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February 19, 2015

The Honorable Janet L. Yellen, Chair
Board of Governors of the Federal Reserve
Federal Reserve Building
20th Street and Constitution Avenue
Washington, D.C. 20551

The Honorable Stanley Fischer, Vice Chair
Board of Governors of the Federal Reserve
Federal Reserve Building
20th Street and Constitution Avenue
Washington, D.C. 20551

The Honorable Daniel K. Tarullo
Board of Governors of the Federal Reserve
Federal Reserve Building
20th Street and Constitution Avenue
Washington, D.C. 20551

The Honorable Jerome H. Powell
Board of Governors of the Federal Reserve
Federal Reserve Building
20th Street and Constitution Avenue
Washington, D.C. 20551

The Honorable Lael Brainard
Board of Governors of the Federal Reserve
Federal Reserve Building
20th Street and Constitution Avenue
Washington, D.C. 20551

Re: U.S. Federal Income Tax Considerations Relating to Forthcoming TLAC Guidance

Dear Ladies and Gentlemen:

I am writing on behalf of the Securities Industry and Financial Markets Association (SIFMA)[1] with respect to the Financial Stability Board's ("**FSB**") November 14, 2014 consultative document setting forth its proposal for total loss absorbency capacity ("**TLAC**") of global systemically important banking groups ("**G-SIBs**"). I understand that the Board of Governors of the Federal Reserve System ("**Federal Reserve**") is planning to issue a notice of proposed rulemaking regarding the TLAC requirements that would apply to U.S. G-SIBs. As described in more detail below, it is important that any United States TLAC rules not include features that create uncertainty with respect to whether TLAC securities are considered debt or equity for U.S. federal income tax purposes.

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

The federal income tax treatment of a security depends on the facts and circumstances regarding the security. Thus, a security that is denominated as debt, and is otherwise treated as debt for non-tax purposes, could be treated as equity for federal income tax purposes if its terms are not consistent with debt characterization. If a TLAC security were not treated as debt for tax purposes, the interest payments on the security would be treated as dividends, and would not be deductible, for federal income tax purposes. This would increase the tax liability of an issuer of TLAC debt securities, thereby increasing the issuer's effective cost of issuing such securities.

Furthermore, interest that is paid by a U.S. issuer on debt that is held by a foreign investor is generally exempt from U.S. withholding tax, while dividends on equity that is held by a foreign investor is generally subject to a U.S. withholding tax. Thus, if a TLAC security structured as debt were treated as equity for tax purposes, foreign investors would generally be subject to increased withholding taxes, which would adversely affect the marketability of such securities to non-US persons. Indeed, even some uncertainty regarding the tax treatment of TLAC debt securities would likely dampen the market for them and increase the issuer's cost of capital, and the associated marketplace confusion regarding the tax reporting and withholding treatment of such securities could impair the placement and trading of the securities. Further, issuers of TLAC could reach different conclusions regarding their US tax treatment as debt or equity and hence add to the confusion in the market place.

We understand that TLAC debt securities are intended to absorb some of the losses of the issuer of the security upon a resolution proceeding with respect to the issuer. At the same time, a hallmark of debt treatment for federal income tax purposes is that the holder has an unconditional right to recover the principal amount of its investment on a fixed date, and risks associated with the operation of the issuer's business are borne first by equity holders. The current provisions for resolution proceedings do not disturb the tax treatment of long-term debt securities, because they generally resemble the proceedings that occur in a bankruptcy. Thus, holders of debt securities may ultimately lose their right to a return of principal if the issuer becomes insolvent, but this (a) does not occur unless and until a formal legal insolvency proceeding has begun, and (b) occurs only to the extent that the assets of the insolvent estate are insufficient to make them whole. This is in contrast to resolution proceedings where holders of TLAC securities might be (a) converted into equity, or forced to accept write-downs, through contractual provisions that operate ahead of, or outside of, a formal legal proceeding, or (b) forced in such a proceeding to participate *pari passu* with equity claimants, through a conversion into equity that occurs notwithstanding that common equity holders have not lost their claims. It is important that the Federal Reserve's rules implementing TLAC for U.S. G-SIBs not change the basic approach to bank-type resolution proceedings in this regard or introduce any new requirements that could create residual uncertainty with respect to the U.S. tax treatment of TLAC debt securities.

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We echo these concerns as applied to any internal TLAC requirements that may be part of proposed rulemaking. For example, as noted in a letter from SIFMA, The Clearing House and several other trade associations dated February 2, 2015, internal TLAC requirements should not empower local regulators in a material subsidiary's host country to convert internal TLAC debt into equity in the absence of a resolution proceeding in the home country of the ultimate parent, because such unilateral conversion could serve to undermine the financial stability that the TLAC approach is designed to ensure. We add to this observation that such empowerment might also create some uncertainty with respect to the characterization of the securities as debt for U.S. tax purposes. Even if the U.S. Treasury were to conclude that such securities were debt for U.S. tax purposes, a conclusion by the home country jurisdiction that such securities were equity for local tax purposes could ultimately force the U.S. to deny interest deductions under the OECD Base Erosion and Profit Shifting Action Plan #2.

SIFMA in any case urges the Federal Reserve to consult with the Treasury Department in developing its guidelines to ensure that TLAC debt securities are clearly treated as debt for federal income tax purposes. In addition, we would urge both the Federal Reserve and the Treasury Department to work with the regulators in other jurisdictions, encouraging them to adopt guidelines that will serve to ensure the uniform tax treatment of TLAC securities in all jurisdictions and to avoid problematic inconsistencies across jurisdictions with respect to either the relevant terms of TLAC securities or the relevant tax rules that govern them.

If you have any questions, please do not hesitate to call me at 202-962-7300 or email me at ppeabody@sifma.org.

Very truly yours,

Payson R. Peabody
Managing Director & Tax Counsel
Securities Industry and Financial Markets Association

Cc: Mark Mazur
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