

Minister of Finance



Ministre des Finances

Ottawa, Canada K1A 0G5

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Mr. Timothy Geithner
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220
U.S.A.

Dear Secretary Geithner:

I am writing to express my concerns regarding the proposed Volcker rule, which could have material adverse effects on Canadian financial institutions and markets.

I understand and support the objectives of the proposed Volcker rule. However, the rule as currently drafted would have an unprecedented extraterritorial reach and significant cross-border effects, which would be particularly problematic for Canada, given the close inter-linkages between the Canadian and U.S. financial systems.

I am particularly concerned that the proposed rule could severely impact the liquidity of Canadian government debt markets and interfere with the risk management practices of banks in Canada. The draft rule could also have serious unintended consequences for Canadian bank-sponsored mutual funds, hampering their ability to provide services to their Canadian clients.

In response to the global financial crisis, you and I have agreed, along with our G20 colleagues, to pursue an ambitious financial regulatory reform agenda to create a stronger and more resilient global financial system that supports economic growth. Canadian and U.S. regulators have chosen different but equally valid regulatory approaches to work towards the same objective. I am concerned that the extraterritorial application of the proposed Volcker rule, by creating conflicting requirements and unnecessary compliance burdens, will interfere with Canadian efforts to strengthen our domestic financial system.

Canada The word "Canada" in a serif font, with a small Canadian flag to its right.

I respect the right of U.S. regulators to extend any new restrictions on the activities of U.S. banks to activities carried out by Canadian banks in the United States. However, the Volcker rule as drafted would also potentially apply to Canadian banks' much larger Canadian operations, which pose no risk to U.S. taxpayers or U.S. financial stability. The Volcker rule could apply to transactions between Canadian banks that are simply facilitated by U.S.-based financial infrastructure, such as U.S. clearing houses. This could have unintended adverse consequences for the U.S. financial system. For example, by imposing a high compliance burden on the use of U.S. financial infrastructure, the proposed Volcker rule could force foreign banks to clear and settle transactions in non-U.S. jurisdictions, or to avoid U.S. exchanges altogether.

The current draft of the Volcker rule would limit the liquidity of Canadian government bond markets. The exclusion of U.S. government securities from the Volcker rule's restrictions on proprietary trading is premised on the importance of the market-making function in ensuring adequate liquidity in government bond markets and the significant role played by government bonds in traditional banking activities. This same logic should apply to government-issued and government-guaranteed securities in other jurisdictions, including Canada. Moreover, the draft rule proposes an onerous reporting regime that risks withdrawing market makers from a wide range of Canada's financial markets, including our corporate bond and equity markets.

The draft rule would also limit Canadian bank-sponsored mutual funds' ability to provide services to their Canadian clients. The rule effectively treats Canadian mutual funds, which are similar in most respects to U.S. mutual funds (which are exempt from the proposed rule), on par with hedge funds and private equity funds. Without a change to the rule, a Canadian covered banking entity could be precluded from continuing to sponsor such a fund if it had unitholders resident in the U.S., even temporarily. This would be inconsistent with the longstanding regulatory practice of the Securities and Exchange Commission to allow Canadian mutual funds to deal with Canadians temporarily resident in the U.S.

The Governor of the Bank of Canada, Mark Carney, and the Superintendent of Financial Institutions, Julie Dickson, have submitted comment letters to the relevant U.S. regulatory agencies, expressing concerns, as they relate to their own mandates, with the proposed rule. The Investment Industry Association of Canada, the Canadian Bankers Association, and the asset management affiliates of the five largest Canadian banks, have also commented on the draft rule. I would encourage you, your staff, and the relevant U.S. regulatory agencies to take careful note of these submissions and of the very important issues they raise.

I share your commitment to fostering a safe and sound financial system. In finalizing rules under the Dodd-Frank Act, I urge you and your colleagues to take careful consideration of any unintended consequences that U.S. rulemaking could have on broader financial systems around the world, including Canada. I am sure that it is

possible to place limits on risk-taking within U.S. financial institutions and to reduce the potential risks to U.S. taxpayers without imposing significant constraints on the Canadian financial sector or conflicting with Canada's own proven regulatory model.

Thank you for your attention to this issue.

Yours sincerely,



James M. Flaherty

c.c.

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RE: Docket No. 2011-1432 and RIN 7100 AD 82

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RE: File Number S7-41-11 and RIN 3235-AL07

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RE: Docket No. OCC-2011-0014 and RIN 1557-AD44