THE BANK OF NEW YORK MELLON

Brian G. Rogan
Chief Risk Officer

Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland

Ladies and Gentlemen:

The Bank of New York Mellon Corporation ("BNY Mellon") appreciates the opportunity to comment on the Consultative Documents, "Strengthening the resilience of the banking sector" ("Resilience"), and "International framework for liquidity risk measurement, standards and monitoring" ("Liquidity"). BNY Mellon is predominantly governed by the U.S. regulatory process as an Advanced Internal Ratings Based/Advanced Management Approach ("A-IRB / AMA") Basel II institution, and has a profile distinct from most companies governed by Basel—a profile dominated by securities servicing and investment management businesses. We also conduct other traditional wholesale businesses with a strong service component. Net interest income accounts for approximately 20 percent of our revenue, and our market risk profile is lower than many of our peers.

For the past ten years, BNY Mellon and its predecessors have worked with regulators and industry groups to develop and implement a capital adequacy framework that adheres to the principles set forth by the Basel Committee for Banking Supervision. We have, and will continue to, support these principles and commend the thoughtful work of the regulators in both recommending changes to the current principles, as well as proposing new guidelines surrounding liquidity. It is in the best interest of all financial institutions to be as prepared as possible in hopes of avoiding, or at least mitigating, market stresses like those we have undergone over the past two years.

After the experience we have all shared with the global liquidity crisis during the last two years, we also appreciate the thoughtful effort to propose a consistent and comprehensive liquidity framework in the proposed "Liquidity" standard.

While these comments will address the "Resilience" and "Liquidity" documents separately, two observations are persistent: both are more prescriptive in approach—less principles-based—and as a corollary both present a uniform approach to measuring and responding to risk. The more an institution has a distinctly different mix of activity and risk profile, the less aptly the prescription portrays the risk of the institution.

One Wall Street, New York, NY 10286
T 212 635 1028 F 212 635 1121 brian.rogan@bnymellon.com

Summary Comments on Bank Capital Standards

Regarding the redefinition of Tier 1 capital, the immediate non-eligibility of trust preferred securities[1] would affect U.S. institutions disproportionately given their current importance in the capital base for U.S. banks. The substantive differences of trust preferred, versus the permitted perpetual preferred equity, are both narrow and tax-driven. They do not necessarily represent differences in their ability to absorb losses as a going concern.

As for other aspects of the redefinition of capital and risk-based capital requirements, such as the full deduction of deferred tax assets which rely on future profitability and the deduction of defined benefit pension assets, we believe the premise that these assets lack any value is flawed. Deferred tax assets have shown, especially throughout the most recent crisis as weaker institutions were being acquired by other institutions, that they contain some value. We would also urge the committee to consider whether the proposed treatment of these assets raises level playing field issues when taking into consideration their tax treatment across different jurisdictions. Likewise, there is clearly value associated with defined benefit pension assets, and we believe that requiring full deduction of these assets may cause institutions to rethink whether they should continue to offer defined benefit plans. Both deferred tax assets as well as defined benefit pension fund assets provide value in terms of the reduction in future expenses which enhances going concern value, which ultimately reduces the likelihood of a liquidation situation.

Additional concerns with respect to the redefinition of capital: (a) full deduction of investment in non-consolidated financial institutions which would disproportionately disfavor service-oriented affiliates, such as securities servicing; and (b) increasing the capital charge for financial institution counterparties which would further exaggerate the risks and capital requirements of even overnight operational interbank exposure. While the proposals appear to correspond to universal banks or retail-oriented banks, they tend to mischaracterize operationally-oriented correspondent banking, and trust and custody banks. One need only compare the risk profile and history of short-term trade finance, or securities settlements with the across-the-board increase in capital for exposures to banks to see the disparity.

Substitution of uniform, mechanical capital buffers and capital conservation measures across all regulated banks and holding companies is an overly ambitious calibration exercise and overlaps with established U.S. practice of managing the same issues via a Pillar 2 supervisory process appropriate to each A-IRB / AMA institution.

With respect to the proposed leverage ratio, implicit inclusion in leverage ratio assets of off-balance-sheet indemnified (for the return of collateral to the custodial account) securities lending commitments, primarily a U.S. phenomenon, is particularly punitive. Overall, the leverage ratio would hinder or preclude indemnification of the securities lent, reducing liquidity that the present indemnities support. Depending on the calibration, it might also punish banks that have reduced risk by building portfolios around regulatory-approved derivative and other close-out netting arrangements, and add substantial capital cost to such volume-driven, but low-risk businesses as short-term transactional foreign exchange. Seemingly, measures aimed at outright risk reduction seem likely to drive out or suppress low-risk activities.

[1] A **trust-preferred security** is a hybrid security which possesses characteristics of both subordinated debt as well as preferred equity and are generally issued by U.S. bank holding companies. They are typically issued with very long maturity dates (30 years or more), are deeply subordinated, and allow for early redemption by the issuer and pay either a fixed or variable rate of interest which may be deferred for up to 5 years.

Summary Comments on Liquidity

BNY Mellon recognizes the need for quantitative measures to guideline liquidity risk management within the banking industry, and is generally supportive of the concepts of the two liquidity ratios that form the foundation of the proposed International framework for liquidity risk measurement and monitoring standards ("Liquidity"). Our own risk management framework considers the importance of a liquid asset pool that helps the firm provide the ability to withstand a short-term, acute liquidity stress scenario, as well as the need for longer-term structural liquidity to fund less liquid assets. The "Liquidity's" proposed timeframes for calculation of the ratios aligns with those used for our internal monitoring and management purposes and are appropriate. We believe that these concepts, properly calibrated, will help to reduce the industry's exposure to a systemic event.

While we generally support the concepts inherent within the proposed "Liquidity" and Basel's initial effort to facilitate consistent measurement of liquidity risk throughout the banking industry, we disagree with the calibration of the metrics (haircut, run-off, and other assumptions) without respect or consideration for an institution's business model, risk profile, product types or role within the financial system. Specifically punitive to BNY Mellon is the fundamental assumption of "Liquidity" that wholesale deposits from a financial institution are inherently "unstable." As confirmed by our experience, this approach can be punitive to low-risk, custody and trust banks such as BNY Mellon; and can result in relatively liquid institutions like ours failing metrics that riskier, more traditional banks may pass. During the recent credit crisis, our company received a large influx of deposits at the most acute juncture of the crisis.

Furthermore, we recommend the Committee re-evaluate its narrow definition of eligible buffer assets to consider other, highly liquid instruments. Paragraph 34 of "Liquidity" should be adjusted to remove sub-criteria items I – III (with the exception of requiring deep repo markets) and allow for discretion of local supervisory judgment in defining eligible assets. This amendment would allow U.S. institutions to include agency and government-sponsored entity (GSE) debt securities, as well as other Federal Reserve discount window eligible collateral, in the buffer, and would align with commonly-held assumptions and observed behavior regarding their liquidity-generating capacity.

Finally, the proposed level of detail for asset and liability data required for calculation of the metrics may not be appropriate for all institutions; our experience to date suggests compliance with the proposed "Liquidity" will create a significant, ongoing burden.

We further elaborate on the specific points of issue within the comments below.

The four sections that follow address (1) the capital definition and risk-based capital provisions of "Resilience," (2) the proposed Leverage Ratio, (3) the proposed standards of "Liquidity", and (4) general observations as to timing, implementation and knock-on effects of these proposals.

I. Capital definition and Risk-based Capital Provisions of "Resilience"

The "Resilience" document raises several prominent issues for BNY Mellon with respect to the definition of capital, risk-weighted assets and capital requirements: excluding some commonly used capital instruments from capital and deducting certain assets from

capital; imposing the volatility of unrealized gains and losses on capital; broadly increasing capital on all exposures to financial institutions; and proposing a mechanical capital buffer calculation that would, in effect, displace Pillar II considerations for an A-IRB institution such as BNY Mellon.

a. Redefinition of Capital

Trust Preferred Securities

As currently drafted, the consultative proposals appear to exclude trust preferred securities from Tier 1 capital. This would be an abrupt change to established U.S. bank funding practices and does not reflect the effectiveness of these securities to absorb losses without affecting a bank holding company's liquidity. Trust preferred securities tend to be U.S.-specific capital insturments, created largely in response to the non-deductibility of preferred dividends for U.S. tax purposes, whereas preferred dividends on non-cumulative perpetual preferred stock are deductible in major non-U.S. jurisdictions. As we read the proposal, because trust preferred securities have a maturity in order to qualify for tax-deductibility, albeit a very long maturity such as 30 years, they will be considered ineligible as Tier I capital. Under current U.S. regulations, they are currently approved as Tier 1 capital precisely because they are able to absorb losses on an ongoing basis.

As of September 30, 2009, there were roughly $141 billion of trust preferred securities outstanding among U.S. bank holding companies, amounting to about 12% of total Tier I capital for the same time period. Given the economic substance of trust preferred securities, we suggest the Committee consider either (1) amending the additional going concern capital criteria or (2) granting a national discretion to allow for the inclusion of trust preferred securities, issued with maturity dates greater than some threshold, to be included in the capital calculation. At a minimum, if the exclusion persists in the final Accord, existing issues should be grandfathered for a 30 year period to facilitate orderly refinancing.

Investments in Non-Consolidated Affiliated Financial Institutions

The deduction of all investments greater than 10% in non-consolidated affiliated financial institutions from capital, for the stated purpose of removing double-counting of capital among financial institutions, suffers from a key flaw: it makes no provision to except investments in financial institutions that have only *de minimis* risk assets, such as custodial, processing or securities servicing affiliates. These affiliates are often capitalized on other bases than risk portfolios, and far in excess of any risk-based capital requirement. Additionally, we believe that the assumption that these investments contain zero value in a stressed going concern situation is flawed and not backed by historical evidence. The income generating ability of such subsidiaries was recognized in the Supervisory Capital Assessment Program (SCAP)[2] exercise in the forecast of capital over the stress period. The assessment within the capital rules should be consistent with this recognition. Conceptually, while we support removing the double-counting of capital among financial institutions, we suggest that given the potential for very different risk profiles of financial institution cross-holdings, as well as the potential

[2] Supervisory Capital Assessment Program (SCAP) was a stress test exercise conducted in the U.S. from February through April of 2009 to assess the capital needs of the 19 largest U.S.-based bank holding companies.

that these investments do in fact have value, the committee either consider increasing the risk sensitivity of this proposal through the differentiation of investments based on a simple measure or categorization of their risk profile, or permit a national discretion regarding a partial deduction for investments in financial institutions, specifically those that carry very low risk.

Full Deduction of Deferred Tax Assets relying on future profitability

We understand that currently, capital treatment of deferred tax assets, is quite different depending on the operational jusisdiction of a banking institution. Because of these differences, we agree with the Committee's attempt to bring consistency to the treatment of deferred tax assets. However, given differences in tax laws across jurisdictions, the current proposal will not change the fact that institutions in certain countries will continue to benefit more so than others with respect to the portion of deferred tax assets that rely on future profitability.

Additionally, we disagree with the premise that these assets lack any value at all. Deferred tax assets, including those which rely on future profitability, do provide value as far as reducing future expenses which increases value on going concern basis. In fact, throughout the most recent crisis, as weaker banking institutions were being acquired by others, it was clear that there was value being given to the weaker institutions based, in part, on their deferred tax position. Under current U.S. risk-based capital standards, the recognition of deferred tax assets in Tier 1 capital is limited to those that could be realized within a one-year look forward horizon based on an institution's net income projections. We believe this strikes the appropriate balance between the uncertainty of ultimate recognition of deferred tax assets and their inherent value on a going concern basis. We favor a partial deduction approach similar to that in force in the U.S. today, whereby the recognition of deferred tax assets would be limited to those that could be realized within a one-year horizon based on a [stressed] net income measure. Finally, requiring institutions to fully deduct deferred tax assets which rely on future profitability is inherently procyclical, as deferred tax assets tend to increase during times of stress. This seems to contradict the committee's intention of mitigating procyclicality issues with respect to capital levels as proposed in other areas of "Resilience."

Defined benefit pension fund assets

The logic adduced in the "Resilience" document is unduly harsh on the value of the assets given their role in meeting the claims of retiree stakeholders. Liquidity of tangible assets such as these should not be the decisive criterion for deduction from regulatory capital. Defined benefit pension fund assets provide value in terms of the reduction in future expenses which enhances going concern value, which ultimately reduces the likelihood of a liquidation situation.

Adjustments for unrealized gains and losses

We recommend the Committee reconsider proposed treatment to include the effects of unrealized gains and losses in Tier 1 capital. Including the volatility of unrealized gains and losses in the capital calculation seems to run counter to procyclicality measures proposed elsewhere for certain assets, particularly for investment or loan portfolios with longer investment horizons or holding periods respectively. The known difficulties of market valuation in stressed markets tend to exaggerate unrealized losses, which might generate or exaggerate a transitory, computed capital shortage for individual institutions during times in which financial institutions are most vulnerable. This will likely lead to asymmetrical treatment of the securities book relative to other asset types, particularly

the loan book. Additionally, allowing unrealized gains to contribute to capital levels may cause a false sense of security, as firms will appear to have increasing capital levels when markets are at their strongest. At a minimum, the Committee should consider updating the standard for risk-weighting such securities based on their fair market value and not based on the securities' cost basis. In our opinion, we do not see this discrepancy as being adequately addressed. If the risk-weighting is not adjusted accordingly, the proposed standard will create a scenario where unrealized losses will be more punitive on capital ratios than impairment losses, which does not seem to be sound practice.

While the pro forma impact of including unrealized gains and losses for investment portfolios in Tier 1 capital would likely not materially alter the volatility of the industry's Tier 1 capital overall, the incremental effect on an individual institution could be significant. Inclusion could create sudden pressure on capital ratios, based on what may be only transient mark-to-market pricing. For portfolios with longer investment horizons, establishing appropriate provisions for losses and recognition of other than temporary impairments (which would reduce Tier1 capital), is a question best left to the accounting standard-setting bodies. Therefore, we suggest, as stated in the consultative document, that the Committee "continue to review the appropriate treatment of unrealized gains" in the going concern context of banks' varying portfolio strategies

b. Increasing Capital Requirements On All Financial Institution Exposures

The "Resilience" proposal to increase the assumed correlation by 25% for all financial institution exposure will increase capital requirements by upwards of 35%. BNY Mellon understands and appreciates the reasoning behind the Committee's proposal to increase the correlation factor of counterparty credit exposures related to financial institutions. Identifying and mitigating excessive concentration risk is clearly worthwhile and important. However, this proposal, in its current form, offers several calibration challenges and a potentially disruptive market impact, and would be best handled via the assessment of concentration risk in the Pillar 2 process rather than a blanket approach.

Its broad application, however, places an incremental tax on the whole interbank market, the network of transfers, clearing, trade finance, and other short-term correspondent banking and administrative functions that are essential to an efficiently functioning banking system. Joined to the historical Basel decision to overweight capital for short maturities, such as overnight operating exposures among banks, the result is a high capital requirement for financial infrastructure activity that has generated *de minimis* losses historically. This proposal adds costs to an already low-margin, low risk business, and thereby may also diminish overall market liquidity by pushing institutions away from this activity.

Moreover, because the correlation multiplier distinguishes between financial institutions that are regulated and greater than $25 billion in size, and those of any size that are unregulated, this proposal would create an incentive for firms to avoid this cost. Banks will be encouraged to move funds from, for example, one large institution, to multiple small institutions to carry out routine banking functions. This regulatory tilt would appear to be counterproductive to the efficient function of the banking system. It could create more instability in the system, and add complexity.

Lastly, should the proposal to increase the correlation multiplier persist into final guidance, the Committee should carefully consider its guidelines for defining 'financial institutions' and aggregation of group exposures relative to the $25 billion threshold, as

ambiguity in defining these guidelines could lead to potential inconsistencies in treatment that are counter to the spirit of the principle.

c. Specifying Capital Buffers and Conservation Requirements to Mitigate Procyclicality

We welcome the Committee's efforts to address those aspects of current Basel II rules that are inherently, albeit to a limited extent, procyclical. We do ask, though, that any approach be handled with caution given the daunting challenge of global calibration. The Basel II Accord, until now, has proclaimed Pillar 2 -Supervisory Review, as one of three "pillars" of a sound regulatory capital regime for internationally active banks. For a U.S. institution that has spent significant effort in developing a Pillar 2 approach that deals with the procyclicality of the Basel II capital requirement through robust capital planning and stress testing, the proposal currently offered in "Resilience" seems to diminish the relevance of Pillar 2 as a methodology.

While the new capital buffer and conservation mechanisms could be effective benchmarks or early warning signals for Pillar 2 discussions, a mechanically applied version of the proposal will most likely hinder the Pillar 2 process now in place for larger U.S. and global banks. That eventuality would occasion a considerable loss of accuracy, flexibility and recognition of institution-specific considerations, which are now handled under Pillar II. We absolutely support early warning measures and triggers to focus on individual banks' capital adequacy and see some limited value to the capital buffer calculations in this regard. The actions to be prescribed in response, however, should be suited to the individual bank's circumstances.

For example, in the U.S., banking institutions are already encouraged, through regulation, to hold capital levels above the minimum levels that Basel II requires. In the sense that U.S. banks already hold capital such that they are deemed 'well-capitalized,' at ratios above minimum required capital levels, the U.S. already effectively functions with a capital buffer concept that facilitates prompt management and supervisory discussion as capital levels approach the 'well capitalized' boundary levels. However, the specific actions responding to such a situation should based on the bank's particular forward-looking assessments and an appropriately approved capital management policy and contingency plan, coupled with supervisory notification and dialogue before and during the actions.

If, in the larger scheme of regulatory supervision, the Basel Committee determines to use such a mechanism, we recommend an "opt-out" provision, with the consent of primary national regulators, or even more cleanly, provision for a national preference to adopt or abstain from the calculated buffer and conservation mechanism on a country by country basis.

d. Other Risk-Based Capital Issues

We view the expansion of targeted capital ratios from two to three—focusing newly on the common equity component of Tier 1 as distinct from Tier 1 generally—as spurring a new drive for increased common equity capital. We agree with the Committee's belief that banking institutions should have more common equity as a proportion of Tier 1 and that the equity should be of high quality, although this proposal may place an additional constraint on institutions' ability to lend. A phased introduction of new common-equity-specific requirements could alleviate both the hindrance to economic recovery and the

possibility of capital markets stress due to institutions' competition to raise required equity capital. For instance, allow the requirements to begin at levels that would not trigger material incremental capital-raising at the outset, and then steadily increase to target levels over a transition period of three to five years.

II. Leverage Ratio

The Leverage Ratio proposed in "Resilience" is explicitly a "non-risk-sensitive" measure, like the leverage ratio currently required in the U.S. As a U.S.-based banking institution, BNY Mellon is accustomed to managing to a leverage ratio. BNY Mellon believes, however, that while a leverage ratio can serve a useful purpose as a general barometer of risk-taking appetite, it does not substitute for a risk-based capital measure. A supplemental metric such as a leverage ratio should be complementary and not a constraining factor. Therefore, the committee should ensure that calibration of the ratio is such that it will not preclude banking institutions from taking any risk. We have identified two broad concerns regarding the new leverage ratio being proposed:

(1) The Leverage Ratio is conceived as a floor to assure an institution does not maintain excessive amounts of risky assets relative to capital; but at the same time, even if unintentionally, it drastically penalizes long-established, low-risk, operational banking exposures.

(2) The Leverage Ratio, if not remediated, may harm the viability of businesses that generate low-risk exposures if the definition of leverage ratio assets or minimum standards are not appropriately calibrated to the substantial variations that will likely arise from implementation across institutions with similar levels of assets but substantially different risk profiles.

As a governing, dominant capital standard, a leverage ratio represents a step backward for Basel. Two of the three prime purposes of Basel I's implementation 20 years ago were to "make regulatory capital more sensitive to differences in risk profiles among banking organisations" and to "lower the disincentives to holding liquid, low risk assets."[3] Ten years ago, Basel II was proposed because in many respects Basel I was not risk sensitive enough to accomplish those goals. A dominant, explicitly non-risk-sensitive leverage ratio negates these efforts, in respect of liquid, low risk assets and low risk credit exposures generally.

This is an old, but large issue: the large-scale disintermediation decades ago that created the prime commercial paper market was driven by non-risk-sensitive bank capital ratio requirements. Traditional, low-risk, functional exposures disfavored by a leverage ratio, e.g., cash collateralized lending, generally earn correspondingly modest spreads, and often facilitate traditional banking operational services.

A leverage ratio intended to provide a crude floor under complex risk-based capital calculations instead tends to identify any institution with a comparatively modest risk appetite as having an elevated amount of leverage. The market, especially given the events of the past two years, tends to view negatively any and all leverage. This would therefore punish banks that may have modest risk levels, but relatively high leverage ratios.

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[3] Jackson, *et al.*, "Capital requirements and Bank Behaviour: The impact of the Basle Accord," BCBS Working Papers No. 1, April 1999, p. 1.

The current proposal would include off-balance sheet items in the leverage ratio with a 100% credit conversion factor, and would include items that are part of low-risk, low-margin businesses, potentially prompting many of these institutions to reconsider operating within these businesses.

By the terms of "Resilience," indemnified securities lending, where exposures are generally held off-balance sheet, appears to be included as part of the proposed Leverage Ratio calculation (though without being named explicitly.) The capital implied by including it at a 100% credit conversion factor, even at a Leverage Ratio calibration of 4%, represents a *capital requirement* greater than the *risk-weighted assets* computed under Basel II. Given the extremely low risk and low spreads associated with indemnified securities lending, the Leverage Ratio itself would present powerful incentive to cease indemnification of these transactions. The liquidity and smooth function of the government securities and other securities markets would likely diminish as institutional investors would have to develop credit infrastructure and expertise to conduct non-indemnified securities lending.

Similarly, short-term transactional foreign exchange (less than 14 days) could significantly inflate the leverage ratio when measured under the current exposure method, especially since the volume of trades (and therefore the add-on computed as a percent of notional) is high. Market risk is typically minimal, given a matched book approach, and counterparty credit risk is similarly low through the use of netting and collateral arrangements, yet many administrative functions in servicing securities and institutional investors involve large volumes of these trades.[4] We therefore strongly urge the Basel Committee to consider exempting highly liquid short-term FX transactions.

As for the last specific element of the leverage ratio proposal, the first approach set forth with respect to netting exposures—to disallow it entirely—seemingly contradicts established regulatory standards, which are in turn based on considered analyses of legal enforceability. Because both prudent risk management and the current form of Basel II have encouraged carefully drawn netting arrangements, the industry has embraced this form of credit risk mitigation. As a result, the un-netted inflation of the balance sheet for purposes of the Leverage Ratio—in the interests of "international consistency"—would be significant and counter to rewarding effective risk management.

Regarding the leverage ratio generally, while it is not hard to discern an uneven playing field for financial institutions when a new regulatory structure is implemented across national boundaries, differences in U.S. GAAP and IFRS, do need to be accommodated. We recommend the Committee consider systematic accounting differences, to the extent the ratio draws from on-balance-sheet measures.

The impact of a leverage ratio on *all* very low risk assets or exposures, short of further disintermediation, will simply raise the costs of these ordinary functions, or further hinder market liquidity and function. Institutions will have incentive to rein in customer accommodations or facilitations that have been made too costly in capital terms.

Notably, the benefits adduced to the proposed Leverage Ratio are already available through a vigorous Pillar II regime that reviews the specific nature of an organization's risk exposures and associated risk management practices. Within the U.S., for instance, where there is a leverage ratio that has been required for many years, neither the indemnified securities lending nor the derivative nominal amounts appear in the ratio.

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[4] On a representative date at BNY Mellon, for instance, 26% of FX nominal principal was on open trades of 7 days or less to maturity, 62% to trades of 30 days or less. 99% of nominal principal pertained to trades of less than 1 year.

Yet the supervisory process has permitted differentiation in practical capital requirements among institutions.

If, as with the proposals for mechanistic capital conservation measures, there are practical supervisory needs that a leverage ratio must serve in some national jurisdictions, we would urge a more refined calibration of the proposed leverage ratio for off-balance sheet exposures or that application be subject to national discretion so as to exempt certain low-risk financial intermediary businesses.

III. Liquidity Framework Appraisal and Comments

a. Calibrations of Assumptions Without Regard for Business Model

Without consideration of the firm's business activities, risk, capital levels, role in the market, credit and CAMEL ratings, liquidity stability cannot be properly assessed. Because liquidity is a second-order risk, these factors cannot be ignored when assessing relative liquidity position and risk under either a short-term or more protracted stress event. By applying the same standards and assumptions to fundamentally different institutions (maturity transformation vs. trust and custody banks) with markedly divergent funding profiles (short-term, wholesale, or unsecured vs. deposit-based funding), the Committee unduly penalizes the relatively stable, risk-averse institutions. Liquidity assumptions about stability should be sensitive to a bank's business and risk profile.

When analyzing BNY Mellon's business model and risk profile, it is important to understand the lines of business in which it participates. This business model is unique, and has specific liquidity implications that differ from a traditional commercial bank. BNY Mellon serves its clients through three primary lines of business: asset and securities servicing (custody, fund services, securities lending, liquidity services, government securities clearance, etc.), wealth management and asset management. BNY Mellon's global client base consists of financial institutions, corporations, government agencies, endowments and foundations and high-net-worth individuals. The proposed framework lacks the specific distinction for BNY Mellon's business model attributes and applies poorly to infrastructure-oriented institutions such as a trust and custody bank managed mostly within the U.S.

In addition, the framework, as designed, applies solely to a bank model and ignores differences in the balance sheets, regulatory and legal requirements, business models, and associated liquidity profiles of certain non-bank entities (e.g. broker dealers). As a result, there is an issue with the application of the proposals within "Liquidity" where the resulting ratios can be misleading and not representative of the risk of the non-bank entity. We recommend the Committee consider a separate calibration for non-bank entities to properly apply the ratios and quantify risk.

We highlight the following assumptions within "Liquidity" that we believe are particularly onerous, are inconsistent with observed behavior, and warrant review by the Committee.

Deposits

We strongly feel that a deposit from a financial institution does not always equal market funding, which appears to be the regulatory view inherent in the proposal. A distinction should be made between "deposits from financial institutions" and those deposits with which BNY Mellon has an operational relationship with a financial service customer.

With the current proposals in "Liquidity", trust and custody banks are unduly penalized due to the overly conservative assumptions regarding the stability of these deposits; the 100% runoff rate assumption does not align with the observed behavior of these deposits during times of stress.

These deposits exist for operational and business reasons. Our historical experience is that they are stable balances despite market factors, and are considered a "core" source of funding for our Company. Our experience through the recent crisis was that deposit balances increased, due to our business model and operational relationship with our clients. For example, in the five month period from August 2008 to December 2008 we experienced a 49% increase in total deposits with a 24% increase in interest-bearing deposits and a 142% increase in non-interest bearing deposits. We suggest that factors applied to these operational deposits be based on average usage of facilities or withdrawal of deposits observed during periods of market stress. The recent financial crisis provides insight into these points of reference.

Committed Facilities

The use of a 10% factor for drawdowns on committed credit facilities with non-financial corporate counterparts versus a 100% factor for "all other" credit and liquidity facilities assumes a strict duality which may not be consistent with actual client behavior. Operational liquidity lines do not consistently exhibit the characteristics suggested in "Liquidity". For example, in the four month period from September 2008 to December 2008 BNY Mellon experienced an average drawdown of 5% on its committed lines.

If the highly conservative drawdown assumptions are applied, then the asymmetry in assumptions should be addressed within "Liquidity". Specifically, we recommend that the assumption that institutions will receive no cash inflows from a committed credit facility during times of stress be recalibrated. The asymmetry in the assumptions is not logical and the proposal appears to assume that all bankers concerned will effectively ignore the rule of law—in this case, contract law. That does not match bankers' historic behavior or profile. The Committee may consider distinguishing between committed lines with material adverse clauses (MAC) or cash flow, coverage and liquidity covenants that would allow banks to renege on committed lines.

Goodwill and Intangibles

The proposal requires that institutions provide 100% long-term stable funding for Goodwill and other intangible assets ("all other assets"). Such assets should be excluded as they are accounting balances that are funded by equity. Since these assets are excluded from the calculation of Tier 2 Capital, they should be excluded from the funding requirement. Otherwise, the funding requirement would be double counted. Any funding required for these assets will represent a significant incremental cost to the institution.

b. Narrow View of Liquid Buffer Assets

The proposal suggests that the sole source of reliable liquidity in the event of a short-term crisis is the stored asset liquidity that a financial institution carries on its balance sheet in the form of unencumbered cash and government securities. While we

recognize the Committee's global approach to definition of buffer assets, we suggest a slightly broader approach that acknowledges local differences in asset liquidity.

The highly restricted definition of liquid assets may have unintended consequences in that it will likely increase the concentration in eligible assets and decrease market liquidity for these same assets. If the assets favored by this regulatory treatment run into problems from any quarter, the entire banking sector will be concentrated in these assets. In times of systemic stress, there is a risk of a "fire sale" effect on eligible assets which can depress prices and further exacerbate the stress. Consider, for example, a market shock that suddenly transmits mark-to-market unrealized loss stresses across the sector.

As mentioned, we recommend the Committee amend Paragraph 34 of "Liquidity"to re-evaluate its narrow definition of eligible buffer assets and allow for local supervisory judgment in defining eligible, highly-liquid assets. This amendment would address the liquidity-generating capacity and application of commonly-held agency and GSE debt securities (FNMA and FHLMC). In the event that such commonly-held agency and GSE debt is excluded from the definition of eligible buffer assets, BNY Mellon would have to convert such assets to qualifying liquid assets. Such a conversion would cost an additional $50 million approximately. In addition, we recommend that the Committee align haircut assumptions with those observed within the Central Bank haircut tables.

c. Potential Unintended Consequences to the Broader Market

In addition to the specific impacts of the proposals in "Liquidity" on BNY Mellon's business model and liquidity risk management framework, the proposals may have broader implications for the market which warrant consideration by the Committee.

- The regulatory mandate towards a matched-funding model will have an impact on bank's traditional maturity-transformation role. This will reduce credit in the interbank market and credit available to consumers and companies.

- Prescriptive rules will lead to the increased size of liquidity pools, resulting in an increase in the negative cost of carry for such liquidity. The higher cost of funds will be reflected through increased costs charged to clients and/or reduced lending and market making.

- Market deposit pricing will change substantially, with term and retail deposits becoming more valuable. Increased competition for the same deposit base may have an adverse impact on the stickiness of these deposits. In addition, as wholesale deposits become comparably less valuable from a regulatory perspective, it can be expected that funding will leave bank balance sheets and flow to money-market funds; this will lead to further disintermediation and further threaten the stability of the system.

- Application of the proposed standards and monitoring tools to individual subsidiaries of internationally active financial institutions may be detrimental to liquidity when viewed in the context of the consolidated organization. Overseas entities may be required to bolster their stock of assets to satisfy the requirements, thus raising costs and potentially "trapping" the liquidity.

These, and other potential issues for consideration are described in detail by the Institute of International Finance; BNY Mellon generally agrees with their assessment of the

proposed guidance in regards to the broader market impacts and comments for consideration.

IV. General Observations as to Timing, Implementation and Knock-on Effects

As a market-infrastructure-oriented, U.S. institution, BNY Mellon has gone through the financial crises of the last two years, and cooperated with the governmental responses at each stage. We would be remiss not to add some general observations that bear on the current Basel consultative documents and the regulatory implementation that will follow.

First, markets anticipate advertised events, such as the implementation of the capital and liquidity proposals—what is frequently termed "announcement risk." Market prices would be quick to respond, whatever the state of the economy. Even if a final implementation date were as distant as 2014, suppliers of capital to banks would see a combined trend of higher capital requirements, higher compliance costs, and more restrictions on their business model, regardless of their risk appetite. Their diminished enthusiasm could only prolong and reinforce the economic downturn that is still with us. If there is good news to be found, such as clarifications and modifications of the more disruptive regulatory proposals, better to get to such news sooner than later. Banks and bank investors alike will benefit from certainty and from credible relief from possible regulatory outcomes.

Finally, the recent crisis has put renewed scrutiny on both risk management and regulatory supervision, but the principle of enhancing these functional competencies is still sound. Enhanced risk management and regulatory supervision are the most promising resources to address the issues of the next crisis.

Certain elements of the current Basel proposals attempt to reduce banks' risks outright, this in contrast to Basel I and earlier versions of Basel II. The Basel proposals have always strongly emphasized and encouraged good risk management and supervision. Regulatory measures to reduce risk-taking *a priori* have historically tended to be imprecise, in part because of differences in national markets, and in part because of the wide variety of businesses and practices actually found among banks. The cost of imprecision will necessarily be to raise the cost of providing financial services, and in some cases dislocate the channels through which services are provided. In our view, investment in enhanced management and supervision capabilities continues to be a safer, more efficient, and more adaptive way to reduce the risks our financial economy will face.

Sincerely,

Brian G. Rogan