Deutsche Bank

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April 30, 2012

Re: Enhanced Prudential Standards and Early Remediation Regulations under Dodd-Frank Sections 165 & 166

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, N.W.
Washington, DC 20551
Docket No. 1438; RIN 7100-AD-86

Dear Ms. Johnson:

Deutsche Bank AG ("**Deutsche Bank**") appreciates the opportunity to provide comments to the Board of Governors of the Federal Reserve System (the "**Board**") on the Board's proposed Regulation YY (the "**Proposal**"), which would implement the enhanced prudential standards and early remediation requirements established by Sections 165 and 166 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**"). Although Deutsche Bank has chosen to comment on this Proposal, Deutsche Bank also intends to submit comments on the Board's forthcoming Regulation YY proposal applicable to foreign banking organizations ("**FBOs**") and their U.S. branch operations.

As a general matter, Deutsche Bank supports efforts to implement prudential standards that are focused on minimizing the damage to the financial system and broader economy in the event systemically significant companies suffer material financial distress. Deutsche Bank believes, however, that many aspects of the Proposal warrant reconsideration, for the reasons set forth in the comment letter of the Clearing House Association L.L.C., the American Bankers Association, the Financial Services Roundtable, and the Securities Industry and Financial Markets Association (the "**Associations' Comment Letter**"). Deutsche Bank supports many of the positions taken in the Associations' Comment Letter, but is writing separately to emphasize five specific issues with the Proposal.

First, Deutsche Bank believes that it is paramount that the Board coordinate Regulation YY with its contemplated rule applying Sections 165 and 166 to FBOs. As an FBO that controls a U.S. based bank holding company ("**BHC**") subsidiary with total consolidated assets of $50 billion or more, Deutsche Bank will be subject to Regulation YY when it becomes effective, and to the Board's final rule applying Sections 165 and 166 to FBOs.

Moreover, the manner in which the FBO proposal treats aspects of Deutsche Bank's U.S. operations will almost assuredly be relevant to Deutsche Bank's obligations under Regulation YY. For this reason, the Board should not finalize Regulation YY until it has received and considered all comments on its forthcoming FBO proposal, particularly comments on the aggregate effects of the proposals. In addition, the FBO proposal and Regulation YY should become effective on the same date.

Second, Deutsche Bank submits that Regulation YY's capital, stress testing, and liquidity requirements should be imposed only at (i) a non-bank operating entity that transacts with third parties and could cause systemic harm to the U.S. financial system if it were to suffer material financial distress (such entities will hereinafter be referred to as **"Systemically Significant Operating Companies,"** or **"SSOCs"**), and (ii) U.S. bank holding companies that have over $50 billion in assets ("**Covered BHCs"**).

Furthermore, for liquidity buffer purposes, the Board should not prescribe the entities in which liquidity buffers are held, as long as those liquidity buffers are reasonably accessible for use by the relevant SSOCs or Covered BHCs. Prescriptive legal entity-specific liquidity buffers could result in a buffer becoming trapped in an entity, rendering it unavailable for use by other U.S. based entities. A trapped liquidity buffer in one U.S.-based entity could, in turn, create the need to raise additional amounts of funding to address liquidity concerns in other U.S.-based entities. This would be an inefficient, duplicative, and costly result.

Third, any SSOC that meets U.S. Basel II reporting requirements should be permitted to report its capital, including under stress, under the same Basel II standards as its FBO parent in order to avoid regulatory burdens that provide limited, if any, regulatory benefit. Alternatively, if the Board requires that the SSOC report its capital under a U.S. version of Basel, then the version of U.S. Basel reporting used by the SSOC should be the same version of U.S. Basel reporting that is currently used by the FBO's top-tier U.S. BHC.

Fourth, counterparty credit exposure limits for major covered companies should not be reduced to 10% of capital and surplus; such a percentage is arbitrary, and there has been no necessary factual support for such a reduced limit. In addition, central clearing parties (**"CCPs"**) and non-U.S. sovereigns with equal or superior creditworthiness to that of the U.S. should be exempt from the 25% counterparty credit exposure limit.

Fifth, risk management prudential standards should apply only to SSOCs and Covered BHCs – not to those entities that have more than $50 billion or more in assets, but do not transact with third parties and are established solely used for tax, accounting, and administrative purposes within a broader corporate structure (such entities are hereinafter referred to as "**Intermediate Holding Companies**"). Moreover, under the final rules, in order to allow SSOCs and Covered BHCs flexibility in arranging their corporate governance, there should not be a specific requirement for the risk committee of a SSOC or Covered BHC, as long as it is not the ultimate parent company, to have independent directors, and the chief risk officer for such entities should be permitted to report to the entity's chief executive officer and, in the case of an FBO, the head office as well.

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I. The Board Should Coordinate Comments on Proposed Regulation YY with Comments on Its Forthcoming FBO Proposal, and Regulation YY Should Not Become Effective Until the FBO Proposal Becomes Effective.

In its preamble, the Board states that the Proposal does "not apply to [FBOs], and the Board expects to issue a separate proposal shortly that would apply the enhanced standards of sections 165 and 166 of the Act to [FBOs]."[1] For an FBO like Deutsche Bank, it is imperative that the enhanced standards required under Regulation YY be consistent and compatible with the enhanced standards required under the Board's forthcoming FBO proposal.

Deutsche Bank operates a branch in New York, in addition to owning both a U.S. BHC with over $50 billion in assets, which controls Deutsche Bank Trust Company Americas, a state member bank, and Deutsche Bank Securities Inc., a registered broker-dealer. For this reason, Deutsche Bank will be subject to the Board's FBO proposal as well as Regulation YY. The nature of Deutsche Bank's business requires that the business and operations of its branch operations be managed in tandem with its other U.S. bank and nonbank operations, and therefore the Board's enhanced standards under the FBO proposal will influence and implicate the business and operations of entities subject to the Board's enhanced standards under Regulation YY.

It is therefore imperative for Deutsche Bank and other similarly situated FBOs that Regulation YY and the FBO proposal be coordinated so that the two regulations complement, rather than contradict, each other.

For the foregoing reasons, Deutsche Bank respectfully requests that the Board coordinate comments on proposed Regulation YY with comments on the Board's

[1] Proposal, at 6.

forthcoming FBO Proposal, and that Regulation YY should not become effective until (i) the FBO proposal becomes effective and (ii) the appropriate global regulators have had an opportunity to conform their regulations, so that duplicative requirements are eliminated and conflicts in regulatory approaches do not require globally operating BHCs and SSOCs to meet inconsistent obligations.

Without waiting for such an approach to occur among the global regulators of BHCs and SSOCs, the implementation of Regulation YY will likely lend to the introduction of identical or similar requirements in different jurisdictions where a BHC or a SSOC operates, which could lead to multiple overlapping and conflicting regulatory regimes being applied to the same entity. As a result, there will be an increased compliance burden, cost, and potential for systemic risk for such entities, without achieving any demonstrable benefits by way of customer protection or market stability.

II. Capital, Stress Testing, and Liquidity Requirements Should Apply Only To SSOCs and Covered BHCs

The Proposal includes rules to implement the requirements of Sections 165 and 166 of the Dodd-Frank Act related to risk-based capital and leverage, liquidity, single-counterparty credit limits, overall risk management and risk committees, stress tests, early remediation and, in the case of covered companies that are determined to pose a grave threat to financial stability, certain debt-to-equity limits. The Proposal applies each of these requirements at the level of the "covered company," defined as any bank holding company with $50 billion or more in consolidated assets and any nonbank financial company designated for Board oversight under Section 113 of the Dodd-Frank Act.

Deutsche Bank submits that the capital, liquidity, and stress testing requirements in the Proposal be required only at SSOCs and Covered BHCs. Intermediate Holding Companies (other than Covered BHCs) should be excluded from the definition of covered company, as there is no reason to require an Intermediate Holding Company to comply with minimum risk-based and leverage capital requirements separately, given its consolidation upward into an ultimate parent company and the absence of transactions with third parties. This is particularly the case where the ultimate parent holding company is the real source of strength for its SSOCs and Covered BHCs, and the SSOCs and Covered BHCs meet applicable capital, liquidity, and stress testing requirements. Moreover, Intermediate Holding Companies do not create any potential for systemic risk to the financial system, since they typically do not transact with third parties and are typically utilized for tax, accounting and administrative purposes within a broader holding company structure.

A. Capital

For FBOs, it is at the SSOC and Covered BHC level where the interconnections giving rise to systemic risk reside, and therefore where capital requirements are needed to account for that potential risk. The Board has the legal authority to tailor the Proposal's requirements to exclude Intermediate Holding Companies and similar entities pursuant to its discretionary powers under Section 165(a)(2)(A) of the Dodd-Frank Act, which provides that the Board may "differentiate among companies on an individual basis or by category, taking into consideration" a company's capital structure, complexity and financial activities, among other factors.[2]

B. Stress Testing

Given that the purpose of stress testing is to determine if the capital levels and liquidity buffers of covered companies (as defined in the Proposal) are appropriate, the foregoing logic applies to the stress testing requirements as well as capital requirements: stress tests should only be required at SSOCs and Covered BHCs.

C. Liquidity

Deutsche Bank believes that, unless the definition of "covered companies" is restricted to only SSOCs and Covered BHCs, Regulation YY would require banking organizations to duplicate liquidity management efforts unnecessarily, and, perhaps more problematically, would distract attention from entities where a liquidity crisis could have a systemic impact, thus potentially increasing systemic risk. Given that many of the inputs to the required liquidity analysis presume an operating business,[3] applying the liquidity requirements to an SSOC is certainly reasonable. Similarly, in the case of a Covered BHC, applying the liquidity requirements is reasonable because, as the Financial Crisis showed, liquidity concerns at the ultimate parent company level can easily undermine confidence in subsidiary banks, leading to a liquidity crisis. Such policy reasons, however, do not support imposing liquidity requirements at the level of Intermediate Holding Companies.

In addition, Deutsche Bank recommends that, for liquidity buffer purposes, any liquidity buffer that is required at a SSOC or Covered BHC subsidiary of an FBO be held in an entity that allows the liquidity buffer to be reasonably accessed by the respective SSOC or Covered BHC. The Board should not prescribe the entity at which this buffer is held, as several U.S. regulations (including the Board's Regulation W and the Securities and

[2] Dodd-Frank Act, Section 165(a)(2)(A).

[3] *See, e.g.*, Proposed 12 C.F.R. § 252.55(c) (comprehensive cash flow projections, including "cash flows arising from contractual maturities, as well as cash flows from new business, funding renewals, [and] customer options.").

Exchange Commission's capital rule that penalizes broker-dealer lending to affiliates) could result in a liquidity buffer becoming trapped, rendering it unavailable for use by other U.S. based SSOCs or Covered BHCs. Without an amendment to the Proposal as set forth above, excess liquidity buffers could develop, because booking amounts and locations naturally vary over time, leading to changing amounts needed by respective legal entities. Should these excess liquidity buffers build in one U.S.-based SSOC or Covered BHC while falling short in another, the established buffer would not be available to other U.S.-based SSOCs or Covered BHCs in the group, creating the need to hold multiple liquidity buffers. As a result, additional external funding would be required in other U.S.-based SSOCs or Covered BHCs, creating an inefficient, duplicative, and costly result. Accordingly, the Board should amend its liquidity buffer requirements to allow for the promotion of a more efficient allocation of resources in a multi-tier corporate structure.

III. Any SSOC That is Owned by an FBO and Meets U.S. Basel II Reporting Requirements Should be Permitted to Report Its Capital Under the Basel II Standards Used by the Parent FBO, or Alternatively, Under the Standards Used by the FBO's Top-Tier Covered BHC.

Proposed section 252.14 of Regulation YY would require each nonbank financial company to report to the Board on a quarterly basis its risk-based capital and leverage ratios "as calculated under section 252.13(b)" of proposed Regulation YY.[4] Proposed section 252.13(b), in turn, requires nonbank financial companies to calculate their capital under, *inter alia*, 12 C.F.R. part 225, appendix G, which implements the Basel II advanced approach for BHCs with more than $250 billion in assets or more than $10 billion in foreign exposure.[5]

The effect of these two provisions is that a nonbank financial company with more than $250 billion in assets (or more than $10 billion in foreign exposure) that has been designated as systemically significant can be required to report capital ratios to the Board on a U.S. Basel II basis. The Proposal should be clarified so that, in the case of an SSOC that meets U.S. Basel II reporting requirements and is owned by an FBO, such company should be permitted to report its capital under the Basel II standards utilized by the parent FBO.

To require the use of U.S. Basel II for one or more U.S. SSOC entities and home country Basel II for the FBO will impose significant operational and compliance burdens on the U.S. operations of FBOs, which will be required to engage in very complex capital calculations under differing standards. The operational and compliance burden stems from the fact that the U.S. version of Basel II is based on definitions (*e.g.*, non-performing assets) that often differ from an FBO's home country Basel II definitions. Because many FBO's

[4] *See* Proposed 12 C.F.R. § 252.14.

[5] *See id.* § 252.13(b).

historical databases are not based on U.S. definitions and do not include intercompany transactions, FBOs are presently unable to populate U.S. Basel II risk models with the necessary information without building new systems at an exorbitant cost. Moreover, the information that would be derived from these new systems could not even be utilized for their home country Basel II reporting, given the differences in the FBO's home country Basel II definitions and the U.S Basel II definitions.

Deutsche Bank, which currently utilizes EC Basel II for its global operations and U.S. Basel I reporting for its U.S. BHC (since its U.S. BHC has less than $250 billion in assets and $10 billion in foreign exposure on an annual basis), under the Proposal would now be required to utilize a third version of Basel reporting (*i.e.*, U.S. Basel II) for any of its SSOCs that have $250 billion in assets or $10 billion in foreign exposure on an annual basis. Such a result would create a compliance and reporting burden that would create limited, if any, effect in reducing the systemic risk of an SSOC. This result would likely not be exclusive to Deutsche Bank, but would extend to many other FBOs.

If the Board chooses not to allow SSOCs to report capital under its home country's Basel II reporting regime, due to the Board's apprehension of not being able adequately to compare institutions that use home country Basel II reporting versus those that use U.S. Basel II reporting, then the Board should amend its Proposal so that any SSOC subsidiary of an FBO should be permitted to report its capital and leverage ratios under the Basel reporting standards currently used by the FBO's top-tier U.S. BHC. Such an amendment to the Proposal would not create a situation under which the aforementioned entities could potentially be a greater risk for causing systemic harm to the U.S. financial system, but instead would cause such entities to maintain even more capital then would be required under U.S. Basel II reporting.

IV. The Proposal's Single-Counterparty Credit Exposure Limits Should be Revised.

For many of the reasons set forth in the Associations' Comment Letter, Deutsche Bank has grave concerns about the single-counterparty credit exposure limits set forth in the Proposal. In this letter, Deutsche Bank wishes to amplify three of these concerns: (1) there is no basis for the Board's proposed reduction of the 25% exposure limit to 10% in the case of major covered companies; (2) there should be an exemption for exposures to CCPs; and (3) there should be an exemption for exposures to high-quality non-U.S. sovereign obligations that are as or more creditworthy than the United States.

In the first case, the reduction of the exposure limit to 10% of consolidated capital stock and surplus in the case of exposures of a major covered company (as defined in the Proposal) to a major counterparty (as defined in the Proposal) will result in a severe retrenchment in the operations of major covered companies, with negative ripple effects throughout the financial system and the economy as a whole. The Proposal does not set forth any meaningful empirical support for this extraordinary deduction, much less that it is necessary to achieve overall financial stability. In the absence of such empirical support, the Board's departure from the statutory 25% test cannot be justified as an appropriate instance of administrative interpretation.

Second, given the requirement in Title VII of the Dodd-Frank Act that derivative transactions be cleared through CCPs, the Board should implement an exemption from the single-counterparty credit limits ("**SCCL**") for exposures to those parties. The need to exempt CCPs from a covered company's SCCL requirements is heightened because under Title VII of the Dodd-Frank Act clients will be allowed to choose the CCP at which they want their derivative transactions cleared, making it quite possible that a swap dealer's otherwise risk-balanced portfolio of derivatives could be split into multiple portfolios of unbalanced risks, which would create random and unpredictable amounts of credit exposure to individual CCPs.

Moreover, it is not abundantly clear, given the pace at which the movement to centralized clearing is proceeding, that there will be many significant CCPs operating in the immediate term. As a result, the imposition of credit exposure limits could operate as a barrier to growth – or worse, a restraint on existing business – in these markets, because covered companies (as defined in the Proposal) would be effectively forced to conduct an unnaturally reduced amount of business with the few significant CCPs that were available to accept their trades. As the Associations' Comment Letter states, any exposure limits to CCPs should be addressed as part of the development of the overall regulatory regime for clearing in United States and abroad.

Finally, there is no reasonable justification for exempting U.S. sovereign debt from the credit exposure limit while at the same time imposing that limit on non-U.S. sovereigns of equal or better credit quality. Such differential treatment will only distort the market for such non-U.S. sovereigns, which in itself – particularly at the present time – will substantially increase, rather than reduce, the potential for systemic risk.

V. The Proposal's Risk Management Standards Should Be Less Prescriptive and Allow for More Flexibility to Covered Companies and FBOs in Designing Enterprise-Wide Risk Management Standards.

The Proposal would require each covered company (as defined in the Proposal) and certain publicly-traded medium-sized BHCs to establish a risk committee of the board of directors to document and oversee, on an enterprise-wide basis, the risk management practices. In addition, a covered company (as defined in the Proposal) would be required to employ a chief risk officer to provide an objective assessment of the risks taken by the company.

Deutsche Bank shares many of the concerns set forth in the Associations' Comment Letter about the prescriptive nature of the Proposal as it relates to corporate governance. Deutsche Bank submits that it is more important from the laudable goal of achieving enhanced enterprise-wide risk management that the chief risk officer report to the top-line managers of the FBO than that there be mandated a risk committee of independent directors in all cases. Deutsche Bank further believes that requiring a risk committee of independent directors is not always necessary to achieving appropriate risk management, and, indeed, because of the Depository Institution Management Interlocks Act and the analogous provision for systemically significant nonbank financial companies contained in Section 164 of the Dodd-Frank Act, many potential independent directors with industry expertise are precluded from service. The crucial condition to achieving enhanced risk management on an enterprise-wide basis is to permit the chief risk officer, who embodies the independence of the risk function, to have a greater report to the organization as a whole.

Moreover, as with the capital, liquidity, and stress testing requirements of the Proposal, Deutsche Bank believes that risk management prudential standards should apply only to SSOCs and Covered BHCs. Intermediate Holding Companies do not pose the same sort of risks as operating companies, and, as noted, it is the ultimate parent company that is the source of strength to its operating entities. Numerous risk committees will result in overlapping responsibilities, a duplication of efforts, and a lack of accountability, which will create the potential for inconsistencies without any appreciable systemic risk reduction purpose.

Based on these concerns, Deutsche Bank recommends that the Board only require a chief risk officer at the SSOC and Covered BHC level, and that the chief risk officer should be an individual that is separate and distinct from the business operations of the aforementioned entity to ensure adequate independence is maintained. Furthermore, the chief risk officer of the SSOC and Covered BHC, in the case of an FBO, should report to such entity's chief executive officer and into the risk management governance structure for the entire FBO. As set forth in the Associations' comment letter, risk management is a global undertaking directed by the FBO's head office; it is therefore entirely natural for a chief risk officer in the U.S. to have a report to the head office. In its final rules, the Board should affirmatively allow for such a result, so as not to unsettle the current governance schemes of many FBOs.

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Deutsche Bank appreciates the opportunity to provide the Board with the foregoing comments and recommendations regarding the Proposal.

Respectfully submitted,

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