



American Express Company
200 Vesey Street
New York, NY 10285

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Via Electronic Delivery

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

Re: Credit Risk – Revisions to the Advanced Approaches

Ladies and Gentlemen:

American Express Company (“American Express” or the “Company”) appreciates the opportunity to provide our comments to the Basel Committee on Banking Supervision (the “BCBS” or “Committee”) on its consultative document (the “Consultation”) that proposes revisions to the internal models based approach to the calculation of credit risk capital requirements for banking organizations (the “IRB Approaches” or “Advanced Approaches”).¹ The Consultation is one of several recently proposed changes to the BCBS measurements for credit and operational risk capital requirements. As a result, our comments address both implications for the capital framework, generally, together with specific considerations related to the Consultation.

American Express strongly supports national regulators’ discretion, as described in the Consultation, to eliminate use of the IRB Approaches. Elimination of the IRB Approaches would meaningfully reduce both complexity and variability of regulatory capital requirements. Importantly, however, significant issues with the proposed changes to standardized approaches to credit and operational risks measurement exist. Those proposals were designed for large universal banks and, as more fully described in our comment letters to the BCBS, would disproportionately impact credit card issuers like American Express.² Thus, as set forth in those letters, American Express has

¹ BCBS, Consultative Document: Reducing variation in credit risk-weighted assets – constraints on the use of internal model approaches (Mar. 2016), available at <http://www.bis.org/bcbs/publ/d362.pdf>.

² See American Express’ comments to the BCBS’ Consultative Document: Revisions to the Standardised Approach for credit risk, available at <http://www.bis.org/bcbs/publ/comments/d307/americanexpress.pdf>

American Express’ comments to the BCBS’ Second Consultative Document: Revisions to the Standardised Approach for credit risk, available at <http://www.bis.org/bcbs/publ/comments/d347/americanexpress.pdf>

recommended certain adjustments to the proposals related to the standardized approach, as well.

For those jurisdictions that do not elect to eliminate the IRB Approaches, American Express believes that the Committee's goals of reducing complexity and improving comparability of the regulatory capital framework may be furthered by incorporating certain enhancements designed to better align risk and capital, especially for credit card businesses like American Express. In addition, expanding certain proposals in the Consultation to apply more broadly throughout the BCBS capital framework, such as the distinction between "transactors" and revolvers" would foster more consistent and risk-sensitive treatment across customer segments. We also urge the Committee to consider the impact of the Consultation in combination with, and as potentially impacted by, other recently proposed revisions to the capital framework.

I. Overview of American Express

American Express is a global services company whose principal products and services include payment card products and services for consumers and businesses around the world. American Express' charge cards, one of our primary products, require customers to pay their bill in full each month, whereas customers of our credit card products have the option to pay their bill in full each month or carry a monthly balance on their cards to finance the purchase of goods or services. Unlike other types of credit lines, credit cards are not designed to provide borrowers with access to cash or liquidity; instead, they are used primarily to facilitate convenience spending. In fact, a significant portion of our customers are "transactors," who pay either in full or a large portion of the balance each month, and are therefore not "revolvers" who routinely carry a balance on their account.

II. Future of the IRB Approaches

Importantly, the Consultation provides that, in lieu of using internal models for calculating regulatory capital, "jurisdictions will be considered compliant with the Basel framework if they do not implement any of the internally modeled approaches (i.e. they allow use of the standardised approaches only)."³ For the reasons described herein,

American Express' comments to the BCBS' Consultative Document: Operational risk - Revisions to the simpler approaches, available at <https://www.bis.org/publ/bcbs291/americanexpress.pdf>

American Express' comments to the BCBS' Consultative Document: Standardised Measurement Approach for operational risk (not yet published by the BCBS)

³ Consultation at 3.

American Express supports the Consultation's statement that local regulators maintain discretion to utilize the standardized approaches only – and, therefore, eliminate the IRB Approaches. American Express similarly encourages U.S. regulators to exercise their authority to rescind the IRB Approaches domestically.

Many U.S. banks incur significant costs to operate an IRB Approaches program but, as a result of the current capital floor, recognize little benefit from a capital perspective. In American Express' experience, the IRB Approaches generate capital requirements that are misaligned with the risk performance of our portfolios. Therefore, the need for the IRB Approaches is not apparent and American Express supports moving to a singular, standardized approach that is adjusted to avoid disproportionately impacting credit card issuers like American Express. Utilizing only the standardized approach would support the Committee's goals to reduce complexity and variability⁴ across banks' regulatory capital regimes more effectively than maintaining the IRB Approaches (even if adjusted as proposed).⁵ Furthermore, in the U.S., the Federal Reserve operates the Comprehensive Capital Adequacy Review ("CCAR"), a capital planning and stress testing exercise that assesses capital adequacy under several supervisory and company-developed macroeconomic scenarios. CCAR includes forward-looking projections of potential losses and revenues based on the bank's portfolio and circumstances, together with a review of the firm's capital planning process. This combination of the standardized approach and CCAR in the U.S., or similar supervisory exercises in other countries, should enhance comparability and ensure that banking organizations maintain sufficient levels regulatory capital even under highly stressful conditions.

III. Adjustments to the Consultation

As set forth above, American Express urges the elimination of the IRB Approaches. To the extent IRB Approaches remain in place in certain markets, American Express urges the Committee to make several important enhancements, in order to better reflect credit risk for credit card businesses, including developing new asset classifications, recalibrating correlation factors and appropriately adjusting the Credit Conversion Factor ("CCF") for use within the IRB Approaches.

⁴ Consultation at 1.

⁵ Eliminating the IRB Approaches would also be consistent with the Committee's efforts to rescind the Advanced Measurement Approach ("AMA") for measuring operational risk capital requirements from the Basel framework.

A. Asset Classifications and Correlation Factors

American Express urges the Committee to ensure that the IRB Approaches provide appropriate exposure classifications for covered banks' portfolios. For example, the risk profile of charge cards, a paid-in-full retail product, does not align with any of the existing categories and the IRB Approaches' asset classifications appear to have been developed without due consideration for charge card products. As a result, a new category designed for these exposures (across product and customer segments) would enhance the IRB Approaches' risk sensitivity and facilitate closer alignment of risk and capital requirements. However, if the Committee determines not to create a new category, it should alternatively ensure that charge card exposures to corporations, small businesses and consumers (regardless of exposure size) should all be classified as Qualifying Revolving Retail Exposures ("QRRE").

In order to appropriately reflect the risk profile of the broad set of institutions currently subject to the IRB Approaches, the BCBS should also conduct a comprehensive Qualitative Impact Study ("QIS") and use those publicly-disclosed results to recalibrate existing correlation factors. The current Asset Value Correlations ("AVCs"), particularly those applicable to credit cards, are disconnected from American Express' historical loss patterns or the risk performance of our portfolio. In order to better reflect the experience of smaller firms subject to this capital framework, such as American Express, we urge the Committee to conduct a robust QIS and gather data from a representative set of firms. Using the results of this study, the BCBS should then appropriately revise the IRB Approaches' correlation factors for retail and wholesale exposures.

B. Transactors and Revolvers

American Express fully supports the Consultation's recognition of the distinction between "transactor" and "revolver" customer segments. Credit card transactors generally pay either in full or a large portion of the balance each month, whereas revolvers routinely carry a balance on their account. Based on our experience, transactors have demonstrated lower credit risk than revolvers over time. This more favorable risk profile is reflected in the lower Probability of Default ("PD") floor proposed in the Consultation. American Express supports recognition of the different risk profile of these customers and urges the Committee to expand this distinction within the IRB Approaches by creating separate asset categories (both retail and wholesale) and correlation factors for transactors and revolvers. We also believe that the Committee should carry this distinction forward into other aspects of the BCBS capital framework, including the creation of distinct and appropriate risk weights for transactors and revolvers under the standardized approach.

In order for the Committee's distinction between transactors and revolvers to be effective, it is critical to define those classifications appropriately. The Consultation provides that such segment includes only those customers tenured for at least six months where the balance has always been repaid at each scheduled repayment date.⁶ American Express believes that such a narrow definition is unnecessary in order to capture the set of customers with the targeted risk profile. This "lifetime" definition would not allow any occasional or even unintentional revolving activities and, in practice, would exclude many customers with transactor-like behavior and risk profile. An alternative definition that includes customers who have on average paid a substantial portion of their total statement balance by its due date for each of the past 12 months would be a more appropriate means to distinguish between transactors and revolvers, as the customers satisfying these criteria maintain a similar risk profile to those that would qualify under the proposed definition. In addition to payment history, transactors should also include exposures related to charge card products which contractually require payment in full by the next repayment date.

C. Commitment

The Consultation also introduces a new definition of the term *commitment* for both the IRB Approaches and standardized approaches, which includes "any contractual arrangement that has been offered by the bank and accepted by the client to extend credit, purchase assets or issue credit substitutes."⁷ In proposing this definition, the Committee explains that "some banks currently treat facilities that are unconditionally cancellable as not being a commitment and thus deem them to fall outside the scope of the capital framework."⁸ American Express includes UCCs as a driver in its Exposure at Default ("EAD") measures under the IRB Approaches and believes it would be appropriate to ensure that other banks also include such commitments in their EAD measures, in order to improve comparability across firms' IRB Approaches capital outcomes. To further improve consistency, American Express urges the BCBS to clarify the definition of *commitment* by specifying that covered contractual arrangements include stated contractual amounts. American Express also believes that the Committee should carefully review the potential impacts of adopting a new definition in the standardized approaches before incorporating the definition into that framework.

⁶ Consultation at 6.

⁷ Consultation at 11.

⁸ Id.

D. EAD Floor

The Consultation also proposes to introduce a parameter floor for the EAD measure based, in part, on the standardized approach's CCF for off-balance sheet exposures. As described more fully in American Express' comments⁹ to the BCBS' recent proposal to revise the standardized approach for credit risk,¹⁰ the proposed revisions set forth in that proposal would inappropriately increase the CCF for unused and unconditionally cancellable off-balance sheet exposures of banks that issue credit cards. With the current proposal directly linking the CCF used for standardized approach to the IRB Approaches, we urge the BCBS to conduct an additional QIS and review any additional data before applying any changes to the CCF that would result in misalignment of risk and capital requirement as it applies to credit cards under both the standardized approach and the IRB Approaches.

E. Excluded Portfolios

The Consultation provides that the low-default nature of certain portfolios and the resulting "lack of appropriate data for risk parameter estimation"¹¹ contributed to variation in modeling results across banks. As a result, the Committee proposes to remove the IRB Approaches for exposures to banks, financial institutions and large corporations. If the BCBS ultimately determines to use the standardized approach for those exposures, American Express urges the Committee to adopt an appropriate risk weight for such exposures. As explained in the Consultation, these exposures have default rates so low that banks do not have sufficient data on which to adequately model their risk. Therefore, a relatively low risk weight (20% or lower) would be appropriate and better align capital with risk.

Separately, American Express submits that any requirement to capture additional information such as consolidated assets or revenue for the purpose of identifying large corporations should be limited to publicly traded entities for which audited financial data is more readily available. Such an approach would avoid unnecessary cost and burden for covered banks in sourcing information on privately-held enterprises. For jurisdictions where the F-IRB approach is not used, American Express also urges the Committee to

⁹ American Express' submitted comments to the BCBS' Second Consultative Document: Revisions to the Standardised Approach for credit risk, *available at* <http://www.bis.org/bcbs/publ/comments/d347/americanexpress.pdf>

¹⁰ BCBS Second Consultative Document: Revisions to the Standardised Approach for credit risk (Dec. 2015), *available at* <http://www.bis.org/bcbs/publ/d347.pdf>

¹¹ Consultation at 2.

clarify which alternative would be adopted for corporations with less than EUR50 billion in total assets but more than EUR200 million in annual revenues. Additionally, American Express supports trade association comments supporting national discretion to provide a lower risk-weight for banking organizations that have non-significant equity exposures.¹²

IV. Cumulative Impact and Calibration Period

American Express urges the BCBS to consider the impact of the Consultation in combination with other recently proposed revisions to the capital framework. We strongly urge the BCBS to consider the cumulative impact of all recently proposed changes across the BCBS capital framework in any QIS exercise and in the finalization of this Consultation. Furthermore, we also believe that the Committee should conduct a comprehensive calibration period, in order to ensure that the resulting framework generates appropriate capital outcomes.

V. Conclusion

American Express appreciates the BCBS' confirmation that local regulators maintain discretion to utilize the standardized approaches only and, additionally, consideration of the various enhancements to the capital framework proposals as discussed in this letter.

¹² See The Clearing House Association L.L.C., the Securities Industry & Financial Markets Association and the Financial Services Roundtable comments to the BCBS' Second Consultative Document: Revisions to the Standardised Approach for credit risk, *available at* <https://www.theclearinghouse.org/issues/articles/2016/03/20160316-tch-comments-to-basel-committee-on-standardized-approach-to-credit-risk>

Basel Committee on Banking Supervision
June 24, 2016

Thank you for considering our comment letter. We appreciate the opportunity to share our views with the BCBS. If we may be of further assistance, please contact Richard Petrino at Richard.Petrino@aexp.com and +1-212-640-5516.

Sincerely,

A handwritten signature in dark ink, appearing to read "Jeff Campbell", is positioned above the printed name.

Jeffrey Campbell
Executive Vice President &
Chief Financial Officer

cc: Andres Espinosa
Paul Fabara
Ashwini Gupta
Anderson Lee
Vernon Marshall
Juliana O'Reilly
Richard Petrino
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