Deutsche Bank

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March 13, 2007

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

RE: OP-1257; Consultation Paper on Intraday Liquidity Management and Payment System Risk Policy

Dear Ms. Johnson,

Deutsche Bank AG ("Deutsche Bank") appreciates the opportunity to comment on the consultation paper issued by the Federal Reserve Board ("Board") on intraday liquidity management and payment system risk policy (the "Paper"). Deutsche Bank through its New York branch and its wholly-owned subsidiary Deutsche Bank Trust Company Americas ("DBTCA") is one of the largest U.S. dollar clearing banks. Accordingly, Deutsche Bank takes an interest in and supports the Board's efforts to reduce risks, while improving efficiency in the payments system.

The Paper addresses several important operational issues and proposes improvements to the Payment System Risk Policy ("PSR"). In addition to the issues raised in the Paper, Deutsche Bank urges the Board to reconsider the disparate treatment of domestic and foreign banks under the PSR. The PSR restricts the intraday credit capacity of foreign banks as compared to their domestic counterparts. Consequently, international banks are at a significant competitive disadvantage with regard to daylight overdraft capacity and the imposition of daylight overdraft fees. Deutsche Bank supports and echoes the comment submitted by the Institute of International Bankers on the cost component of this issue. We also believe that the reduced daylight overdraft capacity for foreign banks that results from this policy is a competitive disadvantage for us when compared to our U.S. bank peers.

Answers to the specific questions posed by the Board are attached as Appendix A hereto. We hope that our responses will assist the Board as it considers improvements to the PSR to reduce risk and increase efficiency in the payment system. We also hope that the Board will consider amending the PSR to provide for equal treatment of foreign and

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domestic banks in determining the cap for daylight overdrafts. Please do not hesitate to contact Joseph Rice at (212) 250-2428 should you have any questions about this letter.

Very truly yours,

Richard Ferguson
Managing Director
Treasurer of the Americas

cc: Joseph Rice
Russell Fitzgibbons
Katelyn Jannelli
Joshua Kaplan, Esq.

Appendix A

Responses to Consultative Paper Questions

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?

While we proactively manage the timing and flow of payments, it is not possible to delay all payments. Depository Trust Corporation ("DTC") payments, CLS Bank International ("CLS") settlements, and time sensitive client payments are always be expedited. Our internal Credit Risk Management process is a natural regulator of payment flow as the amount of intraday credit that we provide to our clients is regulated by this process. Smaller value payments are released as soon as the payment clears our internal Credit Risk Management process. While these actions may delay certain payments, we are actively making payments throughout the day.

We have also actively sought to balance the payment flow between the Clearing House Interbank Payment System ("CHIPS") and Fedwire to avoid large inflows via CHIPS with a disproportionately large outflow via Fedwire. Balancing this flow will have a positive impact on the use of daylight overdraft by DBTCA. We do not anticipate making any changes to our intraday liquidity management process at this time.

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?

Payments to DTC, which must be made earlier in the day, increase our demand for intraday liquidity from the Federal Reserve Bank of New York ("FRBNY").

Imbalances in payment flow between CHIPS and Fedwire also create a demand for daylight overdraft in our account at the FRBNY. As noted above, we have actively sought to manage the balance between CHIPS and Fedwire payments with our clients.

Tripartite repurchase agreements require us to make payments early in the day to release the securities that are financed. The timing of payments made to release securities from tripartite repo and the timing of securities settling through DTC becoming available for repo will have an impact on daylight overdraft usage (discussed in number 3 below).

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?

Our payment systems and staff routinely clear payment queues of thousands of large dollar value payments in short periods of time and, consequently, are capable of managing large concentrations of late in the day payments. However, we believe that spreading out the flow of payments throughout the day would be a benefit to both our institution and the overall payment system. Our concern with late payments is centered on the potential impact on our daylight overdraft capacity at the FRBNY should there be an imbalance in the timing of payment inflows and outflows. Those concerns include but are not limited to the following:

- *DTC requires that we make progress payments to them via Fedwire if the net settlement is an outflow. In the case of new commercial paper that we purchase, DTC does not release the new securities until late in the day. We cannot place those new securities into tripartite repo until they are delivered to us. In some cases, Deutsche Bank must fund the release of maturing commercial paper from tripartite repo early in the day but cannot place new issue commercial paper until later in the day. This causes us to use our daylight overdraft capacity at the FRBNY to cover the timing mismatch.*

- *Other drivers of late day payments are the late return of federal funds sold. This is not a concern as long as we are not asked for early return of federal funds purchased or other maturing liabilities. For example, the Board's recent change in policy on daylight overdrafts incurred by Government Sponsored Enterprises ("GSEs") has led many GSEs to seek the early return of deposits that they place with banks to fund principal and interest payments on key settlement dates creating a timing mismatch between the return of federal funds and depositor withdrawals. While Deutsche Bank incorporates the cost of the early return of funds into the pricing of its deposit products when the customer seeks the early return of funds, we do not believe that this pricing practice is uniform in the market.*

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
    - *Intraday markets for liquidity would be desirable but the systems to manage timed flows would need to be centralized with the Reserve Banks. Deutsche Bank opposes the development of an intraday market with multiple settlements, as this would add to the operational complexity and cost for the member banks.*
- A market for the early return of federal funds or other money market investments
    - *Deutsche Bank supports a market for the early return of federal funds. These payment amounts are known early in the day and there is no operational reason for the delay of payment. It is likely that participants in the federal funds market delay the return of federal funds as a means of minimizing daylight overdraft fees charged by the Reserve Banks.*
- 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
    - *Multiple settlement periods in the private settlement systems during the course of the day may force the release of liquidity and securities earlier in the day and would likely result in a more even distribution of daylight overdraft levels in the system throughout the day. While payment flows on some private settlement systems can be managed, the behavior of participants managing those flows cannot be predicted. Deutsche Bank does not support multiple settlement periods with the Reserve Banks. The current end of day close allows for the member banks to square up their positions after all of the markets and private settlement systems have closed. Front office and operations staff responsibilities are shifted to the end of day closing process at the Reserve Banks. Multiple settlements would require additional cost in staffing and in systems.*
- Liquidity saving mechanisms for the Fedwire funds transfer system
    - *Deutsche Bank supports the concept, however, further study is required.*
- Throughput requirements for the Fedwire funds transfer system
    - *Deutsche Bank supports the concept, however, further study is required.*
- Greater use of voluntary or required collateral to cover partially or fully daylight overdrafts in depository institution accounts at the Reserve Banks

- *A more flexible version of the FRBNY's Max Cap facility would be a welcome development. Today, we need to provide the FRBNY with board approval each time we want to increase the amount of available collateralized daylight overdraft. The FRBNY's ability to receive and return collateral is limited. Both of these factors make utilizing collateralized daylight overdraft cumbersome. Enhancing the FRBNY's ability to accept and return collateral combined with policy changes that allow for the expansion of collateralized daylight overdraft when needed would be a welcome development.*

- Two-tiered pricing for collateralized daylight overdrafts, with a fee charged for collateralized daylight overdrafts set lower than the rate for uncollateralized overdrafts
    - *Increased use of collateralized intraday overdraft facilities would require a two tiered daylight overdraft pricing system (collateralized vs. uncollateralized). Two tiered pricing would need to be priced aggressively as the cost of collateral would need to be considered as part of the total cost of daylight overdraft.*
- Time-of-day pricing of daylight overdrafts
    - *Time of day pricing for daylight overdraft may have the desired effect of moving the return of federal funds settlements earlier in the day. It would also reinforce the concept of pricing timed payments.*

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?

- *Explore opportunities with DTC to accelerate the end of day settlement process.*
- *Explore expansion of netting opportunities among tripartite repo participants and perform an overall efficiency review of the tripartite repo settlement process.*
- *Explore opportunities with CHIPS to further enhance load balancing between CHIPS and Fedwire as well as expediting payments held in the CHIPS payments release engine.*

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?

If the rate paid by the Federal Reserve on reserve balances was a market rate, member banks might view leaving funds with the Reserve Banks as a viable option. For banks that routinely sell excess funds into the market, this may alleviate the daylight overdraft usage that is caused by the late return of funds. It may also increase the number of member banks that borrow from the discount window as liquidity that was available in the market late in the day may now be placed at the Reserve Banks. The net impact to the liquidity in the system would be unchanged, but the Reserve Banks would need to become an active participant in the unsecured federal funds market as it would likely be inserted in the middle of what is now a bi-lateral transfer of end of day liquidity among member banks.