Mark D. Linsz
Corporate Treasurer

October 1, 2010

VIA E-MAIL: **baselcommittee@bis.org**

Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Re: Basel Committee on Banking Supervision, Consultative Document "*Proposal to ensure the loss absorbency of regulatory capital at the point of non-viability*", August 2010

Dear Messrs. and Mmes.:

Bank of America Corporation (together with its affiliates, "Bank of America") appreciates the opportunity to comment on the Basel Committee on Banking Supervision's (the "Committee") Consultative Document entitled "*Proposal to ensure the loss absorbency of regulatory capital at the point of non-viability*" published in August 2010 (the "Consultative Document"). Bank of America, with total assets over $2.3 trillion at June 30, 2010 is the sole shareholder of Bank of America, N.A. and Merrill Lynch & Co. Inc., and has full-service consumer and commercial operations in 50 states and the District of Columbia. We serve clients in more than 150 countries worldwide. Bank of America provides banking, investing, corporate and investment banking services and financial products to individuals and businesses across the United States of America and around the world.

We support the Committee's objective to strengthen the loss absorbency of non-common Tier 1 and Tier 2 capital instruments. The Consultative Document is an important first step towards this goal, but we believe that further refinement of the proposals set forth in the Consultative Document is necessary for a workable solution.

The Consultative Document outlines criteria intended to ensure that qualifying capital instruments issued by banks are capable of absorbing losses in the event that a bank is unable to support itself in the private market. The Committee proposes that the determination of whether a bank is unable to support itself in the private markets be triggered upon a decision to inject public sector capital (or equivalent support) or a conclusion by supervisory authorities that the institution would not otherwise be viable without a write-off of regulatory capital instruments. The proposal requires that regulatory capital instruments include a structural mechanism in their terms and conditions to ensure that they absorb loss at the point of non-viability, either through write-off or conversion to common shares. The articulated policy rationale for the proposal is to decrease the likelihood that public sector injections of capital would protect investors in capital instruments and to reduce the moral hazard associated with the perception of government support.

We highlight the most critical areas associated with the Consultative Document below. We ask that the Committee apply focus to the following areas as it works to strengthen the quality and loss absorbency of capital in the banking industry:

- *Market Feasibility is Uncertain:* The feasibility and viability of contingent capital instruments for United States institutions is uncertain. The viability of contingent capital instruments in the United States remains unclear due to their tax features, investor base size and requirements, and lack of precedent. We believe the cost of issuing such instruments would be substantially greater than current non-equity capital instruments. Their issuance should be voluntary and subject to negotiation by banks and their investors rather than determined by regulators.

- *Tax, Legal and Accounting Differences Could Create an Unlevel Playing Field:* A requirement that United States banks raise significant amounts of non-deductible contingent capital may have unintended negative consequences and create competitive equity concerns relative to banks in other jurisdictions where tax deductibility is not an issue.

- *The Trigger Event for Public Injection of Funds is No Longer Relevant in the US:* The first trigger, concerning the injection of public sector capital, should be viewed as inapplicable to United States banking organizations following the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

- *The Trigger Criteria is Far too Subjective:* Clear and objective guidelines should be established to support the decision that a public sector injection or write-off of regulatory capital is necessary to ensure the viability of an institution. The triggers proposed in the Consultative Document are very subjective, allowing for a high degree of latitude by supervisory authorities without reference to specified criteria.

- *Further Study is Required:* We urge the Committee to consider the Consultative Document's loss absorbency requirements in the broader context of the December and forthcoming proposals for capital surcharges and bail-in debt, as well as with an eye towards recent legislative and regulatory developments in local jurisdictions. Further study would allow a unified package of proposals to be constructed and its impacts evaluated holistically by the industry and supervisory authorities.

- *Additional Technical Concerns:* We recommend that the Committee grandfather instruments issued before the implementation date, permit structures with carefully designed partial or temporary write-down features and permit a reasonable portion subordinated debt to continue to be included in Tier 2 capital.

Bank of America is a member of the International Institute of International Finance ("IIF"), the Risk Management Association ("RMA"), The Clearing House Association and the American Bankers Association ("ABA"), and has participated in the preparation of their

comment letters. We are supportive of the IIF, the RMA, The Clearing House and the ABA comment letters. These letters contain detailed responses to many of the individual recommendations listed in the Consultative Document and therefore are not repeated in this letter.

We support the notion that banks should hold capital of robust quantity and quality, and in levels that are credibly expected to absorb losses in a stressed environment. Banks are already taking measures to enhance the quantity and quality of their capital. However, we encourage the Committee to refrain from introducing requirements that have uncertain market feasibility, do not leave sufficient flexibility for national discretion, promote an unlevel playing field, are unnecessarily subjective and that are not fully harmonized with other initiatives.

Market Feasibility is Uncertain

In the United States ("US"), contingent capital instruments such as those contemplated by the Consultative Document are untested. Investor demand for these instruments has not been ascertained, and this form of capital may prove highly expensive for banks (potentially more expensive than the issuance of common equity or preferred stock). The capital securities proposed in the Consultative Document would have their upside limited to the contractual return of a debt instrument, however the potential risk profile of an equity security, which carries the risk of total loss and is a fully subordinated position during insolvency.

Given limited investor experience with hybrid capital instruments and restrictions applicable to certain traditional subordinated debt investors concerning their ability to hold equity and convertible securities, it is not clear that there would be a ready market for contingent capital in the United States. Additionally, at least one nationally recognized statistical ratings organization has published a view that contingent capital instruments issued in the United States might not be able to obtain credit ratings.[1] Since institutional investors are generally constrained in their ability to invest in unrated securities, market demand will be further reduced. More broadly, investor appetite will be extremely limited for instruments that can be written off on a completely discretionary basis.

As a result, we expect that the cost of contingent capital containing discretionary write-off provisions will include substantial investor premiums to compensate for the limited investor base and substantial uncertainty from subjective conversion or write-off trigger events. Moreover, we expect that the prospect of dilution of ownership interest followed by a trigger event would also increase the cost of capital for common stock.

We believe that contingent capital products should be more carefully considered prior to adopting regulations that in effect mandate that financial institutions issue certain minimum

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[1] *See, Moody's Guidelines for Rating Bank Hybrid Securities and Subordinated Debt*, at page 10, dated November, 2009, and *Moody's Investors Service Special Comment; Ratings Considerations for Contingent Capital Securities*, dated February 2010.

amounts of contingent capital. We fundamentally believe issuing such instruments should be voluntary with the terms and conditions negotiated by banks and their investors to meet their specific funding needs and investment constraints.

Tax, Legal and Accounting Differences Could Create an Unlevel Playing Field

We strongly support the goal of consistent global capital definitions, harmonized capital adjustments, and minimum requirements. However, to maintain the level playing field, it will be critical to address local accounting, taxation, and other regulatory rules through some degree of national discretion. United States tax considerations create regulatory uncertainty for instruments such as contingent capital that contain features of both debt and equity. Until tax and other issues are addressed, it is premature to adopt regulations requiring banks to issue contingent capital.

The proposed rules cannot be applied without distorting international competitive equity. A rigorous definition of capital applied to jurisdictions with significant variances in accounting standards, tax laws and banking regulation will likely undermine consistency in application, causing inequities for comparable businesses across countries. We understand the Committee's goal of minimizing national discretion but urge caution in extending this principle to the point that it exacerbates the impact of differing accounting and tax treatments rather than facilitates comparisons of capital adequacy. Until accounting standards are aligned, a degree of national discretion will be required to ensure the rules as applied are broadly comparable across jurisdictions.

Most instruments eligible for inclusion based on the proposed definition appear unlikely to be tax-deductible in the US, but nevertheless receive favorable tax treatment in non-US tax jurisdictions. As a result, banks outside the US will have the benefit of tax-deductible regulatory instruments and US banks will not. This will raise the funding costs for US institutions and translate into a higher cost of credit for their customers.

The Trigger Event for Public Injection of Funds is No Longer Relevant in US

The first trigger, concerning the injection of public sector capital, should be viewed as inapplicable to United States banking organizations following the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("the Dodd-Frank Act"). We urge the Committee to clarify that national discretion is appropriate in establishing triggers for each jurisdiction.

The Dodd-Frank Act removes the likelihood of public support for specific institutions and provides new resolution mechanisms for failures of both bank and non-bank financial institutions. The recent US legislation creates an orderly liquidation authority which does not permit public rescue of a failing financial firms. Financial firms whose failure could have significant consequences for US financial stability will be resolved in an orderly fashion by the Federal Deposit Insurance Corporation using special tools and authorities. All firms

entering the process must be liquidated with costs imposed on shareholders, regulatory capital investors, and creditors. Additionally, the legislation prohibits public sector rescues through Federal Reserve System emergency lending and other channels.

Existing US legislation therefore already subjects investors in regulatory capital instruments to losses through orderly liquidation authority rendering the need to accomplish this goal through structural features of contingent capital unnecessary. In this context, including an additional write-off feature to regulatory capital instruments will add avoidable complexity, create confusion for investors, reduce funding flexibility, and raise the cost of capital.

The Trigger Criteria is Far too Subjective

The triggers proposed in the Consultative Document are very subjective, allowing for a high degree of latitude by supervisory authorities without reference to specified criteria. Clear and objective guidelines should be established to support the decision that a public sector injection or write-off of regulatory capital is necessary to ensure the viability of an institution. While a subjective approach provides flexibility, it could unnecessarily frustrate market expectations and undermine important principles of fairness. This is of heightened concern because the write-off or conversion of non-common Tier 1 and Tier 2 instruments creates the possibility that more senior capital instruments will absorb losses before common equity and reverses the normal priority of claims.

As noted above, investor appetite will be extremely limited for instruments that can be written off on a completely discretionary basis. Investors in contingent capital instruments generally favor a measurable metric such as the breach of a fixed regulatory capital ratio. Objective criteria may also be required to establish ratings on regulatory capital instruments which are also important to many investors.

Clear guidelines that steer the decision would not only improve investor appetite for contingent capital instruments, but also would mitigate the potential for unintended consequences for troubled yet still viable institutions. We are concerned that there might be a natural bias towards triggering a write-off or conversions due to an excess of caution and the absence of supervisory downside to a false positive declaration of non-viability. In light of this, the threat of a trigger event might also cause investors of regulatory capital to withdraw at early signs of trouble and perhaps preclude an institution from raising capital when needed. Clear guidelines would alleviate this concern. At the same time, the supervisory authorities should be required to fully document the deliberation process and supporting evidence for any declaration of non-viability. Transparency through public disclosure, with an appropriate lag, would help reinforce adherence to the guidelines, ensure equitable treatment across institutions, and promote the appropriate level of due diligence for decisions that have such important ramifications.

Further Study is Required

In a very short period of time, the Committee has proposed significant increases in minimum capital ratios, increased risk weighted assets, introduced capital conservation and counter-cyclical capital buffers, and redefined Tier 1 capital via increased deductions. We understand the Committee is also exploring capital surcharges for systemically important institutions and bail-in debt. We urge the Committee to consider any requirement of new regulatory capital instruments more holistically and in the broader context of these other proposals.

We are very concerned that the issuance of new instruments to meet the non-common Tier 1 and Tier 2 requirements will be very expensive and ultimately uneconomic relative to common equity. The cumulative new requirement for capital may greatly exceed market capacity due to limited investor appetite for the instruments as defined. This situation is particularly acute in the United States where the recent Dodd-Frank legislation has already begun to influence the viability of trust preferred securities as a component of regulatory capital. As a result, United States based institutions may increasingly be forced to meet both Tier 1 and Total capital requirements with a significantly high concentration of common equity.

There is at least a risk that such a concentration of common equity in fact becomes the practical result of the cumulative impacts of many different and overlapping legislative and regulatory demands. We do not believe, however, that this result – with its high cost, lack of flexibility, and unique risks – is the intended result of any one of the ongoing legislative or regulatory initiatives. Accordingly, we urge further dialogue, harmonization and refinement of these proposals in a coordinated and unified manner.

Additional Technical Concerns

Grandfathering and Phase-In

The requirements for new contingent capital instruments should be phased in over at least a 10 year period to allow markets to develop and an orderly realignment of capital structures. We are concerned that the Committee's September 12, 2010 press release indicates that the transition arrangements may only apply to instruments issued before the September 12 release date. This implies current issuances would be required to contain the trigger conditions in order to eventually be recognized. Therefore, firms will need to negotiate the terms and conditions for new capital issues based on the proposal set forth in the Consultative Document and expose themselves to significant uncertainty in the execution of their capital management plans.

We recommend that this approach be modified to allow for a more orderly transition. The Consultative Document's requirements should not become fully effective for all newly issued Tier 1 and Tier 2 instruments until the conclusion of a reasonable and gradual transition period lasting at least 10 years, which would permit the development of a market for contingent capital instruments, including the development of standard structures, the evolution of tax and legal standards, and similar criteria.

Partial and Temporary Write-downs

We urge the committee to consider adapting the required terms and conditions to permit structures that allow, when appropriate, partial write-downs or conversions within reasonable bounds rather than full write-offs. We believe that calibrations of this nature would allow intervention to be designed with a higher degree of precision, and would reduce investor uncertainty while still accomplishing the goal of requiring loss absorbency. Also, we recommend allowing approaches that permit temporary write-offs or conversions, which could be reversed at the time the bank returns to profitability and public sector funds are repaid, or in cases where circumstances develop that demonstrate that the triggering event was a false positive.

Limited Recognition of Traditional Subordinated Debt

The Consultative Document outlines several beneficial features of traditional long-term subordinated debt. These include significant loss absorbency in a gone concern situation, lower funding costs relative to equity, and providing an efficient market mechanism for constraining excessive risk through increased yield requirements. We also note that long-term subordinated debt is an important tool for managing liquidity and interest rate risk. While we understand that the composition of regulatory capital will be more heavily weighted towards common equity and similar instruments, we believe that the Committee's approach to capital requirements should be balanced and recognize the powerful benefits that subordinated debt provides.

We strongly urge the Committee to permit a reasonable portion of Tier 2 capital to continue to be comprised of traditional subordinated debt. We suggest an appropriate limit of 50% is reasonable, particularly in light of the increased weighting that common equity will have in the Tier 1 component of capital. As the Committee observes in section 1 of the Consultative Document, elimination of subordinated debt funding would have undesirable consequences.

Summary

Bank of America strongly supports the objective of improving the capital adequacy of the banking sector, particularly in light of events during the most recent credit cycle. In doing so, it is important to ensure that the framework of international capital regulation remains sound. We are supportive of the Committee's efforts to strengthen and harmonize global capital regulations and promote a more resilient banking sector. At the same time, however, we believe that approaches should be balanced, coordinated, and flexible, and should strive to minimize unintended consequences. Sensible improvements to the banking sector's ability to absorb shocks arising from financial and economic stress will allow banking organizations to serve better their consumer and commercial clients, and to stand as a reliable source of strength performing core financial intermediation functions for the real economy during all points in future credit cycles.

We would be happy to discuss our views in greater detail or discuss any new ideas the regulatory authorities wish to pursue. In that regard, please contact Paul J. Baalman, Managing Director for Capital Management at (980) 386-4573, or John S. Walter, Managing Director for Risk & Capital Analysis at (415) 913-2706.

Sincerely,

Mark D. Linsz
Treasurer
Bank of America