CENTER FOR CAPITAL MARKETS
COMPETITIVENESS

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April 30, 2013

Mr. Robert deV. Frierson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Re: **Enhanced Prudential Standards and Early Remediation Requirements for Foreign Banking Organizations and Foreign Nonbank Financial Companies; FR Doc 1438 and RIN-7100-AD-86**

Dear Mr. deV. Frierson:

The U.S. Chamber of Commerce ("Chamber") is the world's largest business federation, representing over three million companies of every size, sector and region. The Chamber created the Center for Capital Markets Competitiveness ("CMCC") to promote a modern and efficient regulatory structure for capital markets to fully function in the 21st Century economy. The CMCC welcomes the opportunity to comment on the proposed rule: *Enhanced Prudential Standards and Early Remediation Requirements for Foreign Banking Organizations and Foreign Nonbank Financial Companies* ("Proposal") published by the Board of Governors of the Federal Reserve ("Board") on December 14, 2012, regarding the supervision of foreign banking organizations and foreign nonbank financial companies (interchangeably referred to as "FBOs") designated by the Financial Stability Oversight Council ("FSOC") for supervision by the Board as systemically important financial institutions ("SIFIs").

The CCMC believes that the current Proposal—and potential overseas retaliatory actions—will place American businesses at a competitive disadvantage, harming economic growth and job creation.

The CMCC supports the efforts by federal regulators to monitor and address systemic risk. However, the CMCC is deeply concerned that the Proposal appears to be a significant change in how U.S. operations of FBOs are regulated, presenting

highly problematic issues not only for these U.S. based operations of FBOs, but also for their U.S. counterparts operating overseas. Accordingly, the Proposal may have the unintended consequence of causing FBOs to retrench from operations in the United States, leading to less capital formation for American businesses. Additionally, foreign governments may place similar restrictive measures on American banks operating overseas, making it more difficult for American businesses to have the access to resources needed to operate internationally, and thus causing them to face a competitive disadvantage overseas.

Specifically, the Chamber is concerned that the Proposal:

1) Fails to consider impacts on Main Street businesses and the economy;

2) Lacks appropriate cost-benefit analysis;

3) Subjects FBOs to disparate treatment by setting up a ring-fence approach that requires the establishment of an Intermediate Holding Company ("IHC") and applies discriminatory treatment to IHCs, as domestic counterparts are not required to meet the same capital, liquidity and other regulatory requirements; and

4) Places U.S.-owned subsidiaries operating abroad at risk of retaliatory disparate treatment as foreign governments may seek to impose reciprocal requirements on U.S. banks operating in their countries. This may undermine the global financial system.

These concerns are discussed in more detail below.

Discussion

In an effort to mitigate risks to the financial stability of the United States, Congress directed the Board in the Dodd Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") to establish heightened capital, liquidity, and other prudential requirements for designated SIFIs and bank holding companies with total consolidated assets of $50 billion or more ("Large BHCs"). Congress also directed the Board to: 1) give due regard to the principle of national treatment and equity of

competitive opportunity; and 2) take into account the extent to which the FBO is subject on a consolidated basis to comparable home country regulation.

I. The Proposal Fails to Consider Impacts Upon Main Street Businesses

The Board, in proposing, finalizing, and implementing the Proposal, must take into account the impact the rulemaking will have upon liquidity and capital formation for non-financial businesses. Financial institutions provide capital to businesses and serve as a conduit to match investors and lenders with entities that need funding. Banks, in particular, provide credit and lending that businesses use to expand and create jobs. Foreign capital is an important source of liquidity for Main Street businesses.[1]

Therefore, how the Proposal impacts the ability of financial institutions to lend and extend credit will have a direct bearing upon the ability of non-financial businesses to access the resources needed to operate and expand. For example, many American corporations rely on a syndicate of banks—comprised of both domestic and foreign banks—to support their credit facilities needed to finance operations. Without the participation of foreign banks, risk will be more highly concentrated in the remaining domestic banks, and domestic banks may not be willing to make up the shortfall left by foreign banks.[2] Furthermore, the Proposal may impact varying levels of activities such as having a counterparty needed to clear a transaction. In studying the Proposal it seems that the Board has not taken these non-financial business and economic impacts into account.

A contemplation of these issues is critical to insure that financial institutions are acting as the conduit needed to prime the pump of economic growth. Ring fencing FBOs may create overly prescriptive rules and restrictive capital standards for a particular segment of the financial sector that can dry up credit and lead to a similar inefficient allocation of capital, harming Main Street businesses and economic growth.

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[1] *See* letter of U.S. Chamber of Commerce to Treasury Secretary Timothy Geithner, April 16, 2012, regarding Reporting on Interest Paid to Nonresident Aliens REG 146097-09.

[2] *See* attachment: ***How Main Street Businesses Use Financial Services***. This survey of interviews, with 219 CFO's and corporate treasurers, explores the financial needs of mid-cap and large cap and how these Main Street businesses use commercial banking and other financial institutions to meet those capital and liquidity demands.

This is particularly true with the fragile economic and job growth market that we currently have.

II. Cost-Benefit Analysis

The Board is an independent Agency, but it has avowed that it will seek to abide by Executive Order 13563. Consistent with this approach, the Board has stated that it "continues to believe that [its] regulatory efforts should be designed to minimize regulatory burden consistent with the effective implementation of [its] statutory responsibilities."[3]

Executive Order 13563 places upon agencies the requirement, when promulgating rules, to:

1) Propose or adopt a regulation only upon a reasoned determination that its benefits justify its costs (recognizing that some benefits and costs are difficult to justify);

2) Tailor regulations to impose the least burden on society, consistent with obtaining regulatory objectives, taking into account, among other things, and to the extent practicable, the costs of cumulative regulations;

3) Select, in choosing among alternative regulatory approaches, those approaches that maximize net benefits (including potential economic, environmental, public health and safety and other advantages; distributive impacts; and equity);

4) To the extent feasible, specify performance objectives, rather than specifying the behavior or manner of compliance that regulated entities must adopt; and

5) Identify and assess available alternatives to direct regulation, including providing economic incentives to encourage the desired behavior, such as

[3] *See*, November 8, 2011, letter from Chairman Ben Bernanke to OIRA Administrator Cass Sunstein.

> user fees or marketable permits, or providing information upon which choices can be made to the public.[4]

Additionally, Executive Order 13563 states that "[i]n applying these principles, each agency is directed to use the best available techniques to quantify anticipated present and future benefits and costs as accurately as possible."

Conducting the rulemaking and its economic analysis under this unifying set of principles will facilitate a better understanding of the rulemaking and its impact on businesses and the American economy, and give stakeholders a better opportunity to provide regulators with informed comments and information. In studying the Proposal, the CCMC believes that such a rigorous cost-benefit and economic analysis is needed for commenters to fully understand the Proposal and analyze its impacts on the economy. Some sections of the Proposal state that such an analysis will only be undertaken after commenters have submitted comments.

Commenters have been deprived of the chance to provide regulators with the informed commentary needed for effective and efficient regulations. In March 2013, the CCMC released the attached report[5] on the role of cost-benefit analysis in financial services rulemaking and how those legal requirements lead to smarter regulation. We hope the Board provides commenters with a rigorous cost-benefit analysis to better understand the proposal and its impact upon the financial services industry and economy.

III. Creation of a New IHC, Disparate and Discriminatory Treatment

To comply with the Proposal, FBOs with total consolidated assets of $50 billion or more including at least $10 billion in U.S. based operations, must house all non-branch and non-agency U.S. operations, such as investment advisory, broker-dealer or insurance subsidiaries, in an IHC. Such a move would require significant internal reorganization that is costly, complex and difficult. This legal reorganization will no doubt create tax implications, the cost of which will likely be passed on to customers and borne by shareholders. Additionally, FBOs may face logistical challenges moving some of their U.S.-based subsidiaries into the IHC because, while

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[4] Executive Order 13563

[5] *See* attachment, *The Importance of Cost Benefit Analysis in Financial Regulation.*

the FBO may control 25% or more of the voting securities of a subsidiary, it may not have enough control over a subsidiary to make it a part of the IHC. This could lead many FBOs to consider curtailing their U.S. activities, ultimately limiting products and services available to U.S. customers.

Under the Proposal, U.S. subsidiaries of FBOs reorganized into an IHC are placed at a significant competitive disadvantage, some of which is discriminatory. First, regardless of whether the IHC includes a banking subsidiary of an FBO, it is subject to the same risk-based and leverage capital requirements that apply to Large BHCs. This means that for those IHC operations that are not banking related, they would be subject to enhance prudential regulation by the Board in addition to regulations by their primary regulator, such as the Securities and Exchange Commission.

Second, beyond discrimination, the supervisory structure outlined in the Proposal would also seem to undermine the role of the primary regulator and its regulations. In effect, the Proposal would force separate new requirements onto the subsidiaries of foreign-owned banks that similarly situated subsidiaries of U.S.-owned banks are not subjected to. In particular, the Board will be imposing its leverage requirements directly onto foreign owned-subsidiaries through an IHC while permitting U.S.-owned banking organizations to consolidate their subsidiaries under the parent's global capital without a separate IHC leverage requirement.

Third, because the threshold for requiring reorganization under an IHC is only $10 billion in total consolidated assets, IHCs will face significantly higher regulatory burdens and compliance costs from dual regulation than their U.S. competitors of equivalent size that face only their primary regulator. Some FBOs are estimating that compliance costs from the dual regulatory regime will individually exceed over $100 million with little to gain from the duplicative yet potentially conflicting regulatory regimes. Moreover, the Proposal permits U.S. firms to rely on their global balance sheet and capital while an FBO owning a U.S. nonbank subsidiary in the IHC is forced to apply U.S. bank capital and leverage ratios to its U.S. subsidiary on top of the subsidiary's capital requirements from its functional regulator.

Finally, the Proposal is being considered at the same time regulators are contemplating the proposed rulemaking to implement the Basel III capital agreements

("Basel III NPRs"). In our October 22, 2012 comment letter on the Basel III NPR's, the CCMC stated that there must be uniform application of Basel III for an international system of capital standards to work. At that time the CCMC expressed concerns that the European Union and member nations were taking steps to undermine such a uniform application. We have the same concerns with the Proposal, which places IHCs at a different capital level than their domestic counterparts. The Proposal therefore violates the principles of international consistency of global capital standards as articulated by the CCMC.

Given these concerns and those expressed by other commenters, the CCMC believes the Board should modify the Proposal in the following ways making it more effective and less burdensome:

1) Contingent convertible capital provided by a parent FBO to an IHC – including subordinated debt subject to "bail in"—should be counted as equity in that IHC.

2) While the proposal should also make clear that, so long as adequate capital and liquidity are kept in the U.S. to support the operating subsidiaries where losses may occur, structuring flexibility is appropriate.

3) Even where U.S. capital and other BHC requirements are deemed to apply to an IHC, we believe that greater flexibility should be provided to rely on a robust home country's supervisory and governance regime for calculating and implementing these requirements, especially under the Advanced Approaches of the Basel Agreements.

4) Any final rule should make clear that excess liquidity above the minimum amounts required should be permitted to flow freely outside of the U.S. to address needs in other parts of an FBO's operations.

5) To the extent that a substantially higher leverage ratio would be imposed on the IHC than would otherwise be required, that requirement should be phased in over time consistent with the Basel III timetable for phasing in the international leverage ratio.

IV. International Considerations

During the consideration of Dodd-Frank, Congress clearly expressed its intent on how FBOs are to be regulated in the U.S. It explicitly directed the Board to heed deference to an FBO's home country supervision, particularly when there is comparable consolidated supervisory regime.

By now requiring FBOs to reorganize U.S. operations under an IHC, the Board is undermining the home country supervisory regime that has been the cornerstone of financial services regulation. The CCMC has and continues to support efforts for increased coordination and communication amongst regulators through the G-20 process, which is also based upon the home country supervisory approach. By creating IHCs, it is reasonable to infer that two consequences will occur:

1) Foreign nations will require American banks to face similar or more restrictive ring fenced capital structures that will impede the operation of American banks overseas; and

2) The global financial framework will be Balkanized to such an extent that the efficient and effective flow of capital on a global basis will be impeded. This will have broader capital formation and liquidity impacts harming sectors such as trade, thereby impeding economic growth and financial stability.

Because of these concerns, the CCMC believes that a more appropriate way to address systemic risk posed by U.S. operations of FBOs is to address these issues on a global level, to ensure that a level playing field is set for all domestic and global entities worldwide. Accordingly, the talks to devise systems to monitor and regulate Globally Systemically Important Financial Institutions ("G-SIFIs") should also be used to deal with the FBO issues in the context of increased coordination and communication amongst the appropriate national regulators.

Conclusion

The CCMC is concerned that the Proposal fails to take into account the impacts upon Main Street businesses, and may harm the domestic and global financial systems that can harm the competitiveness of American non-financial—as well as financial—firms. The lack of an appropriate cost-benefit analysis also prevents commenters from providing the Board with informed commentary needed for appropriate rulemaking.

The CCMC also believes that the current Proposal will also prompt other nations to adopt similar ring-fencing rules for U.S. banks' foreign operations, which will tear apart the sinews of the modern global financial networks.

Rather than follow the approach put forward in the Proposal, we believe that the Board should engage with its international counterparts to use the existing home country supervisory system and mechanisms for dealing with G-SIFIs as the means for addressing risks posed by FBOs. Enhanced cross-border regulatory cooperation, coordination and communication is a preferable means to dealing with FBO issues rather than the construction of new regulatory systems and subsequent international responses that may cause more economic harm and threaten the global financial system.

Sincerely,

Tom Quaadman