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WACHOVIA

April 2, 2007

VIA ELECTRONIC MAIL

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Electronic Address: reg.comments@federalreserve.gov

RE: Response to the Board's Request for Comment on Intraday Liquidity Management and Payment System Risk Policy

Dear Ms. Johnson:

Wachovia Corporation ("Wachovia"), on behalf of itself and its subsidiaries, including Wachovia Bank, National Association ("Wachovia Bank"), appreciates the opportunity to respond to the request of the Board of Governors of the Federal Reserve System ("Board") for comment on intraday liquidity management and the Board's Payment System Risk (PSR) Policy. In light of market trends, especially the identified increase in large Fedwire payments made late in the day, we believe that it is prudent for the Board to seek input from financial institutions in order to foster the continued safety and efficiency of payments and settlement systems.

Wachovia responds below to the specific questions contained in Section V of the Board's Notice.

1. *What intraday liquidity conservation strategies and technologies does your institution use (such as controlling the timing of payments and introducing queuing techniques to conserve on liquidity)? How do these affect your institution's timing for sending payments? What, if any, changes are you planning with regard to intraday liquidity management?*

Wachovia employs a variety of liquidity conservation strategies, such as controlling the timing of payments, payment queue management, emphasizing CHIPS versus Fedwire, intercompany net-debit caps and requiring Corporate Treasury approval for any time-critical payments. Wachovia also has guidelines on the amount of exposure we have to the late-day funding markets. Although the process for managing the timing for sending payments is manually intensive, it is operationally manageable at current levels. Wachovia is considering the feasibility of a more robust intraday liquidity risk management and profit module accompanied by a revised policy on liquidity management with intraday emphasis.

2. *How do the concentrated demands for intraday central bank money by private sector systems influence intraday liquidity management by depository institutions throughout the day? Are there significant concentrated sources of demand for intraday central bank money beyond those already mentioned in the text and how does this demand affect intraday liquidity management?*

Demands by the private sector greatly influence intraday liquidity management. Coordination is required that involves aspects of credit and liquidity risk management, funding, Federal Reserve position management and payment operations. Net debit caps serve as the outer boundary, because central bank money is the ultimate provider of depository institution daylight overdraft. Customer demands for more intraday liquidity (i.e. requests for committed facilities) have been on the rise and are expected to increase demand for intraday liquidity.

3. *Is the concentration of payments late in the day a concern for your organization? If so, what is the nature of your concern? Does it include operational risk from late-in-the-day payments, and has operational risk to your organization from such payments been increasing or decreasing? What are the key drivers of late-in-the-day payments? How has your organization responded to the late-in-the-day concentration of payments?*

Late-in-the-day payments are a growing concern for our organization because of the operational risk of processing them so close to the Fedwire third party deadline. Competitive pressures and customer demands now make it necessary for us to stretch external customer deadlines right up to payment system deadlines. Therefore, even the slightest technical problem or the need for transactions to be repaired, can sometimes cause late-day transactions experienced by us, our customers and/or any market participant, not to be processed on a same-day basis or cause our funding projections to be inaccurate. Credit risk is also increased due to the decision on whether to grant intraday credit being condensed into a very short period of time or larger overdrafts are created earlier in the day and stay on our books longer. The resulting impact can include customer dissatisfaction and financial loss due to the need for interbank compensation payments or the granting of an unsecured overdraft.

Our approach to mitigate operational risk is to continue to explore ways to increase straight through processing and to complete processing earlier in the day. We look to minimize credit risk by requesting customers to send as many of their payments as possible earlier in the business day even if it means breaking bulk payments into smaller batches later in the business day. We are clearly seeing a general trend towards customer initiation of payments later in the day. We believe that the shift is due to a corresponding shift in our customers' business activities and practices which are conducted around the clock in different time zones around the world.

4. *For the market, operational, and PSR Policy changes discussed in this document and listed as follows, how might the timing of payments and the demand for daylight overdrafts be affected? What advantages or disadvantages do you see for these changes?*

   - *An intraday market to exchange liquidity between institutions that hold positive balances at the Reserve Banks and those that run negative balances*

     This idea could be an outlet that some banks could use in order to decrease reliance on central bank money for intraday liquidity; however, unless there are established rules and a system supporting the intraday liquidity market, we do not think this product would gain market support.

   - *A market for the early return of federal funds or other money market investments*

     If this practice gains further traction in the marketplace, it could be an outlet that some banks could use in order to decrease their reliance on central bank money for intraday liquidity. Offsetting this improvement would be those banks making early repayments that might have to increase their reliance on central bank money. As with the intraday day market to exchange liquidity, this market practice would gain further support if there are established rules and a system supporting early returns. Unless early returns prove to be suitably profitable, most likely any system enhancement to automate early returns would not be forthcoming.

   - *Enhancements by private settlement systems that further economize on the use of central bank money, for example multiple settlement periods to release liquidity earlier in the day*

     This idea merits further review; however, multiple settlement periods may potentially use up quite a lot of central bank money early in the day which may not be returned until toward the end of the day. We have seen part of this with CLS, as the cutoff is 6:00 am New York time. In order to achieve a decreased reliance on central bank money, a careful review of those enhancements must be completed.

   - *Liquidity saving mechanisms for the Fedwire funds transfer system*

     Providing banks with an option to use liquidity-saving mechanisms should be considered, because banks could initiate wires earlier in the payment process without incurring daylight overdraft fees.

- *Throughput requirements for the Fedwire funds transfer system*

  As mentioned in the consultation paper, this option would be difficult to achieve and enforce.

- *Greater use of voluntary or required collateral to cover partially or fully daylight overdrafts in depository institution accounts at the Reserve Banks*

  This idea clearly warrants pursuit and would be enhanced if accompanied by a differentiating pricing system. The incentive for banks to provide collateral for a much lower priced daylight overdraft fee should eventually result in an adjustment in the rising operational risk exposure. It could also represent a business opportunity to certain participants. Mentioned in the consultation paper is the idea of using discount window collateral at a lower OD cost, which seems a logical option for banks and one that Wachovia endorses.

- *Two-tiered pricing for collateralized daylight overdrafts, with a fee charged for collateralized daylight overdrafts set lower than the rate for uncollateralized overdrafts*

  This idea has appeal. It should be attractive to those banks currently paying significant OD charges. It could also represent a business opportunity to certain participants. Another variation would be not charging for daylight overdrafts if the exposure is adequately collateralized.

- *Time-of-day pricing of daylight overdrafts*

  This idea has appeal. It should be attractive to those banks currently paying significant OD charges. It could also represent a business opportunity to certain participants.

5. *What are other possible approaches to consider to reduce delays in payments and to manage efficiently and effectively the Federal Reserve's exposure to increasing daylight overdrafts as well as depository institutions' exposure to intraday liquidity and credit risks? Are there other market or operational changes in the private sector that could help reduce intraday liquidity and credit risks?*

   As discussed in the Report of the Joint Task Force on the PSR Policy Consultation Paper, Wachovia reiterates its support of an improvement to the CHIPS algorithm. This improvement should have a positive knock on effect on those payments that are still in a bank's liquidity and credit queues. Over the years, investor behaviors have changed. More and more investors are making large dollar investment decisions toward the end of the day after the Fedwire Securities Wires and DTC are closed.

6. *Congress is currently considering legislation that would allow the Federal Reserve to pay interest on reserve balances held by depository institutions at the Reserve Banks. How would the payment of interest on reserves affect depository institutions' intraday*

liquidity management, including the demand for daylight overdrafts at the Reserve Banks? Could the payment of interest on reserves be utilized to reduce the value or timing of daylight overdrafts?

For most banks, the analysis will hinge on the profitability trade-off between the current low reserves and no-interest environment and the legislation under consideration that would allow payment of interest on reserves.

Wachovia appreciates the opportunity to provide these comments in response to the Board's request. If you have any questions about these comments, please contact me.

Sincerely,

Eugene M. Katz