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Northern Trust

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VIA ELECTRONIC SUBMISSION

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

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

Office of the Comptroller of the Currency
250 E Street, S.W., Mail Stop 2-3
Washington, D.C. 20219

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

David A. Stawick, Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Comment Letter on the Notice of Proposed Rulemaking Implementing the Volcker Rule — Proprietary Trading

Federal Reserve Docket No. R–1432 and RIN 7100 AD 82; FDIC RIN 3064–AD85; OCC Docket ID OCC–2011–14; SEC File No. S7–41–11; CFTC RIN 3038–AD05

Ladies and Gentlemen:

Northern Trust Corporation ("Northern Trust") welcomes the opportunity to comment on certain proprietary trading portions of the proposed rules (the "Proposed Rules") implementing new Section 13 of the Bank Holding Company Act of 1956 (the "Volcker Rule"). Northern Trust has commented separately with certain other banking entities and trade associations on the covered funds portion of the Proposed Rules. With respect to the proprietary trading portions of the Proposed Rule, Northern Trust concurs with the comment letters submitted by the Securities Industry and Financial Markets Association and other trade associations, the Securities Lending Division of the Risk

Management Association, and the Investment Company Institute, of which Northern Trust is a member.

Northern Trust is a leading provider of investment management, asset servicing and fund administration, banking solutions and fiduciary services for corporations, institutions and affluent individuals worldwide. Northern Trust is based in Chicago and has offices in 18 U.S. states and 16 international locations in North America, Europe, the Middle East and the Asia Pacific region. As of December 31, 2011, Northern Trust had assets under custody of US$4.3 trillion, and assets under investment management of US$663 billion.

Due to the importance of the Proposed Rules to our clients and our business, Northern Trust submits this comment letter separately to support the proposed exclusion of spot foreign exchange from the proprietary trading restrictions and to recommend that foreign exchange swaps and forwards also be excluded from the proprietary trading restrictions and compliance requirements of Sec. 13. We summarize below the adverse impact to our clients and our business if foreign exchange swaps and forwards are subjected to the restrictions of Sec. 13 and the proposed compliance requirements.

1. Spot Foreign Exchange Should Be Excluded From The Proprietary Trading Restrictions, As Proposed (Question 50)

Northern Trust strongly agrees with the proposal of the Agencies to exclude spot foreign exchange from the restrictions in Sec. 13. Spot foreign exchange is a very traditional and low-risk activity that is absolutely essential to the banking business and does not carry any of the risks to banking entities or to the U.S. financial system that Sec. 13 is intended to reduce. It is particularly essential for a global custodian bank such as Northern Trust to be able to conduct spot foreign exchange transactions in connection with our global custody and administration services businesses. If spot foreign exchange transactions were to be subjected to the restrictions of Sec. 13 it would be virtually impossible for a U.S. banking entity to conduct routine foreign exchange activities even on a break-even basis. A business in which U.S. banks are globally competitive would essentially be ceded to non-U.S. banks, with a resulting decrease in low-risk core operating revenues for U.S. banks and a loss of U.S. employment.

Congress recognized the low risk inherent in spot foreign exchange by excluding it from the requirements of Title VII of the Dodd-Frank Act. Spot foreign exchange also has the characteristics described in the proposed "Determination of Foreign Exchange Swaps and Foreign Exchange Forwards under the Commodity Exchange Act" issued by the Department of the Treasury on April 29, 2011 ("Proposed Determination"). The very adverse impact to U.S. banking entities and to U.S. global competitiveness that would result from spot foreign exchange being subjected to the Sec. 13 restrictions is not offset by any possible benefit to U.S. banking entities or to the U.S. financial system.

2. **Foreign Exchange Swaps And Forwards Should Be Excluded From The Proprietary Trading Restrictions And Compliance Requirements In The Proposed Rules (Question 55)**

It is clear that the definition of "proprietary trading" in Sec. 13(f) does not require inclusion of foreign exchange swaps and forwards in the trading restrictions, and there is no indication in the legislative history that members of Congress intended to include these traditional and low-risk transactions in the trading restrictions. The Agencies have discretion whether to include foreign exchange swaps and forwards within the definition of a "derivative" or to include them as "any other financial instrument" that should be regulated under Sec. 13. For the reasons set out below and in other comment letters, Northern Trust strongly recommends that the Agencies exclude foreign exchange swaps and forwards from the proprietary trading restrictions and from the compliance requirements in the Proposed Rules.

As stated above, Northern Trust is a significant global custodian and asset manager and it is typically in that capacity that Northern Trust carries on an active foreign exchange trading operation. The foreign exchange trading operation supports Northern Trust's client focused custody and asset management businesses, and the ability to carry out foreign exchange transactions is a necessary part of the custody and fund administration services business. Foreign exchange transactions are generated as a result of the routine purchase or sale of securities by our clients, or the receipt or payment of income or capital actions or redemptions, or the clean payment of a currency for another reason.

In essence, a foreign exchange swap is simply a spot foreign exchange transaction ("near date") executed simultaneously with a forward foreign exchange transaction ("far date"). These are simple cash management transactions used by our clients to efficiently manage cross currency needs. The foreign exchange swap mitigates foreign exchange exposure for our clients and Northern Trust by removing the foreign exchange risk, since rates are set at the start of the transaction. Both transactions require physical settlement of the currency on the respective dates. Northern Trust does not trade in foreign exchange options, futures or structured derivatives, and we transact a small volume of non-deliverable forwards.

Northern Trust has never had a quarterly loss from foreign exchange trading during the past 20 years. Northern Trust has a robust risk management framework in place to govern the risks involved in its foreign exchange trading business. Thus, the foreign exchange business has been a source of steady and low-risk income for Northern Trust for many years, and the growth of Northern Trust's global custody business has resulted in a steady increase of foreign exchange business. If Northern Trust is restricted from transacting foreign exchange in the manner proposed in the Proposed Rules, or if all trades must comply with the designated exclusions and are subject to the proposed

compliance regime, our foreign exchange business will be at significant risk due to increased costs of compliance.

Foreign exchange trading is a truly global business, and operates with extremely thin margins; trading is always conducted on a principal-to-principal basis and is based on bid/offer spreads and not on fees. A significant percentage of our foreign exchange business is with clients that are not located in the U.S.; these clients can easily move their foreign exchange business to a non-U.S bank that will be able to operate without the impediments of the Volcker Rule. For example, in 2011 Northern Trust reported approximately $324 million in foreign exchange trading income. Approximately 50% of our foreign exchange volume was transacted outside the U.S., primarily for non-U.S. clients. We estimate that if the Volcker Rule includes foreign exchange swaps and forwards in the proprietary trading restrictions and compliance requirements, as much as 50% of our foreign exchange trading volume will be at risk of moving to non-U.S. bank providers. We believe other U.S. banks will experience similar erosion of foreign exchange revenues. This will significantly damage the amount and diversity of our revenues and our ability to continue to provide cost-efficient services to our clients. There is absolutely no offsetting benefit to the U.S. financial system or to our safety and soundness that would result from this very negative impact.

Northern Trust believes that the foreign exchange market is qualitatively different from the markets for other derivatives, and that as a result the risks related to foreign exchange trading are materially lower than for many other financial instruments. The distinctiveness of the foreign exchange market was acknowledged by Secretary Geithner in the Proposed Determination. The Proposed Determination identified the distinctive characteristics of the foreign exchange market, in that foreign exchange swaps and forwards have (i) fixed payment obligations, (ii) are physically settled, and (iii) are predominantly short-term. The Proposed Determination correctly concluded that foreign exchange swaps and forwards "already reflect many of Dodd-Frank's objectives for reform including high levels of transparency, effective risk management, and financial stability". They are more similar to funding instruments, such as repurchase agreements, than they are to other types of derivatives such as commodity forwards and swaps. Foreign exchange transactions are more similar to commercial transactions than to speculative transactions, and they have a qualitatively different risk profile that is based more on settlement risk than on counterparty credit risk. The fact that most foreign exchange forwards and swaps are settled through CLS Bank, and that approximately 98% settle on a net basis, mitigates the settlement risk significantly.

Northern Trust's foreign exchange business follows the pattern described in the Proposed Determination. On average approximately 75% of foreign exchange transactions are spot, which are excluded from the restrictions in the Proposed Rules. Of the remaining total foreign exchange swaps and forwards, more than 98% mature in less than 12 months and the weighted average duration of the transactions is under 3 months.

In order to manage the risk of foreign exchange trading, Northern Trust has a very robust risk management framework and follows applicable supervisory guidance related to risk management of foreign exchange trading. In addition to foreign exchange trading in the U.S., Northern Trust also conducts foreign exchange trading in London and Singapore in order to be able to operate in all time zones, and is subject to supervisory standards for foreign exchange trading in those jurisdictions.

The proposed compliance framework in the Proposed Rules, and the required metrics, to demonstrate that every transaction falls under one of the permitted exclusions, is particularly onerous and should be reconsidered. This "one-size-fits-all" approach to compliance metrics does not appropriately consider the different risk attributes of various types of financial market transactions. For example, foreign exchange trading is predominantly based on the bid/offer spread, and it would be impracticable to produce Fee Income and Expense data. In addition, we would be unable to produce a Spread Profit and Loss because we have never accounted for foreign exchange trading revenues in this manner. To the extent that the Agencies insist on including foreign exchange in the Volcker Rule compliance framework, it will be more appropriate to use traditional measures of foreign exchange trading risk, such as Value at Risk (VaR).

It also is not appropriate to require the full panoply of compliance for very small trading positions. Aside from foreign exchange trading, Northern Trust from time to time may have very small mark-to-market exposures in "plain vanilla" derivatives and securities. Where a banking entity has occasional and modest "covered financial positions", the banking entity should not be required to incur the very heavy costs of a full compliance framework and metrics simply to demonstrate that each position is not "proprietary trading". The Agencies instead should use their existing supervisory authority, together with their backup authority to prevent high-risk trading and conflicts of interest, to assure that the banking entity is conducting trading in a prudent manner and consistent with Sec. 13.

If the Proposed Rules were implemented as drafted, Northern Trust has estimated that the up-front cost of enhancing systems and compliance to meet these requirements will be at least $3.8 million and that the annual cost of compliance will be at least $700,000. We believe other banking entities will experience similar costs, and that these costs have not adequately been considered by the Agencies in issuing the Proposed Rules. Even with these costs the Agencies should understand that many of the metrics in the Proposed Rules simply cannot be produced by banks that are not engaged in true proprietary trading. Currently, for example, Northern Trust would be able to produce up to 11 of the 28 variables called for in Appendix A. Many other variables in Appendix A could only be produced with extensive systems enhancements and, as indicated above, would be of little or no value. These overly prescriptive requirements simply to document that no transaction is "proprietary" are an absurd and abusive implementation

of the Volcker Rule, and the costs and burden are not offset by any possible benefit to individual banks or the U.S. financial system.

The Agencies have asked whether, if foreign exchange swaps and forwards are included in the definition of a "derivative", they should be permitted under Sec. 13(d)(1)(J). Northern Trust believes that, although permitting foreign exchange swaps and forwards under 13(d)(1)(J) is better than not providing for any permission at all, Sec 13(d)(1)(J) is not an appropriate alternative to excluding these types of transactions from the definition of a "derivative". Permitting the activity under 13(d)(1)(J) would subject the activity to the full compliance and record-keeping burden set forth in Appendix A of the Proposed Rules. The result would be, as indicated earlier in this comment letter, a significant increase in the cost and risk of transacting foreign exchange for our clients and for Northern Trust with no offsetting benefit to the banking entity or to the U.S. financial system. This additional burden would decrease the ability of U.S. banks to compete in the global foreign exchange markets and would inevitably lead clients to move their foreign exchange activity to non-U.S. banks that are not subject to the same compliance burdens.

Accordingly, for the reasons set out above, Northern Trust strongly recommends that the best way for the Agencies to deal with foreign exchange swaps and forwards is to exclude them completely from the definition of a "derivative" in the Proposed Rule and to exclude them from the compliance requirements of Appendix A.

Northern Trust appreciates the opportunity to provide the Agencies with the foregoing comments and recommendations regarding the Proposed rules.

Respectfully submitted,

James E. Roselle
Associate General Counsel