



**International
Banking Federation**

Pinners Hall
105-108 Old Broad Street
London EC2N 1EX

tel: + 44 (0)20 7216 8947
fax: + 44 (2)20 7216 8928
web: www.ibfed.org

Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland
baselcommittee@bis.org

February 12, 2016

Dear Sir/Madam:

Re: *IBFed Response to Basel Consultation on TLAC Holdings*

The International Banking Federation (IBFed) is supportive of the purposes of the FSB's Total Loss Absorbing Capacity (TLAC) standard, to ensure that sufficient resources exist to safely resolve all covered banks, without impacting critical functions or using taxpayer funds. The FSB's TLAC framework should be implemented consistently across jurisdictions to realise the benefits for cooperation and stability envisaged by the FSB while also ensuring a level playing field for G-SIBs in terms of their respective TLAC. The framework when implemented needs to be mindful of the market depth and funding capacity of investors to allow banks to fulfil the requirements at a sustainable cost. We note that the potential application of the standard beyond Global Systemically Important Banks (G-SIBs) to other banks would further exacerbate the pressures for banks to fund TLAC eligible instruments in markets.

We support the intention of the Consultative Document to establish a framework that mitigates the risk of contagion with a view to ending the 'Too Big to Fail' problem. Thus, while in principle we understand the Basel Committee's aim to limit the cross-holdings of TLAC from other banks, we also consider it essential that some allowances should be made for market making activities, if TLAC is to benefit from a liquid market. Restrictions on holdings of TLAC therefore should not be more severe than those already in place under the Basel framework of deductions for capital instruments or under large exposure rules. We also believe that a separate and distinct limit for TLAC holdings will be important to ensure market liquidity for these instruments.

With regard to the Basel Consultation on TLAC Holdings, the IBFed therefore wishes to express the following comments.

Mitigating and balancing the Risk of Contagion

Whilst we agree that the effects of contagion must be limited as far as is possible, it must be noted that excessive TLAC requirements themselves can create contagion risks in the market, as it is self-evident that if TLAC is bailed-in, TLAC-holders will bear the losses. Hence, excessive TLAC requirements will shift risk in significant degree elsewhere in the financial system.

Given that Tier 1 and Tier 2 holdings are already subject to a deductions regime, which is rightly not proposed to be amended, this proposal in reality deals only with TLAC-eligible instruments that are not Tier 1 or Tier 2. Such TLAC-eligible debt instruments rank senior to capital instruments, and provide the basis for recapitalisation efforts involved in addressing a troubled bank. They carry therefore less credit risk than capital instruments, and this should be taken into account in the proposal. If and when converted, these instruments will have to be deducted from the CET1 of the holder of the instrument in accordance with the existing Basel III deduction approach.

The approach taken, of deducting TLAC holdings from Tier 2 instruments, will have the effect of making investment in TLAC-eligible debt instruments economically unviable for the banking sector. Whilst focused on the narrow aim of preventing contagion from a failing bank to other banks, it will also shift and perhaps concentrate risk in the non-bank sector.

Corresponding deduction approach

We believe that requiring a deduction from Tier 2 for TLAC holdings is very onerous and will not only misalign incentives but will also reduce the liquidity of TLAC-eligible liabilities and lead to an over-concentration of TLAC holdings in non-bank sectors. This impact will be particularly challenging at the time of regulatory implementation since banks will likely not be investors in TLAC instruments and the depth of this market will subsequently be diminished. Since a large amount of new issuance is required over the coming years to enable G-SIBs to meet the TLAC requirements, this reduced demand will create a challenging environment for G-SIBs. G-SIBs could also find these restrictions reduce their ability to raise TLAC in a stressed environment.

This treatment also seems particularly harsh when compared to the Basel III framework where financial institutions holding capital instruments of other financial institutions must make a like-for-like deduction, subtracting holdings of the other banks' Tier 1 capital instruments from their own Tier 1 capital, and holdings of Tier 2 from Tier 2. We believe that TLAC should follow the corresponding deduction approach as established in Basel III. This has been proven to be an effective approach for Basel III capital instruments, and would ensure further consistency with the Basel framework. The corresponding deduction approach can be applied consistently to G-SIBs and those that have domestic TLAC requirements.

Large exposures for non-G-SIBs

Generally, for non-G-SIBs not subject to a requirement to maintain additional liabilities which can be subject to loss in a resolution, such as via bail-in, we recommend applying the Basel Committee's large exposure framework rather than the Tier 2 deduction approach for TLAC holdings. This would help to address the concern that would arise should the G-SIBs be allowed a like-for-like deduction while non-G-SIBs would be left with a Tier 2 deduction in the absence of any TLAC. In addition, we do not share the concerns outlined in Section 3.4 about the complexity caused by application of a different treatment to G-SIBs and non-G-SIBs, but view this as an appropriate and simple solution.

Deduction Threshold

As mentioned above, market making is a very important function for many banks and it has broad systemic benefits. If a deduction approach is retained and the current threshold for equity instruments is simply considered to include TLAC holdings, we do not believe that it will be sufficient to permit market making activities. We suggest that, in addition to the

current 10% of common equity threshold, another 10% threshold specific to investments in TLAC instruments be set up to ensure an active and deep market for such TLAC instruments. We believe this is necessary to preserve banks' function as an intermediary, ensuring market liquidity for senior unsecured funding. An additional standalone threshold specific to investments in TLAC instruments would limit the amount of TLAC instruments that banks can invest in, while not inadvertently creating greater capacity for banks to invest in the capital instruments of other financial institutions, and the systemic risk that this may create.

Definition of a TLAC holding

Instruments subordinated to Excluded Liabilities

Asymmetric treatment, i.e. broadening the definition of "TLAC holdings" to cover instruments that are not or no longer TLAC-eligible for the issuer, is inappropriate, in our view and works against the system generating sufficient TLAC volume. The definition should, in principle, be identical with the TLAC eligibility criteria, i.e. in particular, all instruments that, for example, do not or no longer fulfil the criteria under Section 9 of the TLAC term sheet (e.g. residual maturity of less than 1 year) should not be included in the TLAC holding. All positions that are not TLAC-eligible should be consistently recognised as part of risk-weighted assets.

Instruments ranking pari passu to Excluded Liabilities

We believe the proposed approach will likely have implications for the existing senior market. It would be extremely challenging from an operational perspective to identify the senior unsecured instruments with the 2.5-3.5% allowance from the rest of the senior unsecured instruments. The likely consequence is that the investors will have to deduct all of the senior unsecured instruments. To avoid the likely negative consequence for the existing senior market, we recommend that these instruments not be subjected to the deduction approach, but be subject to the large exposure limits.

Respecting local market access and investor capacities

It is critical from the perspective of stabilising the global financial system to enable G-SIBs to issue the necessary volume of TLAC-eligible liabilities. In light of differences across jurisdictions in terms of capital market participants and investors in debt issued by banks, and also in order to ensure smooth issuance of TLAC instruments in the markets, flexibility should be permitted so each jurisdiction could take into account their debt capital market conditions.

Evidence from the QIS and phasing-in of TLAC Holding requirements

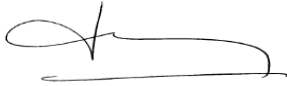
The results of the QIS should be interpreted very cautiously. The study itself says at various points that not all the data delivered could be used and that certain information was missing. Generally speaking, this also raises the question of whether the QIS as a whole uniformly draws on a consistent set of data (e.g. did all banks really include TLAC holdings with a residual maturity of less than 1 year?).

Considering the potential impact of this proposal on the market and the operational difficulties of identifying TLAC holdings, especially with the wide scope being proposed by the Basel Committee when defining TLAC holdings, we recommend a phase-in approach. While TLAC and the disclosure rules enter into force in 2019, the deduction regime should only come into force in 2022.

Finally, if non G-SIBs are in the scope of deductions, as opposed to our proposal, there should be a detailed QIS and impact survey. As only G-SIBs were in the scope of the FSB work on TLAC, it is important to ensure that limiting the investments in TLAC by non-G-SIBs not raise additional issues.

We thank you for taking our comments into consideration, and we look forward to future discussions on these issues.

Yours sincerely,



Ms. Hedwige Nuyens
Managing Director
IBFed



Ms. Debbie Crossman
Chair Prudential Supervision WG
IBFed