Bank of America

Legal Department

October 25, 2010

BY ELECTRONIC MAIL

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 1-5
Washington, DC 20219
Docket Number OCC-2010-0016
RIN 1557-AD35

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Docket No. R-1391
RIN 7100-AD53

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
RIN 3064-AD62

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attention: OTS-2010-0027
RIN 1550-AC43

Re: Advance Notice of Proposed Rulemaking Regarding Alternatives to the Use of Credit Ratings in the Risk-Based Capital Guidelines of the Federal Banking Agencies

Dear Messrs. and Mmes.:

Bank of America Corporation (together with its affiliates, ("Bank of America") appreciates the opportunity to comment on the advance notice of proposed rulemaking issued by the federal banking agencies ("Agencies") regarding alternatives to the use of Credit Ratings in the Risk Based Capital Guidelines (the "ANPR"). 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.

Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act[1] (the "Dodd-Frank Act") requires removal of any reference to, or requirement of reliance on, credit ratings from all of the Agencies' rules, including the capital rules cited in the ANPR. Bank of America appreciates the

[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 (2010).

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congressional concerns regarding the accuracy of some of the ratings issued by Nationally Recognized Statistical Rating Organizations ("NRSROs"). At the outset, we wish to emphasize that we agree with the goal of reducing overreliance on credit ratings. However, Bank of America's overarching observation is that Section 939A is too broad and that in attempting to address acknowledged weaknesses, it creates issues where they had not previously existed. While we recognize inadequacies in the issuance and use of credit ratings contributed to recent financial difficulties, we believe this problem was most prevalent in the area of structured securitizations and more specifically the residential mortgage product. In other asset classes, the NRSRO ratings were not a significant contributor to the credit related issues experienced. In our view a broad scale deletion of credit ratings in all risk based capital guidelines is unwarranted.

Moreover, we believe other provisions of the Dodd-Frank Act and changes in industry practice are responsive to the identified problems.

- Specifically, Section 932 of the Dodd-Frank Act requires the NRSROs to provide more extensive and enhanced disclosure of their methodologies and to take actions to mitigate potential conflicts of interest.
- In addition, the Securities and Exchange Commission ("SEC") is required to establish an Office of Credit Ratings to protect users of credit ratings, promote accuracy in ratings, and ensure that ratings are not impacted by conflicts of interest.
- Section 939F of the Dodd-Frank Act allows the SEC to impose a new government-dictated approach to selecting NRSROs. Exercising this option could promote the development of a subscriber-paid rating agency model.
- Section 933 of the Dodd-Frank Act extends liability for private securities fraud actions to NRSROs under Section 15E of the Securities Exchange Act of 1934, creating a private right of action for securities law violations.
- Beyond the regulatory changes, NRSROs are adopting new corporate governance procedures, enhanced controls for managing potential conflicts of interest, and new analytical tools.[2]

These new legal, regulatory and market disciplines have yet to be tested. We believe these safeguards should be given time to prove their efficacy. Section 939A prematurely concludes these safeguards will prove insufficient. In doing so, Section 939A unnecessarily and unintentionally results in increased risk, cost and burden.

Abandoning the use of credit ratings in the capital rules adopted by US regulators would have negative implications for the adoption of the internationally agreed upon Basel II and Basel III standards and will lead to competitive distortions across the international banking industry. It would also send the wrong signal to the other Basel member countries about the willingness of the US to adhere to internationally agreed standards. As evidence, the European Parliament has taken note of the concerns raised by Section 939A, stating they are:

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[2] See, e.g., www.standardandpoors.com/about-sp/leadership-actions.

> "very much concerned that limitations laid down in various national laws adopted in response to the crisis (in particular in the US Wall Street Reform and Consumer Protection Act, limiting recognition of external ratings) would result in a serious fragmentation of the application of this global standard."[3]

In light of these factors, we encourage the Agencies to seek a legislative amendment that would substantially modify Section 939A of the Dodd-Frank Act. Bank of America's position is consistent with those expressed by Acting Comptroller of the Currency, John Walsh. In his prepared testimony before the Senate Committee on Banking, Housing, and Urban Affairs on September 30, 2010, Acting Comptroller Walsh observed:

> "[T]he prohibition against references to ratings in regulations under section 939A goes further than is reasonably necessary to respond to [concerns that credit ratings contributed to the financial crisis]. Rather than disregard credit ratings, it may be more appropriate to assess their strengths and weaknesses and to supplement ratings with additional analysis in appropriate cases. We suggest that section 939A be amended to direct regulators to require that ratings-based determinations be confirmed by additional risk analysis in circumstances where ratings are likely to present an incomplete picture of the risk presented to an institution, or where those risks are heightened due to concentrations of particular asset classes."[4]

Potential Risks

Absent the law's repeal or modification, we recognize the Agencies must remove all references to NRSRO from all regulations, including those with regulatory capital impact. We have conducted a high level assessment of the impact of this change on our ability to calculate regulatory capital under Basel II. Bank of America has a well established internal risk ratings process, but there are a large number of areas where we are heavily reliant upon external credit ratings. Examples include municipal and corporate bonds, securitizations, investment securities, and even the inclusion of insurance benefits for operational risk. Bank of America's internal risk rating processes for Sovereign, Bank, and Corporate exposures are well established and would be minimally impacted by Section 939A. However, we have noted several potential risks as highlighted below.

US Regulatory Capital Inconsistent with International Rules

The wholesale deletion of NRSRO references mandated in the Dodd-Frank Act is at variance with other national regimes. Elimination of NRSRO references would create a disparity between the applicable US capital requirements and various Basel capital approaches. This lack of uniformity would reduce the competitiveness for US institutions, especially those operating under the advanced approaches.

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[3] *European Parliament Resolution of 7 October 2010 on Basel II and Revision of the Capital Requirements Directives* (CRD 4), paragraph 11 (2010/2074 (INI)).

[4] John Walsh, *testimony before the United States Senate Committee on Banking, Housing, and Urban Affairs* (Sept. 30, 2010), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=bfae9142-8caf-465d-b473-a04fecd13f3a.

Lack of Risk Sensitivity

We acknowledge the Congressional interest in eliminating approaches that rely exclusively on NRSRO ratings for securitizations. However, several of the ANPR proposals suggest a return to risk insensitive approaches that resulted in capital arbitrage. This is particularly true for Securitizations where proposals suggest a return to pre-recourse rule approaches that proved inadequate for securitization exposures a decade ago. Bank of America does not believe regression to a risk-insensitive general risk based capital regulations is a viable alternative. In our view, this is inconsistent with capital framework that international banking supervisors have been promulgating for over a decade.

Concentration Risk

The inability to rely upon external ratings for public securities could lead to a contraction of the types of investment securities banks would be willing to purchase. Banks would logically conduct the credit analysis on the largest issuers, such as Fannie Mae and Freddie Mac. The burden and cost of conducting such analysis on individual corporate or non-US government issuers, including states and municipalities, may not be worthwhile. This could result in a narrowing of the practical field of eligible investment securities that banks will purchase.

This contraction has two negative market consequences. Greater concentrations of risk in bank portfolios and less diversity of issuers could result in banks being more susceptible to market disruptions. Additionally, the availability of a strong market for the issuance of debt securities by a deep and diverse mix of corporations, municipalities and foreign sovereigns may be curtailed. Banks are key market participants and purchasers of investment securities and it would have negative and unintended repercussions on credit availability for smaller issuers and liquidity of those securities if bank investors become more limited.

Guiding Principles

Several guiding principles are outlined below that should be actively considered in any changes made to the regulatory capital rules.

Changes should align with the goal of an internationally consistent, risk sensitive framework

Rather than making unilateral changes mandated by Section 939A, ultimate resolution should be coordinated with the Basel Committee. On October 20, 2010, the Financial Stability Board (FSB) endorsed principles to reduce authorities' and financial institutions' reliance on NRSRO ratings. [55] The language in the FSB release suggested replacing references to NRSRO ratings in laws and regulations, wherever possible, with suitable alternative standards of creditworthiness assessment. In addition, the FSB expects that banks, market participants and institutional investors will make their own credit assessments, and not rely solely or mechanistically on NRSRO ratings. The FSB comments are more nuanced than Section 939A, suggesting an application more consistent with the Acting Comptroller Walsh's comments referenced previously. We acknowledge that completion of other regulatory

[5] Financial Stability Board October 20, 2010 press release www.financialstabilityboard.org/press/pr_101020.pdf

guidance is dependent upon a satisfactory resolution of this issue and appreciate the urgency in crafting a workable solution. However, failure to synchronize with the international regulatory capital guidance, will negatively impact US banks. The need for consistency counterbalances the desire for urgency.

All relevant inputs, including NRSRO ratings, should be considered in the Internal Credit Assessment

While Section 939A requires the Agencies to remove references to NRSROs in their regulations, we do not interpret it as prohibiting banks from using third-party inputs. We believe prudent risk management practices should consider all relevant inputs in making risk determinations.

Long-standing industry experience has determined NRSRO ratings remain one of the most replicable, transparent, timely, and efficient methods of assessing credit risk for many asset classes. This solid history is what led to the inclusion of the NRSRO ratings in the regulations in the first place. But deletion from the regulation is not equivalent to having them no longer be a viable consideration in the determination of credit worthiness for select asset classes.

Framework should allow for diversity of alternative approaches appropriate for risks and capabilities of each bank

While we agree with the Agencies that any alternative should not be overly complex, in our view simplicity should not come at the expense of a sound risk rating process. We believe there should be room for diversity of alternatives based on the size, sophistication and capability of the bank that owns the exposure. The key focus of any approach should be ensuring all banks have sufficient information, conduct sufficient diligence, and understand the risk of their exposures.

Currently, regulatory capital rules ranging from 1996 Market Risk Amendment through Basel II are significantly different dependent upon the size of the bank. Those differences will increase with implementation of Basel III. So rather than focusing on consistency of treatment for all banks, the Agencies should ensure each population is held to a reasonable standard appropriate for their size and level of sophistication.

Implementation should include grandfathering and a delayed effective date

Bank of America requests the Agencies be mindful of the time and potential burden to implement any associated changes and the potential unintended consequences of market disruptions that could ensue. Whatever approaches are adopted, we believe there should be adequate phase-in periods and grandfathering to avoid abrupt and potentially destabilizing changes and to provide banks the necessary time to make system changes.

We recommend a delayed effective date following issuance of a final rule in order to give ample time for banks to conform their practices to the new requirements. While the challenges of the implementation are difficult to anticipate, the implementation timeline should be no less than one year.

Suggested Approach

The significant majority of credit rating assessments conducted by Bank of America do not incorporate NRSRO input. However, Bank of America believes banks should be allowed to consider all relevant third-party analytics, including NRSRO ratings, as part of well-founded, disciplined credit-risk assessment. Banks should supplement NRSRO ratings with their own analytics, such as market-based measures for publicly traded firms or financial measures for firms with published financial statements. The sophistication of these analytics should be appropriate to the size and sophistication of the bank and the complexity of its exposures. Banks with complex, structured exposures should be expected to have more sophisticated analytics.

For Securitization exposures we request banks not be required to follow a hierarchy of approaches. Banks should be offered a range of alternatives to include:

1. Adapt the Internal Assessment Approach in Basel II to allow banks to internally rate all securitization exposure for which sufficient information is available.

2. Consistent with the comment above, we suggest banks be granted the flexibility to incorporate third party inputs to determine the risk-based capital charge. While NRSRO inputs could not be the sole input in this analysis, they could be among the inputs considered.

3. The simplified Supervisory Formula Approach ("SFA") referenced in the ANPR may have some applicability. But to improve viability, SFA needs to be broadened to:
   - Improve risk sensitivity, eliminating "cliff risk" and reducing the volume of deductions;
   - For securities and synthetic exposures, simplify current regulatory requirements to derive capital charge as if assets had not been securitized ("KIRB");
   - Differentiate between securities and synthetics that are held for sale ("HFS") vs. those held for investment, subjecting HFS position to a more simplistic KIRB calculation;
   - Expand use of segmentation beyond wholesale assets greater than 1 year, and
   - Improve transparency to support pricing of prospective transactions.

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Bank of America appreciates the opportunity to comment on the proposed regulations, and we thank you for your consideration of our comments.

Sincerely,

Kenneth L. Miller / by Caroline D8m.

Kenneth L. Miller
Deputy General Counsel