCs”) that are required to comply with the “modified” LCR requirements prescribed in Subpart M.

To address this concern regarding the potential for over-inclusive application of the NSFR requirements to Covered IHCs, and consistent with the longstanding policy of national treatment, we respectfully recommend that the methodology be revised to exclude a Covered IHC’s exposures to its parent FBO, its other non-U.S. affiliates and the FBO’s U.S. branches and agencies from calculation of the \$10 billion threshold. As discussed below, exposures of an IHC to its parent FBO’s home country sovereign (including its agencies, instrumentalities and political subdivisions) also should be excluded.

These same concerns, and the same recommendation, would apply equally were the Board to determine in a future rulemaking to adopt substantially the same approach to applying NSFR requirements to those IHCs that are not Covered IHCs.

- The assessment of the potential impact of the Proposal understates the potential costs to all Covered Companies, and Covered IHCs in particular. This consideration underscores the concerns raised in the Joint Trade Associations Letter regarding the Proposal’s procedural shortcomings and provides further support for the request to delay the compliance date and provide additional time to prepare for implementation of the proposed disclosure requirements requested.

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<sup>2</sup> The Proposal applies to those IHCs which have a U.S. bank subsidiary and therefore, in their capacity as bank holding companies, are Covered DIHCs, and not to those that are not themselves bank holding companies. See also 81 Fed. Reg. at 35128 (“The proposed rule would also not apply to the U.S. operations of foreign banking organizations or intermediate holding companies required to be formed under the Board’s Regulation YY that do not otherwise meet the requirements to be a covered company (for example, as a U.S. bank holding company with more than \$250 billion in total consolidated assets).”).



**Potential Over-Inclusive Impact of the \$10 Billion Foreign Exposure Threshold as Applied to Covered IHCs<sup>3</sup>**

The \$10 billion foreign exposure test is based on total on-balance sheet exposures as reported on FFIEC Form 009.<sup>4</sup> Under this form, the calculation of foreign exposures of a U.S. bank or U.S. BHC reflects the bank's or BHC's claims on and liabilities to foreign residents.<sup>5</sup> The calculation looks at the BHC's exposures from the perspective of its U.S. domicile and location and from the perspective of its operations abroad. Both U.S.-headquartered Covered DIHCs and IHCs are required to report on a fully consolidated basis in accordance with the principles set forth in the instructions for the preparation of the FR Y-9C.<sup>6</sup>

In the case of a Covered DIHC that is headquartered in the United States and is the top-tier BHC in the consolidated group, this approach includes in the determination of "foreign exposures" at the BHC level only those outside the group. As stated in the explanation of "cross-border claims" at page 11 of the FFIEC 009 Instructions:

Since the reports are on a fully-consolidated bank (or bank holding company) basis, cross-border claims exclude any claims against those branches or subsidiaries that are part of the consolidated bank (or bank holding company).

When applied to an IHC, this approach excludes its exposures to any of its non-U.S. subsidiaries but includes its exposures to its parent FBO and offices of the parent FBO outside the United States, any parent of the parent FBO and any other non-U.S. affiliates of the parent FBO. In addition, because "claims on a bank branch (but not on a subsidiary) of a banking organization are considered to be guaranteed by the head office of the organization, even without a legally binding agreement," an IHC's exposures to any U.S. branch or agency of its parent FBO are reported as exposures to the FBO itself and, as such, included in the IHC's reportable "foreign exposures" and allocated to the bank sector in the parent FBO's home country.<sup>7</sup>

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<sup>3</sup> We have raised similar concerns with the application of the \$10 billion foreign exposure threshold to IHCs, and made the same recommendations on how to address them, in our June 3, 2016 comment letter on the Board's proposed rulemaking to implement the single counterparty credit limit ("SCCL") requirements prescribed in Section 165(e) of the Dodd-Frank Act.

<sup>4</sup> 81 Fed. Reg. at 35128 n. 19. Extension of FFIEC 009 reporting requirements to IHCs is scheduled to become effective September 30, 2016. See 81 Fed. Reg. 47237 (July 20, 2016).

<sup>5</sup> See Instructions for the Preparation of Country Exposure Report (FFIEC 009) (Dec. 2013) ("FFIEC 009 Instructions").

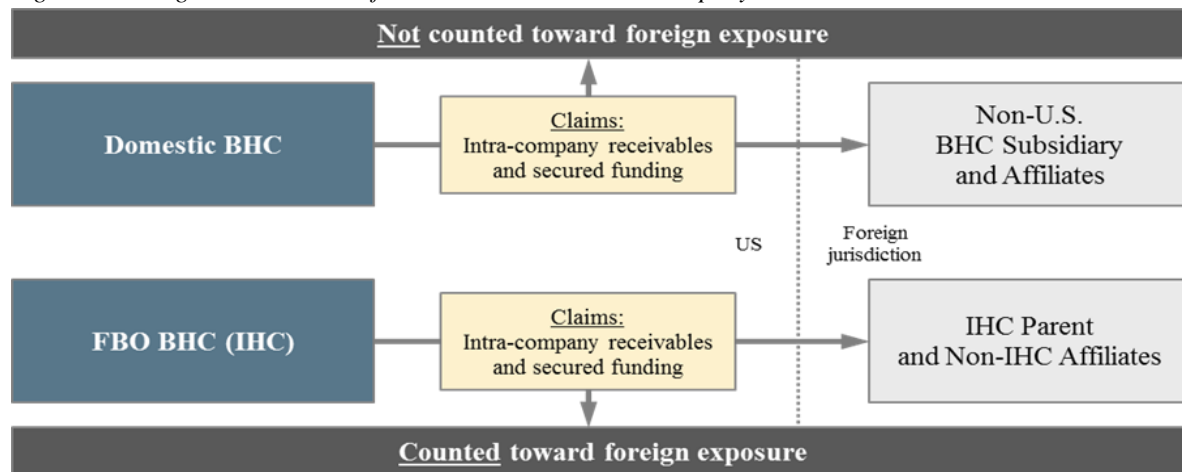
<sup>6</sup> See id. at page 4 (Consolidation Rules).

<sup>7</sup> See id. at 12 (Head Offices).



Furthermore, the \$10 billion foreign exposure threshold was constructed prior to the introduction of the concept of an IHC by the Agencies and does not take into account the commonplace nature of intra-company transactions between an FBO parent and its affiliates that are external to the IHC (Figure 1). For example, intra-company receivables between a U.S. BHC and a foreign-domiciled subsidiary of the BHC would be excluded from the foreign exposure calculation. However, for an IHC, inter-company receivables with its foreign domiciled parent or affiliate are counted as a foreign exposure. Secured financings are a second type of common intra-company transaction between an IHC and its parent or parent affiliate. This type of transaction also would not count as a foreign exposure between a U.S. BHC and its foreign-domiciled subsidiary but would count for an IHC conducting the same type of transaction with its foreign parent or parent affiliate—despite being collateralized at over 100% on a daily mark-to-market basis. Intra-company transactions do not pose the same nature or magnitude of risk as the types of third-party risks that the foreign exposure calculation is intended to capture. To the contrary, inter-company exposures between an IHC and its parent inherently pose less risk than equivalent inter-company exposures between a U.S. BHC and its foreign-domiciled subsidiaries because the IHC’s parent is on average more diversified and maintains significantly greater capital and liquidity available to cover these “exposures”, whereas foreign-domiciled subsidiaries will be less diversified and a fraction of the size of their U.S. BHC parent.

Figure 1. Incongruent treatment of domestic and FBO intra-company transactions



In our view, this disparate treatment between U.S.-headquartered Covered DIHCs and IHCs is not supported by the policy objectives underlying the Proposal.<sup>8</sup> Inclusion of the \$10 billion foreign exposure test as a separate basis on which to impose the NSFR requirements regardless of the amount of a Covered DIHC’s total consolidated assets is intended to identify firms with a “significant international presence” whose degree of interconnectedness with

<sup>8</sup> As discussed in the FFIEC 009 Instructions (Introduction and Purpose), the data collection conducted through the FFIEC Form 009 reporting requirements serves a variety of purposes unrelated to application of NSFR requirements to Covered DIHCs. Our comments in this letter do not address these other purposes.



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sources of funding outside the United States pose a sufficient degree of risk to their safety and soundness and to the resilience of the U.S. financial system to merit application of the “full” NSFR requirements, notwithstanding that, by measure of its total consolidated assets, a Covered DIHC would be subject to only the modified NSFR requirements.<sup>9</sup>

The liquidity buffer requirements applicable to IHCs under the Board’s Regulation YY significantly limit reliance on intragroup funding flows (including with the FBO’s U.S. branches and agencies) and effectively trap their liquidity in the United States.<sup>10</sup> As the Board explained in connection with its adoption of Regulation YY, this approach addresses the Board’s concern that internal cash flow sources may not be available to an IHC in times of stress.<sup>11</sup> This acknowledged difference in the treatment of IHCs as compared to U.S.-headquartered is attributed to the structural differences between FBOs and U.S. banking organizations and is seen as necessary to ensuring that FBOs maintain liquidity in the United States to support their U.S. operations.<sup>12</sup>

In our view these structural differences do not support disparate treatment of FBOs and U.S. banking organizations vis-à-vis the measurement of IHCs’ “foreign exposures” for purposes of the Proposal. The potential impact of intragroup funding relationships on an IHC’s liquidity, and the potential implications for the resilience of the U.S. financial system, are effectively addressed by the liquidity constraints imposed Regulation YY. These constraints result in treatment of IHCs that is substantially the same as the treatment of U.S.-headquartered DIHCs – in each case, the regulated entity must maintain sufficient liquidity on a consolidated basis. Where for IHCs the consequence is maintenance of liquidity on a U.S.-only basis, the “international” risk profile of the IHC accordingly should be measured on a basis comparable to how U.S.-headquartered DIHCs are measured. This approach more closely comports with the policy of national treatment than one which treats otherwise similarly-situated IHCs different from their U.S.-headquartered DIHC counterparts.

We therefore respectfully recommend that the methodology for calculating the “foreign exposure” of IHCs be revised to exclude an IHC’s exposures to its parent FBO, its other non-U.S. affiliates and the FBO’s U.S. branches and agencies. Inclusion of such exposures would require an IHC to comply with the “full” NSFR requirement when the profile of its international activities otherwise more closely resembles that of Covered DIHCs to which the modified NSFR

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<sup>9</sup> See 81 Fed. Reg. at 35128.

<sup>10</sup> Under Regulation YY an IHC is required to conduct liquidity stress tests based on overnight, 30-day, 90-day and 1-year planning horizons and maintain a liquidity buffer sufficient to meet its projected net stress cash-flow need over the 30-day planning horizon. The methodology for each of the liquidity stress test planning horizons, including the 1-year horizon, significantly limit reliance on intragroup funding flows.

<sup>11</sup> See 79 Fed. Reg. 17240, 17296 (March 27, 2014).

<sup>12</sup> See *id.* at 17299 - 300.



requirements will apply. In addition, exposures of an IHC to its parent FBO's home country sovereign (including its agencies, instrumentalities and political subdivisions) should be excluded from the foreign exposures calculation for NSFR purposes. As the Board has recognized in providing an exemption for such exposures from the SCCL requirement, FBOs may be required to have exposures to their home country sovereigns.<sup>13</sup> Footnote 10 of the Board's Staff Memorandum accompanying the SCCL rulemaking proposal indicated that an IHC's exposures to its parent FBO, non-U.S. affiliates and home country sovereign should not be included in the foreign exposure calculation, an apparent acknowledgement that counting such exposures would be unduly punitive for IHCs.<sup>14</sup>

### **The Impact Assessment Understates Costs to IHCs**

The IIB's membership welcomes the concept of a longer-term measure of structural liquidity and firmly supports incentivizing Covered Companies to develop and maintain sustainable funding structures. Our concern with the Proposal lies specifically with the determination of its potential costs, the resulting overall impact assessment, and lack of sufficient evidence that the Proposal will deliver its stated objectives in a manner that appropriately balances benefits and costs.

The Agencies have concluded that the Proposal would result in an overall liquidity shortfall of approximately \$39 billion. This impact assessment was made as of December 31, 2015, *i.e.*, prior to the date on which FBOs were required under Regulation YY to establish IHCs and transfer to them the FBO's entire ownership interest in any BHC subsidiary (other than one which itself is designated as the IHC (such an IHC, a "Designated IHC")), any insured depository subsidiary and U.S. nonbank subsidiaries holding at least 90% of the FBO's other U.S. non-branch assets.<sup>15</sup>

Given the gap in time between the impact assessment and the establishment of IHCs, it would appear that the impact assessment did not take into account the following:

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<sup>13</sup> See 81 Fed. Reg. 14328, 14347 (March 16, 2016) (such an exemption "would recognize that a foreign banking organization's U.S. operations may have exposures to its home country sovereign entity that are required by home country laws or are necessary to facilitate the normal course of business for the consolidated company").

<sup>14</sup> We submit that the use of the FFIEC 009 calculations to define "foreign exposure" in other contexts is also inappropriate. See, e.g., the liquidity coverage ratio (12 C.F.R. § 249.1(b)(1)(ii)) and the U.S. implementation of Basel III (definition of advanced approaches banking organization in 12 C.F.R. § 217.100(b)(1)(i)(B)(2) as made applicable to an IHC through 12 C.F.R. § 252.153(e)(2) (but subject to Fed-approved opt out in 12 C.F.R. § 252.153(e)(2)(i)(C)). We would be happy to discuss with the Board a broader set of modifications that would eliminate their use for FBOs and IHCs, or at least modify them significantly to eliminate intragroup and home country sovereign exposures as discussed above.

<sup>15</sup> 12 C.F.R. § 252.152(c)(c)(2)(i).





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- Covered IHCs that are not Designated IHCs and that became BHCs upon their establishment as IHCs by virtue of acquiring the entirety of the FBO’s ownership interest in a bank subsidiary that previously either (i) was not held under a U.S. BHC subsidiary or, (ii) if previously held under a BHC subsidiary, the BHC subsidiary did not become a Designated IHC.
  - In the first case, the U.S. non-branch operations of the FBO likely were excluded entirely from the impact assessment. The extent of the resulting understatement of costs depends on the size and components of the omitted operations. Where these operations are extensive and large, the impact could be substantial.
  - In the second case, the extent of the understatement depends on the degree to which the FBO’s combined U.S. non-branch operations were conducted through the pre-existing BHC. Where the U.S. BHC subsidiary accounted for only a small portion of the FBO’s combined U.S. non-branch operations that were transferred to the IHC the understatement of costs also could be substantial.
- In the case of Designated IHCs, any portion of the FBO’s U.S. non-branch operations that were conducted outside the U.S. BHC subsidiary prior to the effective date of its designation.

It would also appear that the impact assessment did not adequately consider the location of long-term debt within the organizational structures of FBOs vis-à-vis U.S. BHCs. U.S. BHCs benefit from long-term debt held at their top-tier holding companies when “available stable funding” (“ASF”) is calculated. Because of inherent regulatory and structural requirements for operating in the U.S. as part of a foreign-headquartered enterprise, an IHC is not able to similarly utilize long-term debt at its parent holding company for the purposes of calculating ASF. IHCs and U.S. BHCs, despite being treated as equivalents under the Proposal, are structurally fundamentally different and these differences require consideration to be consistent with the longstanding policy of national treatment.

Two recent publications also support the assessment that the Agencies may have underestimated the overall stable funding shortfall under the Proposal. The European Banking Authority (“EBA”) in its impact study<sup>16</sup> estimated the EU-wide NSFR shortfall at approximately €595 billion, which equals 1.9% of total assets of the banks in the study. Applying this factor to the total assets of U.S. banks, the NSFR shortfall would be in the range of \$300 billion<sup>17</sup>—nearly eight times the Agencies’ estimate. For capital markets activities, the study estimated the average NSFR of these businesses at 60.1%—nearly 30 percentage points below the average of credit-oriented businesses.

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<sup>16</sup> See EBA Report on Net Stable Funding Requirements under Article 510 of the CRR, p. 29 (December 15, 2015).

<sup>17</sup> 1.9% times \$15.9 trillion in total US bank assets. See Assets and Liabilities of Commercial Banks in the United States (Weekly) – H.8, Board of Governors of the Federal Reserve System.



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A publication<sup>18</sup> by Barclays Research concluded that if the commercial banking system returns to operating at a loan-to-deposit ratio of greater than 88%, it will be NSFR-deficient. As a result, NSFR could very likely become a binding constraint on commercial lending growth in a recovering economic cycle where loan growth outpaces deposit growth. This publication further concluded that broker-dealer businesses would be even more punitively treated under the Proposal and would operate at material NSFR shortfalls comparable to those estimated by the EBA.

In addition, remarks in industry discussions by a number of U.S. BHC and FBO participants on their individual evaluations of the Proposal further support the position that the \$39 billion estimate is low.

These considerations underscore the concerns raised in the Joint Trade Associations Letter regarding the Proposal's procedural shortcomings and provide further support for the request to delay the compliance date and provide additional time to prepare for implementation of the proposed disclosure requirements requested.

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We appreciate your consideration of our comments. Please contact the undersigned if we can be of further assistance.

Sincerely,

A handwritten signature in black ink, appearing to read 'Richard Coffman', written in a cursive style.

Richard Coffman  
General Counsel

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<sup>18</sup> See Monteleone, Brian, Jeffrey Meli and Daniel Lang, NSFR: Implications for Loans and Liquidity. Barclays/Credit Research, May 19, 2016.