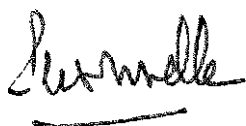


MICHEL BARNIER

Membre de la Commission européenne



Brussels, 18. 04. 2013
BD/cq D(2013) 810846

Dear Mr. Bernanke,

The European Commission closely follows regulatory developments in the area of financial services in the United States given the strategic role of your country as trade partner of the European Union and the close interconnections between our financial systems. We pursue a very fruitful informal Regulatory Dialogue, including in the area of financial services, and hopefully will also have the opportunity to engage with you in the near future in the negotiations for Transatlantic Trade and Investment Partnership

In this context, my staff have carefully analysed the Notice of Proposed Rulemaking (NPR) on Foreign Banking Organizations (FBOs) and its potential impact on EU banks with a commercial presence in the US. I would like to thank you for the very fruitful meeting we had during my last visit to the US and for the positive collaboration of your staff in the course of our assessment of the proposed FBOs rules. It has hopefully meant that our responses to your consultation have been constructive.

First of all, I want to stress that the Commission fully shares one of the general objectives of the NPR, which is to limit the risks that operations of large FBOs may pose to the US financial system, including through the implementation of effective cross-border resolution mechanisms. However, in line with the position taken by G20 leaders at the Washington Summit of 2008, I believe that, even though regulation remains first and foremost the responsibility of national regulators, the global nature of financial markets and the lessons drawn from the recent crisis clearly call for a globally-coordinated response. Indeed, as a central part of our response to the vulnerabilities unveiled by the crisis, the EU and the US have been at the forefront of promoting and implementing an internationally-harmonised approach to banking regulation.

On 20 March 2013, the European Parliament and the Council of the EU reached an agreement on the legislative package implementing the Basel III rules in the EU from the 1 January 2014. I am sure that you share my conviction about the importance of this achievement, which paves the way to a strengthened, more resilient and better-regulated banking sector. Together with the other pillars of the future Banking Union, including the Single Supervisory Mechanism, it will help enhance financial stability in the EU and in all countries where EU banks are active, including the US.

I now expect the US to come forward with final rules on the implementation of the Basel III agreement, thereby honouring the G20 commitment.

Mr. Ben BERNANKE
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If we have to maximize the effectiveness of the new international standards, it is more essential than ever to direct our common efforts towards ensuring their timely and consistent implementation in each jurisdiction, avoiding potential adverse cross-border effects. The EU is fully committed to this goal. As a consequence, in order to avoid unnecessary administrative burdens and duplicative regulatory costs on foreign institutions active in the EU, the EU framework exempts foreign banking subsidiaries from certain requirements, particularly in the area of consolidated supervision, provided, in the home jurisdiction, they are subject to a regulatory and supervisory framework equivalent to that of the EU. I would hope that the same approach is implemented also by all other jurisdictions, particularly those actively involved in the harmonization of banking rules at global level.

Against this background, certain elements of the FBOs' NPRs seem to be in substantial contradiction to the global regulatory convergence and could have a negative impact on the implementation of Basel III, jeopardizing and/or delaying the process. This may also prove detrimental for the integration of international capital markets, and for the global economic recovery.

In my opinion, the NPR would seem to represent a radical departure from the existing US policy on consolidated supervision of FBOs, in a way that may frustrate the efforts to ensure a consistent implementation of the Basel III standards across jurisdictions. Indeed, the proposed rules implement a 'one-size-fits-all' approach to consolidated supervision of FBOs, preventing US Supervisors from being able, under certain conditions, to rely on the capital provided by their parent and on supervision or regulation on a consolidated basis to which the latter is subject in its home jurisdiction.

The Intermediate Holding Company (IHC) requirement, which is one of the most important innovations of the NPR, depends exclusively on the amount of global and US assets of the institution, completely disregarding whether the latter is subject or not to a consolidated supervision in its home country equivalent to that of the US.

I fully acknowledge that, in certain circumstances, the IHC would provide an effective instrument to enhance the consolidated supervision over FBOs. However, its indiscriminate application, i.e. without linking it to a proper ex-ante equivalence test, would be against the global efforts towards harmonized rules in the area of prudential standards and cross-border resolution, and may have relevant negative impacts.

Let me in particular draw your attention to two possible unintended consequences deriving from its proposed application. The first refers to its impact on the level playing field between US domestic banks and FBOs; the second, to the potential reaction of other jurisdictions.

In my view, the IHC requirement, together with the application of heightened prudential standards at sub-consolidated level, entails relevant economic consequences for FBOs in terms of increased costs. In particular:

- Costs for establishing and maintaining the IHC and for ensuring compliance with governance and risk management standards;
- Costs for ensuring compliance with the enhanced prudential requirements at IHC level and in relation to the additional reporting burden;
- Costs for the reduced flexibility in carrying out capital and liquidity management strategies at group-wide level.

Such costs would be justified only if the FBOs were not subject, on a consolidated basis, to home country standards comparable to those of the US and if the US financial stability were at stake. In reality, despite the declared intention of putting FBOs on an equal competitive footing with US BHCs, the new framework may, instead, result in a competitive disadvantage for FBOs when considering their operations on a global basis.

We fear that the NPR could spark a protectionist reaction from other jurisdictions, which could ultimately have a substantial negative impact on the global economic recovery. Indeed, the potential retaliation effects of the new rules could end-up with a fragmentation of global banking markets and regulatory frameworks, with foreseeable consequences in terms of higher concentration of markets and lower levels of competition. These developments would translate into higher costs for banks, particularly those which are internationally active, with negative repercussions on their ability to finance the real economy and economic growth.

The "territorial" approach, as proposed in the NPRs, has a ring-fencing effect, which, besides fragmenting the global banking activity, also affects cooperation among regulators in the resolution of cross-border institutions. Such cooperation is essential not only in the implementation of the resolution strategies but also in their design. Trust among regulators is therefore essential to ensuring more efficient and effective resolution plans and living wills.

This "territorial" approach, in particular if replicated by other regulators, would instead preclude the possibility to resolve a G-SIFI in its entirety in a coordinated manner among different national authorities in accordance with the single point of entry strategy. This is clearly in contradiction with the international standards on cross-border cooperation in bank resolution adopted by the Financial Stability Board and endorsed by the G20.

Therefore, in light of the potential negative effects of the envisaged application of the FBOs' NPR, I would like to invite you to reflect further on their scope of application with particular regard to the conditions of the IHC requirement.

I firmly believe that, in the spirit of good cooperation between national supervisors, the new US FBOs rules should be better tailored and set precise conditions to allow, in certain circumstances, that due consideration is given to the principle of 'equivalent' consolidated supervision in the home country. This should, for instance, apply to the IHC requirement, which should be imposed only in cases where the FBO is not subject on a consolidated basis to home country standards comparable to those applied in the US.

This would bring, in my opinion, more consistency between FBO rules and other areas of the US financial reform, such as the final rules adopted for the implementation of Section 113 of Dodd-Frank, where this principle has been fully maintained. We hope the same might occur in the final rules on FBOs.

My staff is ready to work closely with your staff for the achievement of such objective.

Yours sincerely, *at his; ardwalement*



Michel BARNIER