INSTITUTE OF INTERNATIONAL BANKERS

299 Park Avenue, 17th Floor
New York, N.Y. 10171
Direct: (646) 213-1149
Facsimile: (212) 421-1119
Main: (212) 421-1611
www.iib.org

RICHARD W. COFFMAN
General Counsel
E-mail: rcoffman@iib.org

February 2, 2015

Secretariat to the Financial Stability Board
c/o Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland
Email: fsb@bis.org

RE: Consultative Document entitled "Adequacy of loss-absorbing capacity of global systemically important banks in resolution" (the "Proposal")

Ladies and Gentlemen:

The Institute of International Bankers ("IIB") appreciates the opportunity to participate in the consultation on the above-referenced Proposal. The IIB is the only national association representing the interests of banking institutions headquartered outside the United States with respect to their operations in the United States. Each global systemically important bank ("G-SIB") covered by the Proposal that is not a U.S.-headquartered institution is a member of the IIB.

It is essential to minimize the impact the resolution of a G-SIB might have on financial stability and to put in place measures that will ensure with a high degree of confidence the continuity of critical functions and avoid exposing public funds to loss. The Proposal represents important progress toward achieving these goals, and the IIB supports the underlying goals of this project fully.

There are two central components of the Proposal: "external" and "internal" total loss absorbing capacity ("TLAC"). We focus our comments in this letter on certain aspects of internal TLAC and in particular wish to underscore the critical importance of achieving an appropriate balance between home and host country authorities with regard to implementation of the internal TLAC requirement.[1]

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[1] In addition to the issues addressed in this letter, the other aspects of the Proposal are comprehensively discussed in the letter submitted jointly by the Institute of International Finance and Global Financial Markets Association. Our remarks are intended to be consistent with those expressed in that letter, and overall we support its conclusions and recommendations.

The internal TLAC requirement is designed to provide sufficient assurances to a host country authority that, in the event that a G-SIB is subject to resolution in its home country, there will remain sufficient support for the G-SIB's subsidiary operations in the host country. The home-country resolution should be accomplished in a manner that reinforces the degree of confidence between home and host authorities and thereby enhances home-host cooperation in connection with a G-SIB's cross-border resolution. In general, we strongly support international efforts to strengthen and reinforce confidence between home and host country authorities. These efforts are especially critical to effectively addressing the challenges presented in the context of cross-border resolutions of G-SIBs.

Fundamental to this process is recognizing and appropriately accommodating the respective interests of home and host country authorities, bearing in mind that a G-SIB's resolution ultimately rests in the hands of the home country authority. On the one hand, it is important to address the host authority's concern that a home country resolution might not be sufficiently supportive of the subsidiary operations in the host country. On the other hand, it is equally important to avoid "trapping" such resources in the host country in a manner that would preclude their deployment in normal times to support operations across the group and avoid resolution. Impeding, or prohibiting outright, the transfer of resources from host country operations to support operations elsewhere in the world would introduce an unnecessary and potentially harmful degree of "brittleness" into the global financial system that in turns promotes its fragmentation. We firmly agree that host country ring-fencing, and in particular *ex ante* ring-fencing, must be avoided.

Striking the appropriate balance between the interests of home and host country authorities is critical to ensuring an orderly resolution process and preventing destabilizing fragmentation throughout the global financial system. In our view, the provisions of the proposed Term Sheet dealing with internal TLAC in significant ways embody too strong of a bias in favor of host country interests at the expense of equally legitimate and compelling global concerns. In the end, we believe that host nations benefit most from a comprehensive solution that supports bank resilience and financial stability overall. We respectfully recommend that the balance between home and host country authorities be recalibrated. Specifically:

- <u>Determining the size of the internal TLAC requirement</u>

  Section 22 of the Term Sheet provides that the amount of required internal TLAC "would be determined by the relevant host authority in consultation with the home authority" and that, in making that determination, the host authority would treat the material subsidiary as if it were itself a resolution entity that is subject to the host country's Pillar 1 external TLAC requirements.

  This approach is troubling in that it relegates the home authority to a secondary position with respect to a key question regarding the allocation of the external TLAC that is raised at the home country level and pursuant to home country requirements. Recognizing that as a legal matter a host authority in all cases may act as it determines is appropriate in the circumstances with respect to the operations of material subsidiaries conducted within its territory, we urge the adoption of a more balanced approach whereby application of internal TLAC is not automatic, but a decision is made following discussion with the home authority as well as input from the Crisis Management

Group ("CMG"). By these means the allocation of a resolution entity's TLAC can be more effectively coordinated with its overall resolution plan and, if necessary, internal TLAC imposed. Without such coordination, there is the danger that different authorities feel pressure to raise local requirements ahead of others and move to "ring fence" early. Review of firm-specific TLAC determinations in the context of the Resolvability Assessment Process, as contemplated by the Proposal, provides another important means to strike the appropriate balance between home and host authorities.

Likewise, where a host authority looks to the external Pillar 1 TLAC requirements of G-SIBs that are headquartered in the host country as the basis for prescribing internal TLAC, this "national treatment" approach should be tempered by requiring that the host authority give due regard to the interests of the home authority as overseer of the parent resolution entity's resolution with a view to optimizing the proportional allocation of TLAC across the group. For example, it should be clarified that usually the applicable leverage ratio for determining internal TLAC is the material subsidiary's share of the group leverage ratio, rather than double the applicable local leverage ratio.

A related concern is the prospect that the host authority would "goldplate" the internal TLAC requirement, [2] thereby distorting the allocation of TLAC throughout the larger group and enhancing the prospect that, especially if spread across multiple host jurisdictions, the aggregate amount of internal TLAC would exceed the resolution group's consolidated standalone external TLAC. To address these concerns, the final standards should highlight the importance of achieving an appropriate degree of proportionality in the allocation of internal TLAC across the material subsidiaries in various host countries – a goal consistent with allocating an increased role to the home country and CMG in determining the need for and size of the internal TLAC requirement.

- Pre-positioning internal TLAC

Section 22 of the Term Sheet states that the full amount of internal TLAC, however determined, should be pre-positioned on the balance sheet of the material subsidiary "unless otherwise agreed between home and relevant host authorities." Here too, there is a strong bias in favor of the host authority – for those seeking to ring-fence their local operations, there is no incentive to accommodate home country (as well as other host country) considerations to the contrary – thereby significantly expanding the risk that the regime would contribute to the "brittleness" of the resolution entity and the fragmentation of the global financial system. To address these concerns, the determination of whether to require pre-positioning of internal TLAC (and the amount thereof) should be incorporated into the overall process of determining the amount of internal TLAC, modified as discussed above. It may be that the level of pre-positioning should be set at the lower end of the range, and anything above that subject to the kind of assessment envisaged when determining the Pillar 2 component of the resolution entity's external TLAC.

Our members have a strong track record in supporting their local operations, and see this as integral to their global franchise. These natural economic forces will normally provide sufficient protection

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[2] While we concentrate our comments on the internal TLAC requirement, it is equally important to strengthen incentives encouraging the consistent application of external TLAC requirements across jurisdictions.

for major host countries. In addition, we believe the use of guarantees and capital commitments can play an important part in addressing the concerns discussed above in a fashion that is less likely to lead to ring-fencing or brittleness.

- Identifying host country "material subsidiaries"

  The discussion of material subsidiaries in Section 21 of the Term Sheet focuses on operating entities. The final standards should take into account host country structures in which, whether by choice or pursuant to host country legal requirements, a resolution entity organizes its subsidiary operations in the host country under a host country holding company. In these circumstances, the general rule should be that such an intermediate holding company should be designated the sole material subsidiary (if any) in the host country. We would also welcome greater definition of what is meant by material for the exercise of critical functions, as we believe it may lead to inconsistencies and some authorities identifying too many subsidiaries, thereby increasing fragmentation overall.

  The penultimate paragraph in Section 20 of the Term Sheet appears to provide host authorities a basis for imposing their own external TLAC requirements on any material subsidiary as well as external or internal TLAC requirements on any non-material subsidiary. In doing so, host authorities are directed to take "due account of TLAC requirements applied to similar firms within their jurisdiction." Recognizing that a host authority in all cases retains the legal authority to regulate entities operating in the host country as it considers appropriate, the exercise of that authority nevertheless should also take due account that any such subsidiary operates within a larger, internationally active group. From that perspective, the application of a host country external TLAC requirement appears contrary to the guiding principles of the Proposal. Regarding the imposition of any TLAC requirement on a non-material subsidiary (whatever the criteria for "materiality"), this approach would only exacerbate the risks of brittleness and fragmentation discussed above. To address this concern, the final standards, at a minimum, should provide for a strong presumption against the application of a TLAC requirement (and, should there be any such requirement, only internal TLAC) to a non-material subsidiary and that, consistent with the discussion above regarding the determination of the amount of internal TLAC, any such application involve strong input from the home authority and CMG.

- Exercising internal TLAC by means of write downs and/or conversions to equity

  Section 23 of the Term Sheet provides that the host authority must have the ability to write down and/or convert to equity internal TLAC at the point of non-viability (as determined by the host authority) without putting host operations into resolution. It is further provided that any such action is subject to the consent of the home authority (except where Basel 3 provides that such consent is not required), but there is an important qualification – the host can subject internal TLAC to its own resolution bail-in or other resolution powers if the home authority withholds its consent. Such action by the host authority risks the significant disruption of the resolution entity's cross-border resolution contrary to the principles underlying the Proposal. The final standards should emphasize that any such action would be an extreme measure and should be strongly discouraged.

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We appreciate your consideration of our comments. Please contact the undersigned if we can provide any additional information.

Sincerely,

Richard Coffman
General Counsel