September 11, 2015

Electronically Submitted

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

Re: Consultative Document – Interest Rate Risk in the Banking Book

Ladies and Gentlemen:

We appreciate the opportunity to provide comments to the Basel Committee on Banking Supervision (the “Basel Committee”) in response to the consultative document on “Interest Rate Risk in the Banking Book” (the “Proposal”). Due to the importance of this topic, we are filing this comment letter to highlight our significant concerns with several aspects of the Proposal and to express our support for positions set forth in the comment letters filed by the American Bankers Association; The Clearing House Association L.L.C., the Securities Industry and Financial Markets Association, and the Financial Services Roundtable; and the Institute of International Finance, the International Banking Federation, the Global Financial Markets Association, and the International Swaps and Derivatives Association (collectively, the “Trade Association Letters”).

We support the stated goal of the Basel Committee and agree that banking organizations must ensure appropriate identification, measurement, monitoring, and control of interest rate risk in the banking book (“IRRBB”), including ensuring that adequate capital exists to “cover potential losses from exposures to changes in interest rates.” We strongly oppose, however, the introduction of a mandatory Pillar 1 approach to IRRBB. As discussed in more detail in the Trade Association Letters, given its simplified and standardized nature to accommodate a global application, the proposed Pillar 1 approach to measuring IRRBB is fundamentally flawed. First, there is a serious measurement issue with IRRBB due to the lack of a well-defined standard to determine the level of real loss to a banking organization’s capital as a result of a reduction in either

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1 Each of the undersigned institutions is a U.S. bank holding company with total consolidated assets between approximately $80 billion and $420 billion, as of June 30, 2015. Our institutions are traditional banking organizations, focused on domestic business activities, whose sizes are modest in relation to both the U.S. banking sector and U.S. economic activity. For example, each of the undersigned, as of June 30, 2015, had national deposit shares under 3% and total consolidated assets that represented less than 3% of U.S. gross domestic product, and in the aggregate, had less assets than the single largest U.S.-based globally systemically important bank (“U.S. G-SIB”) identified by the Financial Stability Board.

the economic value of equity ("EVE") or net interest income ("NII"). Secondly, a "one-size-fits-all" measurement would provide an inaccurate assessment of IRRBB due to the diversity of banking models and products across countries and markets, and even within individual jurisdictions. For example, our institutions have significantly different business models than the U.S. G-SIBs. In light of the flaws of a standardized measurement for interest rate risk, importing a standardized calculation and disclosure framework into Pillar 2 would effectively have the same impact as introducing a standardized Pillar 1 approach and would not provide an accurate or meaningful representation of any individual banking organization’s interest rate risk. Accordingly, a standardized Pillar 1 approach would not only result in an interest rate capital charge that is misaligned with actual risk, but also would risk creating confusion in the markets. For these reasons, as supplemented by the discussion in the Trade Association Letters, we urge the Basel Committee to (1) forego adopting a mandatory Pillar 1 approach for IRRBB, instead allowing national regulators to apply a robust Pillar 2 approach to address interest rate risk; and (2) exclude any standardized calculation of IRRBB and related disclosures from the Pillar 2 framework of the Proposal.

To achieve the goals of the Basel Committee, we would recommend enhancements to the Pillar 2 framework, including requiring banking organizations to report to national supervisors the results of internally-modeled IRRBB measures under interest rate shock scenarios defined by national supervisors. Supervisors could tailor such scenarios to specific institutions or groups of institutions, thus providing banking organizations the necessary flexibility to evaluate their sensitivity to IRRBB using an EVE or NII framework (or both), based on characteristics that would best suit their portfolios. The Basel Committee could establish principles for national supervisors to follow in developing jurisdiction-specific scenarios.

The Trade Association Letters discuss our concerns with the proposed Pillar 1 and Pillar 2 approaches in additional detail. However, we believe it is important to emphasize the following points, which are of particular interest to U.S. regional banking organizations.

With respect to the Pillar 1 approach:

- The manner in which the Proposal would establish a Pillar 1 surcharge is fundamentally flawed, including, for example, by (a) capitalizing for fluctuations in future earnings, which would impose a capital charge on the loss of an opportunity for higher earnings, even when the underlying earnings stream remains positive; and (b) implementing an earnings-at-risk measure assuming a static balance sheet with standardized run-off scenarios, rather than a dynamic balance sheet, incorporating rate risk impact of new volumes and balance sheet convexity.

- A one-size-fits-all approach would not reflect each banking organization’s risk management framework or actual interest rate risk. Each banking organization effectively would be required to manage IRRBB under its internal risk management frameworks and a standardized Pillar 1
approach that would not accurately reflect its actual interest rate risk. The resulting obligation could incent banking organizations to manage risk to the standardized approach and the related capital surcharge, even when doing so may increase their actual interest rate risk exposure.

- The standardized calculation contains serious analytical and practical shortcomings, in particular with respect to non-maturity deposits ("NMDs"), which have diverse characteristics and interest rate risk profiles.

- U.S. banking organizations have empirical models to estimate balance and rate behavior of NMDs for interest rate risk measurements. These models are calibrated with each banking organization's internal historical data and reflect characteristics specific to the products offered by the institution, behavioral characteristics of its customers, pricing strategy, competitive factors in its footprint, the interest rate environment, and lending opportunities. These models are independently validated and monitored by an independent second line of defense. U.S. banking supervisors review closely these deposit models in the context of interest rate risk measurement, stress testing, and capital adequacy. Given its simplified and standardized nature to accommodate a global application, a Pillar 1 standardized approach will not reflect each banking organization's specific deposit portfolio characteristics (let alone different deposit products across different jurisdictions and markets) or actual levels of interest rate risk.

- The proposed standardized treatment of NMDs, which constrains the pass-through rate, stability, maturity, and weighted average life ("WAL") parameters, is far too restrictive and does not enable a realistic representation of the interest rate sensitivity of deposits. In particular, transactional accounts characterized as demand deposit accounts in the United States are often non-interest bearing. Accordingly, the pass-through rate is by definition 0%; the Proposal, however, imposes a 25% pass-through floor for transactional accounts. The standardized global WAL assumptions also are capped effectively at 2.4 years for retail transactional and 2.1 years for retail non-transactional accounts. U.S. banking organizations have internal models to estimate WAL assumptions based on their own product characteristics and other relevant factors noted above, which can result in significantly different outcomes from the one-size-fits-all WAL caps and stability floors.

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3 Based on the 80% stability cap and WAL cap for transactional deposits (80% x 3 years = 2.4 years) and 70% stability cap and WAL cap for non-transactional deposits (70% x 3 years = 2.1 years) in the Proposal.
in the Proposal. We expect that the combination of pass-through rate, stability, and WAL floors/caps would result in significant misestimate of over five-years of duration of equity.

- For retail NMDs, the proposed static NII approach without consideration of future deposit volumes would significantly misestimate the interest rate risk because new NMDs do not come on the books at the prevailing market rates (i.e., NMDs do not reprice 100% with market rates). The proposed approach mistakenly reprices all new deposits (beyond the balance attrition from its economic-value-of-equity framework) at full market rates. Additionally, the static nature of cash flows in the proposed NII approach fails to capture any convexity in the balance sheet.

With respect to the Pillar 2 approach:

- While we support a robust Pillar 2 approach to addressing IRRBB, any final Pillar 2 approach should not require banking organizations to model and disclose IRRBB based on a standardized measure. As discussed above, such an approach would necessarily result in the inaccurate estimation of IRRBB due to the variations in the markets, customer profiles, and products of banking organizations across and within jurisdictions, and would risk creating confusion in the markets.

- Whereas disclosure of a standardized calculation of IRRBB presents the same fundamental concerns as a standardized Pillar 1 approach, there may be value in reporting EVE and/or NII sensitivity results to national supervisors under standardized rate and curve scenarios determined by national authorities in each jurisdiction.

- While there may be opportunities to enhance public disclosures of interest rate risk, it is important that any such disclosure requirements not force banking organizations to disclose sensitive, confidential, or proprietary business information. The disclosure requirements in the Proposal’s Pillar 2 approach would require banking organizations to disclose confidential and proprietary business information. Banking organizations spend significant time and resources developing the key assumptions underlying their interest rate risk models. These assumptions reflect the unique characteristics of each banking organization’s products and customers. Accordingly, disclosure of those assumptions would cause banking organizations to reveal proprietary information to competitors, in particular deposit pricing assumptions.

- We oppose the inclusion of any required standardized outlier test. We acknowledge the usefulness of an outlier test for jurisdictions with less robust supervisory processes. However, we believe that U.S. regulators already have all the information and expertise needed to monitor interest
rate risk at internationally active U.S. banking organizations. The outlier test is therefore simply unnecessary in jurisdictions with a strong supervisory approach. As a result, the Basel Committee should encourage national regulators to develop local outlier tests as needed.

- There are a number of basic foundational approaches to measuring capital for interest rate risk. Each one has benefits and drawbacks. Specifying any approach (whether EVE and/or NII) is inappropriate.

- Any final standard should not require a banking organization to incorporate credit spread risk in the banking book into its IRRBB models. This concept is not adequately developed in the Proposal. The characterization and assessment of this risk should be determined by national supervisors in each banking organization’s home country.

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We continue to support robust interest rate risk management and strong supervisory oversight of the same through evaluation of both a banking organization’s interest rate risk management processes and its capital adequacy. We appreciate the opportunity to provide these comments to the Basel Committee and respectfully ask for consideration of the recommendations and suggestions in this letter and in the Trade Association Letters.

If you have any questions regarding the content of this letter or would like more information, please do not hesitate to contact any of the individuals listed in Attachment 1 appended hereto.

Sincerely,

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