Industry Supports Total Loss Absorbency Requirement
to Help Ensure G-SIBs Can Be Resolved in an Orderly Manner without Taxpayer Assistance

Industry’s empirical analysis shows FSB’s TLAC calibration is higher than needed

New York, NY – Today, The Clearing House (TCH), the Securities Industry and Financial Markets Association (SIFMA), the American Bankers Association (ABA) and the Financial Services Roundtable (FSR) filed a comment letter with the Financial Stability Board (FSB) in response to its proposal to impose a total loss absorbing capacity (TLAC) requirement on global systemically important banking groups (G-SIBs). The letter expresses the industry’s strong support for a TLAC requirement for G-SIBs to help ensure that these institutions can be resolved in an orderly way at creditor rather than taxpayer expense, bringing us one final step closer to ending “Too Big to Fail.” The letter also highlights the importance of ensuring that any such requirement be empirically calibrated to achieve its express policy objective – which is to ensure that a G-SIB can absorb sufficient losses to permit its orderly resolution and recapitalization without taxpayer assistance.

Empirical analysis performed by The Clearing House (and included in the comment letter) demonstrates that FSB’s proposed TLAC requirement of 16-20% of risk-weighted assets, plus the 2.5% capital conservation buffer and the G-SIB surcharge, is in excess of the loss absorbency necessary to prevent against even the most extreme historical or stress loss estimates. Specifically, the analysis shows that the FSB’s proposed 16% TLAC requirement would produce a loss absorbing capacity that is:

- 4.4 times greater than the average losses projected for U.S. G-SIBs under the Federal Reserve’s severely adverse scenario for the 2014 Dodd Frank Annual Stress Testing (DFAST) stress testing and Comprehensive Capital Analysis and Review (CCAR) exercise – which assumes, for example a 50% drop in the stock market and a 4% increase in unemployment to a 11.25% level, the highest since the great depression; and

- 2.6 times greater than average historical losses experienced at the largest failed U.S. financial institutions.

A 20% TLAC requirement would push these loss coverage multiples to 5.2 times greater than DFAST losses and 3.1 times greater than average historical losses.

“TLAC is an essential part of the new resolution framework that will ensure that creditors and shareholders, and not taxpayers, bear losses in the event of a G-SIB’s failure,” said Paul Saltzman, President of The Clearing House Association. “But our empirical analysis shows that a TLAC requirement calibrated even on the low end of the FSB’s proposed range is more than is needed to ensure these institutions can be resolved in an orderly way.”

“TLAC brings us even closer to the goal line in our efforts to end ‘Too Big to Fail,’” said Kenneth E. Bentsen, Jr.,
SIFMA president and CEO. “As with our previous comments on living wills and capital and liquidity requirements, we fully support the objectives of TLAC and the single point of entry model for resolving US G-SIBs. While supporting the concept of TLAC, for TLAC to succeed, we must study the costs and benefits of the proposed rule and adopt a balanced calibration level that will allow banks to be resolved without putting taxpayers on the hook. If our regulators act in haste and miss the mark, the cumulative impact of these rules will cause negative consequences for the availability of credit, job creation, and economic growth.”

The letter recommends that the FSB both (i) identify and explain the standard it uses in calibrating TLAC and (ii) support its calibration against that standard with empirically-based forward-looking stressed analyses as well as analyses of losses experienced by large institutions historically.

The letter also makes a number of other technical suggestions to help make the proposal more effective and workable:

- **Underwriting and market making exemption.** The final TLAC framework should carefully craft any limitations on G-SIBs’ holdings of other G-SIBs’ external TLAC, including by providing an exception for bona fide underwriting and market making activities needed to ensure a viable market in TLAC instruments.

- **Scope of Eligible TLAC Instruments.** The final TLAC framework should define the scope of liabilities that qualify as TLAC in a manner that better reflects the loss-absorbing capacity of various instruments, including structured notes, long-term debt instruments with meaningful remaining maturity, and instruments governed by foreign law.

- **Internal TLAC.** The final TLAC framework should reflect a revised approach to internal TLAC by narrowing the amount of prepositioning required and the universe of cross-border subsidiaries that must receive such support in a way that better reflects its purpose—to provide host country authorities with sufficient confidence that systemically-important subsidiaries will remain solvent and open in the event of their parent company’s resolution.

- **Subordination/excluded liabilities.** The final TLAC framework’s binary approach to excluded liabilities should be revised to, among other things, provide G-SIBs with sufficient flexibility to continue to maintain a narrowly-tailored set of critical holding company liabilities that pose no systemic risk.

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