BMO Financial Group

June 21, 2019

Via Electronic Mail

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Office of the Comptroller of the Currency
250 E Street, SW
Washington, DC 20219

Re: Notice of Proposed Rulemaking - Prudential Standards for Large Foreign Banking Organizations; Revisions to Proposed Prudential Standards for Large Domestic Bank Holding Companies and Savings and Loan Holding Companies, Federal Reserve Docket No. R-1658 and RIN 7100-AF45

Joint Notice of Proposed Rulemaking - Changes to Applicability Thresholds for Regulatory Capital Requirements for Certain U.S. Subsidiaries of Foreign Banking Organizations and Application of Liquidity Requirements to Foreign Banking Organizations, Certain U.S. Depository Institution Holding Companies, and Certain Depository Institution Subsidiaries, Federal Reserve Docket No. R-1628B and RIN 7100-AF21, OCC Docket ID OCC-2019-0009 and RIN 1557-AE63, and FDIC RIN 3064-AE96

Ladies and Gentlemen:

BMO Financial Group, a highly diversified financial services provider based in North America, operates in the United States through BMO Financial Corp. ("BFC"), an intermediate holding company ("IHC"), as well as through two branches and an agency of Bank of Montreal, a Canadian chartered bank (together with its affiliates and subsidiaries, "BMO"). BMO Harris Bank, NA, a subsidiary of BFC, is a federally chartered bank that has been serving retail and commercial customers in the Midwest for over 100 years. BMO provides lending, deposit taking, wealth management, and investment banking services in the United States.

We appreciate the opportunity to comment on the above referenced notices of proposed rulemaking issued by (i) the Board of Governors of the Federal Reserve System (the "Board") and (ii) the Board, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation, respectively (collectively, the "Agencies"). In this letter we collectively refer to the above referenced notices as the "Proposal."

We understand that the Canadian Bankers Association, the Institute of International Bankers and the Bank Policy Institute together with the American Bankers Association each plan to submit letters setting forth suggestions and comments with regard to the Proposal. We share the views expressed in those letters and we respectfully urge the Agencies to carefully consider the positions set forth therein.

We support the Agencies' ongoing efforts to appropriately tailor regulatory requirements to address specific, identified risks, as well as the Agencies' ongoing efforts to improve the simplicity, transparency and efficiency of regulations while still achieving their respective regulatory objectives.

We are submitting these comments, however, to express our concern that the Proposal falls short of these goals. The consideration of risks external to IHCs in crafting regulation for IHCs has resulted in a Proposal that is unduly complex and that does not efficiently address the risks perceived by the Agencies. In fact, rather than tailoring regulation to relevant and identified risks, it potentially expands regulation at IHCs based on risks that are not relevant to the IHCs' operations.

As set forth below, we believe that evaluating an FBO's combined U.S. operations ("CUSO") to determine the level of regulation on the FBO's IHC (1) misaligns the identified risk and the proposed solution (as illustrated by the potential impact on BFC, as discussed below), (2) places an unnecessary burden on IHCs putting them at a competitive disadvantage to domestic BHCs, and (3) is duplicative of existing home and host country regulation that already addresses and mitigates this risk. Accordingly, we believe that the Agencies should revise the Proposal so that it scopes the regulation for the IHC based only on the assets and characteristic of the IHC. Any consideration of risk at the branch should be considered separately through regulation applied to the branch with due consideration given to existing home and host country regulation already in place.

1) <u>The regulatory requirements applicable to an IHC should be based on the assets and activities of the IHC and should not be based on risks contained within the FBO's U.S. branches.</u>[1]

As drafted, the Proposal will impose regulatory requirements on IHCs for liquidity (LCR and NSFR) and SCCL based not solely on the characteristics of the IHC, but also on the characteristics of the FBO's U.S. branches, which are separate and distinct from the IHC.

Attempting to address liquidity risk presented by the U.S. branches of FBOs through regulation of IHCs misaligns risk and regulation. The misalignment causes additional high quality liquid assets (HQLA) to be held within the IHC, where there is no additional liquidity need. The misalignment

[1] As used throughout this letter, references to an FBO's "branch" or "branches" means a collective reference to such FBO's branch and agency network, as applicable.

therefore results in additional, unnecessary and burdensome requirements for IHCs and puts IHCs at a competitive disadvantage to their domestic peers.

The IHC structure was required to provide a consolidated platform for the application of enhanced regulation at a distinct entity where appropriate capital and liquidity could be isolated in order to support risk contained within the IHC. The Proposal abandons this framework and conflates the IHCs' risks with external risks, thereby resulting in a regulation that is not tailored to the risk that the IHC presents. In this manner, the Proposal fails to achieve any supervisory goal.

The potential impact of the Proposal on BMO exemplifies the misalignment of regulation and risk. As noted, BFC is the intermediate holding company for BMO's subsidiaries in the U.S. BFC is comparable to a regional bank holding company in the U.S. and currently has over 14,000 employees. Our four main business lines are: personal banking, commercial banking, wealth management and capital markets, with our principal focus on small- and medium-sized business lending. Our core business is our banking business which is based mostly in the Midwest where we are one of the top ten agricultural lenders and one of the largest providers of truck and trailer financing in the U.S.

BFC has a strong balance sheet and a conservative risk profile, with high levels of liquidity and capital. Over 75% of the assets in BFC are contained within BMO Harris Bank, our nationally chartered bank, which is supported by over $80B in deposits, one of the most stable sources of funding available. BFC is already subject to enhanced prudential standards, including an LCR, and holds ample liquidity to accommodate its operations, even in times of stress.

As proposed, BFC falls into Category IV for both capital and liquidity requirements under the current parameters of the Proposal. However, the inappropriate scoping of CUSO assets to determine the application of liquidity regulation to BFC provides for the possibility of increased regulation even if BFC's business doesn't change. For reasons wholly unrelated to BFC's risk profile, BFC could potentially move into Category III or even Category II and be subject to heightened liquidity and daily reporting requirements. Even minimal branch growth in the United States with no corresponding increase in BFC's risk could cause BFC to be subject to the more stringent standards. BFC's business profile simply does not merit or require the application of the heightened liquidity standards set forth in the Proposal.

2) <u>The framework of the Proposal creates an unnecessary regulatory burden on IHCs without efficiently or effectively accomplishing an identified regulatory goal.</u>

Imposing heightened liquidity and SCCL requirements on an IHC would not efficiently or effectively address risks at the FBO's branches for the following reasons.

a) Any additional liquidity held by an IHC as required by the Proposal may not be readily available to address a liquidity problem at the FBO's U.S. branch and, in any event, is not appropriately sized.

Liquidity is not always fungible between different legal entities. An IHC's ability to support branch operations through the provision of liquidity is severely limited by both practical considerations (*i.e.*, ongoing business at the IHC and its subsidiaries) and statutory and regulatory restrictions on the transfer of funds (*e.g.*, Regulation W), as well as the IHC's continuing requirement to maintain newly increased liquidity to support its own operations. As a result, any increased liquidity held at an IHC as a result of the Proposal may not be easily deployable to address a liquidity problem at an affiliated branch. The Proposal therefore creates excess liquidity that may be trapped within IHCs, thereby failing to provide any definitive or guaranteed corresponding benefit to affiliated branches or the system overall.

Even if liquidity at an IHC could be transferred to an affiliated branch, the amount of liquidity required to be held at IHCs under the Proposal is inappropriately sized to support the needs of affiliated branches because the Proposal requires IHCs to maintain liquidity based on the potential needs of the IHC, not the potential needs of the affiliated branch. As such, the Proposal does not effectively address the targeted risks

b) If there are liquidity risks presented by the operations of FBOs' U.S. branches, the Proposal does not fully address them because the enhanced liquidity regulation applies only to those FBOs with IHCs with more than $50B in assets.

Assuming that potential liquidity issues at FBOs' U.S. branches present an unaddressed risk to the U.S. financial system, the Proposal does not adequately address such risk because it only applies to a small portion of FBOs operating in the U.S. The Proposal does not address the perceived liquidity risk at the U.S. branches of FBOs that have small IHCs or no IHC at all. There are well over 150 FBOs operating in the United States, while only twelve of these FBOs have IHCs with over $50B in assets. As such, the rule would leave the perceived liquidity risk posed by these entities unaddressed solely because they utilize a different organizational structure.[2]

c) Requiring IHCs to hold excess liquidity based on external risks within a U.S. branch is not only inefficient, but will place IHCs at a competitive disadvantage to their domestic peers.

The Proposal will place foreign banks at a competitive disadvantage to domestic banks and runs counter to well-established principles of national treatment and competitive equality. Requiring IHCs to hold HQLA based on risks not contained within the IHC is unnecessary because it does not contribute to the safety or soundness of the IHC. At the same time, the cost of maintaining the required HQLA will impose significant costs on the IHC, placing it at a competitive disadvantage to domestic BHCs. Ultimately, this will reduce competition for American consumers and make the U.S. financial system less efficient. Such inefficiency could be further exacerbated if other jurisdictions were to replicate this framework and adopt a more nationalist approach.

[2] Such structure would also put certain FBOs at a competitive disadvantage to other FBOs, which we do not believe was the Agencies' intent.

3) Even if imposing liquidity requirements on an FBO's IHC was an appropriate, efficient and effective way to address liquidity risks at the FBO's U.S. branches, no such additional requirements are necessary because such risks have already been addressed by existing regulation.

FBO branches, as part of a larger, highly regulated organization, are already subject to home-country regulations applicable at the consolidated FBO level. Reliance on comparable home-country standards recognizes that branches are simply extensions of the FBO and is consistent with U.S. statutory mandates.[3] Standardized liquidity requirements applicable to FBOs have been established based on standards approved by the Basel Committee on Banking Supervision and the Financial Stability Board and, in the case of BMO, include a consolidated LCR and NSFR.

In addition to home-country obligations, FBOs' U.S. branches are already subject to U.S. regulation. Regulation YY (which was implemented post-financial crisis to address, among other things, liquidity risks) imposes a variety of liquidity and risk-based requirements (including liquidity stress testing and a liquidity buffer) on the U.S. branches and CUSOs of FBOs. Regulation YY also mandates certification and reporting requirements with respect to compliance with home-country standards. In light of these requirements, it is unnecessary to impose additional requirements.

The Agencies should therefore rely on existing home-country requirements and Regulation YY obligations to address any liquidity risks presented by U.S. branches of FBOs. The Agencies should not impose additional regulations to address risk that has already been analyzed and mitigated through international efforts and standards. We recognize, and we understand that the Agencies recognize, that not all countries have the same standards as the United States or Canada. It is, however, unnecessary to impose burdensome and duplicative regulatory requirements on all FBOs operating in the U.S. in order to address any such inconsistencies.

In the event the Agencies' identify any risk that is not currently addressed by the existing requirements, such as home-country regulations that do not adequately implement internationally agreed upon standards, cooperation between the Agencies and the applicable home-country regulator could be used to address and remedy any such situation. In the absence of any such solution, the Agencies have adequate and sufficiently broad supervisory and examination powers to impose any additional obligations they deem necessary. We understand and appreciate that the Agencies value consistency and transparency, which are often better achieved through regulation rather than supervision. However, in the context of liquidity risk for an FBO branch network subject to home-country supervision, we think achieving the goals of consistency and transparency should not be at the expense of appropriate tailoring and efficiency. The Agencies' examination and supervisory powers exist to address idiosyncratic concerns identified at firms, including the robustness of home-country supervision. In this context, imposing an additional layer of regulation on all FBOs (i) penalizes banks that operate in home countries where regulations promulgated pursuant to international standards have been adopted and (ii) is inconsistent with the concepts of national treatment and competitive equality.

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[3] *See* 12 U.S.C. § 5365(b)(2).

Conclusion

We believe that any liquidity risk presented by the U.S. branches of FBOs has been sufficiently mitigated through home-country regulation and the additional regulation imposed under Regulation YY. Notwithstanding, in the event any such unmitigated risk does exist, we believe it is inappropriate and inefficient to apply heightened regulation to an IHC based on the characteristics of the FBOs' CUSO. In this way, we believe the Proposal is not appropriately tailored to address the identified risks. We therefore respectfully request and recommend that the Proposal be revised to apply regulation at the IHC based only upon the risks posed by the IHC. Without such changes, the Proposal will not meet the objective of appropriately tailoring the stringency of enhanced prudential standards to match the risk profile of the entity being regulated.

If the Agencies have concerns that the U.S. branches of FBOs present liquidity risks that are not currently addressed, we recommend that those concerns be analyzed and considered separately from the tailoring of IHC regulations. The imposition of standardized liquidity requirements on the U.S. branches of FBOs is, as the Board has noted, a novel concept in the context of international regulation. As such, we believe the costs and benefits of any such proposal and any potential impacts thereof should, at a minimum, be fully and rigorously analyzed and discussed, including at an international level.

We appreciate the Agencies' efforts to thoughtfully consider tailoring regulation for FBOs operating in the U.S. and hope that you will consider these comments as you move forward. We would be happy to discuss in further detail any of the recommendations herein. Please contact the undersigned for questions or any additional information.

Sincerely,

Darryl White
Chief Executive Officer
BMO Financial Group

David R. Casper
U.S. Chief Executive Officer
BMO Financial Group