BANK POLICY INSTITUTE

American Bankers Association

April 1, 2022

*Via Electronic Mail*

Secretary
Securities and Exchange Commission,
100 F Street NE, Washington, DC
20549–1090

Re: Share Repurchase Disclosure Modernization (File No. S7–21–21) and Rule 10b5-1 and Insider Trading (File No. S7–20–21)

To Whom It May Concern:

The Bank Policy Institute[1] and the American Bankers Association[2] (together, the "Associations") appreciate the opportunity to comment on the Securities and Exchange Commission's proposals relating to Share Repurchase Disclosure Modernization (the "Share Repurchase Proposal") and Rule 10b5-1 and Insider Trading (the "10b5-1 Proposal"). The Associations understand the SEC's efforts to provide investors with more meaningful disclosure pertaining to share repurchases and to limit opportunities for inappropriate use of plans designed to benefit from the Rule 10b5-1(c) safe harbor; however, the Associations share the concerns of issuers across industries that, contrary to the SEC's intentions, certain elements of the proposals would disrupt markets, facilitate manipulation and harm investors. The Associations encourage the SEC to accept recommendations to address these concerns.

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1 The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation's small business loans, and are an engine for financial innovation and economic growth.

2 The American Bankers Association is the voice of the nation's $23.7 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $19.7 trillion in deposits and extend more than $11.2 trillion in loans.

In addition to agreeing with those broad concerns, the Associations are further concerned that, due to the interplay between these proposals and the extensive capital and capital planning regulatory requirements already applicable to large bank holding companies and savings and loan holding companies (collectively, "Regulated Banking Institutions"),[3] certain elements of the proposals would adversely and disproportionately impact Regulated Banking Institution issuers and would contradict longstanding U.S. bank regulatory policy to encourage Regulated Banking Institutions to use share repurchases rather than dividend distributions as the preferred mechanism for returning capital to shareholders. For this reason, it is imperative that the SEC consult with the Board of Governors of the Federal Reserve System, which is primarily responsible for administering the capital requirements applicable to Regulated Banking Institutions, prior to finalizing these proposals. Doing so would help to ensure that any securities regulations that might impact the share repurchase practices of Regulated Banking Institutions will harmonize with the important safety, soundness and financial stability policies of the Federal Reserve.

This harmonization is particularly important because, due to the extensive capital and capital planning regulatory framework applicable to Regulated Banking Institutions, and the frequency with which Regulated Banking Institution issuers typically engage in share repurchases, the general concerns cited in the proposals with respect to inappropriate and opportunistic use of share repurchases should not apply in the same way to Regulated Banking Institution issuers. Thus, the benefits of applying the proposals to Regulated Banking Institution issuers would not outweigh the costs.

Part I of this letter details how the 10b5-1 Proposal's cooling off period could make it difficult for a Regulated Banking Institution to execute the share repurchases contemplated by its capital plan. Part II of this letter describes how the new disclosures that would be required under Item 703 of Regulation S-K could require Regulated Banking Institutions to publicly disclose information that is competitively sensitive or confidential supervisory information. Part III of this letter explains how, taken together, the various elements of the proposals could impact Regulated Banking Institutions' share repurchase practices in a way that runs counter to longstanding Federal Reserve policy.

## I. The 10b5-1 Proposal's 30-day cooling off period does not provide the flexibility necessary to engage in prudent capital management and, particularly when combined with the proposed prohibition on multiple overlapping 10b5-1 plans and the daily volume limits of Rule 10b-18, could make it difficult for a Regulated Banking Institution issuer to repurchase the amount of shares reflected in its regulatory capital plan and deemed optimal by its board.

The 10b5-1 Proposal's introduction of a mandatory cooling off period of at least 30 days between adoption or any modification of a Rule 10b5-1 plan and the first trade under the newly adopted or modified plan would significantly reduce the utility of the Rule 10b5-1(c) safe harbor and hamper Regulated Banking Institutions' share repurchase practices. A 30-day delay between setting trade parameters (including pricing) under these plans and executing such trades, combined with the prohibition on overlapping 10b5-1 plans, does not leave sufficient flexibility for a firm to prudently react to any developments—even those that do not involve material nonpublic information ("MNPI")—that may occur during this period. Given this inflexibility, firms may be unwilling—or unable—to use these plans as part of their holistic capital management strategies. In addition, for some Regulated Banking

[3] All bank holding companies and savings and loan holding companies are subject to capital and capital planning requirements. These requirements become more detailed and prescriptive for banking institutions with at least $100 billion in total assets.

Institution issuers, this cooling off period would, in practice, shorten the window within each quarter during which they would be able to execute share repurchases, thereby making it difficult, if not impossible, for them to execute the amount of share repurchases contemplated by their regulatory capital plans and deemed optimal by their boards.

It is already impermissible to adopt or modify 10b5-1 plans or otherwise enter into share repurchase agreements while in possession of MNPI, and firms have robust policies and procedures in place to avoid doing so. For reasons entirely unrelated to possession of MNPI, issuers, including Regulated Banking Institutions, that frequently engage in share repurchases may adopt or update 10b5-1 trading plans (including by terminating existing plans and adopting new ones) several times over the course of a year. Adopting or updating these plans helps maximize shareholder value by allowing issuers to account for general market developments (whether positive or negative), unforeseen circumstances, and issuer performance over the period since the previous 10b5-1 plan adoption or update. In addition, Regulated Banking Institutions constantly manage their regulatory capital ratios to ensure they are meeting regulatory minimums and management targets; therefore, 10b5-1 plan adjustments may help ensure that the Regulated Banking Institution's share repurchases are properly calibrated to support these regulatory capital requirements and goals.

In light of these considerations, it would be highly inefficient, and not in the best interest of shareholders, for an issuer to establish a single 10b5-1 plan and have no ability to adjust it for 30 days without the imposition of yet another 30-day cooling off period. Particularly for Regulated Banking Institutions, whose capital levels are closely scrutinized by both the market and banking regulators, and whose financial stability underpins the stability of the entire financial system, failing to adopt or update 10b5-1 plans to account for the considerations noted above could, in some circumstances, be an unsafe or unsound practice that is inconsistent with bank regulatory requirements.

In addition, Regulated Banking Institution issuers are subject to extensive capital planning requirements that require them to plan out their share repurchases and other capital actions many months ahead.[4] These requirements allow for some flexibility to make capital distributions that differ from those reflected in a firm's capital plan; however, frequently doing so would call into question the strength of the Regulated Banking Institution's capital planning process and could give rise to supervisory concerns. Thus, to the extent possible, Regulated Banking Institutions typically hew closely to the distributions contemplated by their capital plans, absent a compelling reason to diverge. And although the capital planning rules require Regulated Banking Institution issuers to project their planned uses of capital, including planned share repurchases, many months ahead, precise decisions as to the pricing and timing of repurchases, as well as the ultimate decision as to whether to execute the planned repurchases, any of which could require adjustments to 10b5-1 plans, are not contained in the capital plans. Thus, although Regulated Banking Institution issuers plan the amounts of share repurchases far

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[4] 12 C.F.R. § 225.8 (with respect to large bank holding companies); 12 C.F.R. § 238.170 (with respect to large savings and loan holding companies). By April 5 of each year, a Regulated Banking Institution with at least $100 billion in average total consolidated assets must submit a detailed regulatory capital plan to the Federal Reserve describing, among other things, all planned capital actions over the planning horizon, defined as the period of at least nine consecutive quarters, beginning with the quarter preceding the quarter in which the Regulated Banking Institution submits its regulatory capital plan, over which the relevant projections extend. Smaller Regulated Banking Institutions likewise face capital planning requirements, although the process is somewhat less prescriptive. *See*, *e.g.*, Division of Supervision and Regulation of the Board of Governors of the Federal Reserve System, Bank Holding Company Supervision Manual § 1050.2.3.2.

ahead of time and stay consistent with these plans to the extent their baseline projections regarding economy-wide and firm-specific performance are consistent with reality, this regulatory capital planning process does not address the need for flexibility in execution when inconsistencies between projections and reality do occur. In this regard, consider how the market has evolved and market expectations have changed considerably during the 30-day period from February 20 to March 22 of this year, or during the same period in 2020. Whereas currently 10b5-1 plans can assist Regulated Banking Institutions in appropriately managing their capital levels and executing their capital plans, the lack of flexibility imposed by the 10b5-1 Proposal's cooling off period, paired with the prohibition on overlapping plans, would impede these efforts.

The 10b5-1 Proposal would further erode the utility of the Rule 10b5-1(c) safe harbor for many Regulated Banking Institution issuers due to the way many issuers use it in practice. In order to minimize the possibility of violating the SEC's antifraud and antimanipulation rules, Regulated Banking Institution issuers generally structure trades under their 10b5-1 plans to conform to both the Rule 10b5-1(c) safe harbor and the Rule 10b-18 safe harbor. Thus, in practice, the volume limits of Rule 10b-18 would be layered on any mandatory cooling off period under the 10b5-1 safe harbor. This would significantly limit the utility of the Rule 10b5-1(c) safe harbor, since only one 10b5-1 plan could be in place at a time, and any trades executed under it would also need to conform to the Rule 10b-18 safe harbor volume limits. In addition, many Regulated Banking Institution issuers rely on 10b5-1 plans to execute trades during the self-imposed blackout periods around quarter-end and quarterly earnings releases, when other methods of executing trades would not be available due to the potential possession of MNPI; thus, for these firms, any non-MNPI developments between 10b5-1 plan adoption and trade execution that render the planned trades disadvantageous would effectively shorten the firm's trading window for that quarter.[5] In addition, the cooling off period could lead to artificially created market volatility due to the shortened windows within which issuers would be executing their planned repurchases.

To illustrate, consider an issuer that implements a new share repurchase plan on November 20, such that under the 10b5-1 Proposal, the first trade could not occur until December 20, the beginning of the firm's quarterly black-out period. If the market appreciated significantly within that window, the target pricing contained in the share repurchase plan might no longer be available from December 20 through the end of the year. Under existing rules, the issuer could amend the plan up until its self-imposed blackout period begins on December 20, and purchases could start that date as scheduled. However, the added 30-day cooling off period would cause the Regulated Banking Institution to diverge

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[5] In this context, an issuer enters into a 10b5-1 plan *prior to* the beginning of the firm-designated blackout period, during which, under firm policies and procedures designed to comply with the prohibition on trading while in the possession of MNPI, firms deem themselves to potentially be in possession of MNPI due to the availability of preliminary information about quarterly results. 10b5-1 plans in this context include trades to be executed during the blackout period, when other methods of executing share repurchases are not possible, thereby allowing issuers to spread their share repurchases more evenly throughout the quarter. Under the 10b5-1 Proposal, if an issuer's blackout period begins ten days prior to quarter-end and extends until its earnings announcement about 14 days after the end of the quarter, then the issuer would need to enter into a 10b5-1 plan covering trades as many as 55 days in the future (the 30-day cooling off period, plus a 25-day blackout period). If any developments during the 30-day cooling off period (which would be prior to the beginning of the firm's blackout period), render the execution parameters under the 10b5-1 plan disadvantageous, then the issuer would be unable to execute any share repurchases during at least a portion of the firm's blackout period (since the issuer would be subject to an additional 30-day cooling off period before the execution of any trades).

from its capital plan or regulatory capital management strategies due to the inability to adjust the 10b5-1 plan and still execute trades in this period (since the firm's self-imposed blackout period would preclude it from using other means to execute share repurchases). This could be avoided by allowing the Regulated Banking Institution to adopt or modify a 10b5-1 plan without imposing a cooling off period.

We understand the SEC's desire to ensure that 10b5-1 plans are not inappropriately used to shield insiders and issuers trading while in possession of MNPI from liability under Rule 10b-5; however, none of the evidence cited in the 10b5-1 Proposal suggests that this has been a problem with respect to issuer 10b5-1 plans, as opposed to insider plans. In fact, the recommendation of the Investor Advisory Committee cited in the 10b5-1 Proposal explicitly states that the committee "did not consider issuer share buybacks in its deliberations on this recommendation and believes that any changes to the regulation of these programs should be addressed separately."[6] Furthermore, as noted above, entering into or modifying a 10b5-1 plan while in possession of MNPI is already impermissible, and issuers—particularly Regulated Banking Institution issuers—have robust compliance programs designed to avoid trading on the basis of MNPI, including with respect to entering into or modifying 10b5-1 plans. In this regard, we note that, based on a review of the annual reports of the SEC's Division of Enforcement for years 2016 through 2021, we are not aware of any instances in that period of an enforcement action against a Regulated Banking Institution relating to insider trading. In the absence of evidence indicating that issuers are nevertheless circumventing this prohibition (we are unaware of any), and in light of the multitude of legitimate reasons why an issuer may periodically update its share repurchase strategies, it is inappropriate to implement a cooling off period with respect to an issuer's adoption or modification of a 10b5-1 plan, and we respectfully request that the SEC remove this requirement from the final rule.

Even if the SEC determines that, with respect to most issuers, the benefits of the 30-day cooling off period outweigh its costs, it should consider the specific costs that this requirement would impose on Regulated Banking Institution issuers, discussed above, and carve Regulated Banking Institutions out of this requirement. As noted above, Regulated Banking Institutions are subject to extensive regulatory capital planning requirements, and their regulatory capital planning, review and approval processes receive a great deal of regulatory scrutiny. Decisions relating to the target amount of share repurchases are made months ahead, and deviations from regulatory capital plans are subject to regulatory scrutiny. In addition, Regulated Banking Institutions are typically in the share repurchase market on a very frequent—and sometimes daily—basis in order to somewhat evenly distribute their planned share repurchases over time. In this environment, it would be difficult for a Regulated Banking Institution to engage in the sort of MNPI-driven, opportunistic trading that the proposed cooling off period is intended to address. Layering a 30-day cooling off period and restriction on multiple overlapping 10b5-1 plans on a Regulated Banking Institution's other regulatory capital planning requirements would jeopardize a Regulated Banking Institution's ability to return capital to shareholders in the manner deemed appropriate under the capital planning regulatory framework and optimal by its board of directors, could create market volatility and would not contribute to the SEC's antifraud and antimanipulation goals. Therefore, if the SEC retains this element of the proposal in its final rule, it should exempt Regulated Banking Institution issuers.

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[6] Recommendations of the Investor Advisory Committee Regarding Rule 10b5–1 Plans (Sept. 9, 2021), note 1, *available at* https://www.sec.gov/spotlight/investor-advisorycommittee-2012/20210916-10b5-1-recommendation.pdf.

If, despite all this, the SEC believes it necessary to impose a cooling off period on the 10b5-1 plans of Regulated Banking Institutions, shortening the proposed cooling off period would reduce whatever possibility there could be of a Regulated Banking Institution issuers' acting on the basis of MNPI while avoiding some of the particular challenges for Regulated Banking Institution issuers. Specifically, the cooling off period should be shortened to no more than two weeks. Even if a firm entered into or modified its share repurchase plan while in possession of MNPI (which, as noted above, is already impermissible and would remain so under the revised safe harbor), a maximum two-week cooling off period would reduce the possibility that the market would not have received and reacted to that information by the time any trades actually occur, thereby reducing the chance that any issuer malfeasance would actually harm investors. At the same time, although the existence of the cooling off period would still create the challenges outlined above, the shorter period would permit Regulated Banking Institutions a greater level of flexibility to effectively execute their regulatory capital plans and capital management strategies.

In addition, and in response to Question 14 of the 10b5-1 Proposal, if the SEC retains a cooling off period of any length of time that applies to issuer 10b5-1 plans, it should further clarify in the text of the rule that the prohibition on overlapping share repurchase plans only applies to 10b5-1 plans, and does not prohibit issuers from executing other types of share repurchases that are not intended to take advantage of the Rule 10b5-1(c) safe harbor, even if those trades occur during a period covered under a 10b5-1 plan, including during any cooling off period associated with the 10b5-1 plan. Specifically, the SEC should amend proposed Subsection (B) of Rule 10b5-1(c)(1)(ii) to clarify that the only disallowed trades during a cooling off period are those that would be effected pursuant to the newly adopted or modified 10b5-1 plan and should amend proposed Subsection (D) of Rule 10b5-1(c)(1)(ii) to clarify that only overlapping 10b5-1 plans are disallowed, but that trades not executed pursuant to a 10b5-1 plan are permitted to occur while a 10b5-1 plan is in place. Such clarifications would more closely align the text of the final rule with the intent expressed in the commentary accompanying the 10b5-1 Proposal that the prohibition is only intended to apply to trades made pursuant to overlapping 10b5-1 plans. If the rule was to be interpreted more broadly, it would exacerbate the practical difficulties described above by further reducing Regulated Banking Institution issuers' options for executing entirely appropriate share repurchases.

## II. The new disclosures under Item 703 of Regulation S-K relating to details of an issuer's share repurchase plan could require Regulated Banking Institution issuers to disclose key elements of their capital management policies and practices, which, for these issuers, is competitively sensitive information and, potentially, confidential supervisory information.

Investors already have a great deal of information with respect to the capital actions of Regulated Banking Institution issuers due to the public information available about regulatory capital requirements and the regulatory capital planning process applicable to these issuers. Investors have access not only to the detailed capital and capital planning regulations with which these issuers must comply, but also to disclosure about firms' performance under supervisory and, if applicable, firm-run stress tests. Although this information does not directly align with the share-repurchase-specific disclosure the SEC is proposing to require, it nevertheless provides investors with insights into firms' capital planning processes and actions. In addition, the regulatory requirements and scrutiny applicable to Regulated Banking Institutions' capital planning processes and actions act as a *de facto* constraint on any of the manipulative activity that the Share Repurchase Proposal is attempting to address in proposing additional disclosure with respect to share repurchase activity, both in Item 703 of Regulation

S-K and elsewhere. Thus, in the context of Regulated Banking Institutions, the additional disclosure in the proposals is not necessary.[7]

Furthermore, in the context of Regulated Banking Institutions, the additional disclosure could have anticompetitive effects or be impermissible under rules pertaining to confidential supervisory information. Unlike issuers in other industries, where capital strategy and planning are generally an issue of prudent financial management, in the banking industry, capital strategy and planning are central to a firm's overall competitive strategy, as capital allocation decisions are at the heart of the business of banking. Thus, requiring Regulated Banking Institution issuers to disclose detailed information about key elements of their capital management policies and practices would have an anticompetitive effect on the banking industry. In addition, it is possible that Regulated Banking Institutions' share repurchase plans could be influenced by supervisory communications from the Federal Reserve or another bank regulatory agency, which information could be confidential supervisory information and prohibited from disclosure. It is therefore imperative that the Share Repurchase Proposal's proposed modifications to Item 703 of Regulation S-K, if finalized, not require disclosure of information that would be competitively sensitive for Regulated Banking Institutions or considered confidential supervisory information. Specifically, the Associations recommend removing from the proposed additional disclosure any information pertaining to the "process or criteria used to determine the amount of repurchases," as this category of information is likely to include competitively sensitive information, such as management's desired capital levels or target pricing for share repurchases, or confidential supervisory information. We also note that requiring disclosure of target pricing information, or information that could allow for the calculation of target pricing information, even in a general sense, would contribute to the possibility of front-running and market manipulation regardless of the issuer's industry. For similar reasons, the SEC should not further expand the proposed additional disclosure under Item 703 of Regulation S-K in any of the ways contemplated in Question 17 of the Share Repurchase Proposal.

If the SEC does finalize additional disclosure under Item 703 of Regulation S-K, it should clarify that the required disclosure would not include competitively sensitive information or confidential supervisory information pertaining to share repurchase plans or capital strategies more broadly. The SEC could do so by including an instruction to Item 703 similar in form to that of instruction 4 to Item 402(b) of Regulation S-K, which clarifies that issuers are not required to disclose competitively sensitive information in the context of executive compensation disclosure.[8] Including a similar instruction, covering both competitively sensitive information and confidential supervisory information, with any revised Item 703 of Regulation S-K would address any potential for the final rule to require issuers to disclose competitively sensitive information or confidential supervisory information.

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7 It is not entirely clear that the additional disclosure included in the proposals would actually reduce the inappropriate activities cited in the proposals, such as real earnings management or increasing executive compensation, but, even assuming the proposals would reduce these activities with respect to non-Regulated Financial Institution issuers, for the reasons discussed herein, existing disclosures should already limit these activities with respect to Regulated Financial Institution issuers.

8 17 C.F.R. § 229.402(b).

## III. The proposals would disincentivize the use of share buybacks rather than dividend distributions, an outcome which, with respect to Regulated Banking Institution issuers, contradicts longstanding policy of the Federal Reserve to encourage share buybacks rather than dividend distributions.

Certain elements of the proposals would significantly hinder Regulated Banking Institution issuers' ability and willingness to return capital to shareholders using share buybacks and would therefore incentivize them to increase dividend distributions. For example, and as highlighted in the comments of other industry participants, the Share Repurchase Proposal's requirement to file a new Form SR within one day of executing a share repurchase would enable sophisticated traders to model the trading patterns of issuers such as Regulated Banking Institutions that frequently engage in share repurchases, and thereby front-run trades, or detect when an issuer deviates from its typical pattern and surmise the existence of MNPI, thereby triggering market speculation. This type of market speculation could occur regardless of the reason for an issuer's suspension of its share repurchases. The frequency of the reporting requirement could also result in information asymmetries, with the potential to harm retail investors who are not able to use sophisticated tools to synthesize the information being provided as quickly as more sophisticated traders.

In addition, and in response to Question 39 of the Share Repurchase Proposal, the new Form SR filing requirement would significantly increase the administrative burden and compliance risk associated with executing share repurchases. This increased administrative burden would be particularly acute for Regulated Banking Institution issuers, who, due to the sophisticated nature of their capital management strategies, tend to execute share repurchases on a very frequent, and often daily, basis; thereby resulting in the draconian need for them to file a Form SR daily (or close to daily). Even if a Regulated Banking Institution issuer is furnishing, not filing, disclosure, it takes great care and expends appropriate resources to ensure that the disclosure is accurate and complete. Daily filings would consume significant employee training and time resources and, for the reasons discussed above, would provide little—if any—investor benefit, and could in fact harm investors. If additional disclosure regarding share repurchase practices is nevertheless deemed necessary, reducing the frequency of any such disclosure to no more than monthly, and on an aggregated basis, would ease this administrative burden and avoid some of the broader issues noted above.

Furthermore, as described in greater detail in Section I above, the practical issues associated with the 10b5-1 Proposal would limit the utility of 10b5-1 plans for Regulated Banking Institution issuers by limiting issuers' ability to react appropriately to non-MNPI developments. In some situations, the unavailability of 10b5-1 plans would simply reduce Regulated Banking Institutions' ability to execute share repurchases at all during certain periods.

Ultimately, the various challenges and costs the proposals would create for Regulated Banking Institution issuers would significantly reduce their ability and willingness to rely upon share buybacks as a frequent and predictable means of returning capital to shareholders, as doing so could have the consequence of reducing shareholder value. This could drive Regulated Banking Institution issuers to rely more heavily on dividend distributions, which would not present the same practical challenges and limitations, as a means of returning capital to shareholders.

Disincentivizing Regulated Banking Institutions' use of share repurchases as a means of returning capital to shareholders contradicts longstanding Federal Reserve policy to encourage firms to use share repurchases rather than dividends distributions. Beginning as early as 2010, the Federal Reserve has repeatedly reiterated this preference. In 2010, the Federal Reserve stated that regulatory capital plans that provided for common dividend payout ratios above 30% of projected after-tax net income would receive "particularly close scrutiny" and did not impose similarly objective thresholds with respect to planned share repurchases.[9] In eliminating this guidance in 2020, the Federal Reserve indicated that it had initially adopted it "to encourage firms to increase payouts through additional share repurchases rather than dividends" but that it was no longer necessary because new requirements would "sufficiently restrict dividend increases in the future."[10]

The Federal Reserve implemented these new requirements in 2020 in connection with finalizing the stress capital buffer, a buffer over minimum capital requirements below which a firm's capital distributions are limited, and related amendments to the capital and stress testing requirements applicable to Regulated Banking Institutions. The stress capital buffer framework remains in effect today and generally treats all capital actions, whether dividend distributions or share repurchases, in the same way, with one important exception. To calculate the stress capital buffer, the Federal Reserve adds a firm's losses under the supervisory stress test to the sum of the dollar amount of the firm's planned common stock dividends for four quarters of the planning horizon subject to the stress test. Only dividends, and not share repurchases, are included in this *de facto* prefunding requirement. In proposing this requirement, the Federal Reserve noted that it was "based on the [Federal Reserve]'s experience with large bank holding companies' capital distribution practices during the recent financial crisis. Additionally, evidence in the academic literature generally indicates that repurchases are more flexible than dividends."[11] The Federal Reserve went onto explain that market participants could interpret a firm's reduction in dividends as a signal of long-run deterioration in firm profitability, which could lead to a negative stock price reaction; therefore, even if the outlook for a publicly traded firm has significantly worsened, public pressure and competition may deter the firm from reducing dividend payments. The Federal Reserve concluded, "Requiring a firm to pre-fund one year of dividends reflects the assumption that the firm will strive to maintain its current level of dividends even during times of stress."[12]

A Federal Reserve Bank of New York staff report authored by Beverly Hirtle, now the bank's head of research, more clearly explains the reason for this policy preference for share repurchases rather than dividend payments. The report analyzed the dividend and share repurchase actions of Regulated Banking Institutions during the 2007-2009 financial crisis and found that many Regulated Banking Institutions continued to pay dividends during the crisis, even as financial market conditions deteriorated, large losses accumulated, and emergency capital and liquidity were being provided by the official sector. In contrast, the report found that Regulated Banking Institutions' share repurchases dropped sharply in the early part of the crisis. Hirtle went on to state that, "From a policy perspective, the results suggest that [bank holding companies] could be encouraged to make more of their capital

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9 Federal Reserve System, Revised Temporary Addendum to SR letter 09-4: Dividend Increases and Other Capital Distributions for the 19 Supervisory Capital Assessment Program Bank Holding Companies, at 3 (Nov. 17, 2010). *See also* Federal Reserve System, Comprehensive Capital Analysis and Review: Summary Instructions and Guidance, at 18 (Nov. 22, 2011) *available at* http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20111122d1.pdf.

10 Regulations Q, Y, and YY: Regulatory Capital, Capital Plan, and Stress Test Rules, 85 Fed. Reg. 15576 at 15579 (Mar. 18, 2020).

11 Federal Reserve System, Amendments to the Regulatory Capital, Capital Plan, and Stress Test Rules, 83 Fed. Reg. 18160 at 18165-66 (Apr. 25, 2018).

12 *Id.* at 18166.

distributions in the form of share repurchases, due to the greater flexibility and market tolerance for variability in this form of distribution."[13] She also noted that, "…supervisory measures encouraging [bank holding companies] to rely more on repurchases could enhance the stability of individual [bank holding companies] and of the banking system if these distributions can be reduced without sending potentially destabilizing signals to market participants."[14]

The Federal Reserve has a longstanding and well-founded policy of encouraging Regulated Banking Institutions to return capital to shareholders using share repurchases rather than dividend payments. This policy protects the financial safety and soundness not only of individual firms, but also of the entire financial system. By increasing the potential for market manipulation and speculation, as well as administrative and compliance burdens, and decreasing the practical ability of Regulated Banking Institutions to effectively use share repurchases, the proposals would disincentivize the use of share repurchases and contradict the Federal Reserve's policy. Alternatively, if the proposals are finalized without modification, to the extent Regulated Banking Institutions do continue to use share repurchases, the additional and frequent disclosure could make these issuers less willing to deviate from business-as-usual practices, even in situations where deviations could have financial stability benefits. In this way, the proposals could create similar problems with respect to share repurchases as Hirtle highlights in her report with respect to dividend payments.

If the SEC declines to implement broader industry recommendations to address these issues with the proposals, it should carve Regulated Banking Institutions out of their application to avoid undermining Federal Reserve policy. In addition, and regardless of whether the SEC adopts any recommendations from the Associations or other commenters, we strongly encourage the SEC to consult with the Federal Reserve prior to finalizing any elements of these proposals that would apply to Regulated Banking Institution issuers. Doing so would avoid any unintended interplay between existing regulations and the proposals that would undermine existing bank regulatory policy or unnecessarily harm Regulated Banking Institutions, their investors and financial stability.

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13 Beverly Hirtle, "Bank Holding Company Dividends and Repurchases during the Financial Crisis," Staff Report No. 666 at 3 (Mar. 2014, revised Apr. 2016), *available at* https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr666.pdf. Although Hirtle only explicitly refers to bank holding companies, the same logic applies to the capital actions of savings and loan holding companies.

14 *Id.* at 19.

The Bank Policy Institute and the American Bankers Association appreciate your consideration of the views expressed in this letter. If you have any questions, please contact the undersigned by phone at (202) 589-2533 or by email at [redacted].

Respectfully submitted,

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cc: Mark E. Van Der Weide
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