**SOCIETE GENERALE**

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April 30, 2013

Robert deV. Frierson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

*Sent by electronic mail to: regs.comments@federalreserve.gov*

Re: Regulation YY: Enhanced Prudential Standards and Early Remediation Requirements for Foreign Banking Organizations and Foreign Nonbank Financial Companies; Docket No. 1438 and RIN 7100 AD 86

Dear Mr. Frierson:

Société Générale ("SG") appreciates the opportunity to provide comments to the Board of Governors of the Federal Reserve System (the "Board") on the proposed regulations (the "Proposed Rules")[1] published by the Board to implement Sections 165 and 166 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act")[2] for foreign banking organizations ("FBOs") and foreign nonbank financial companies.

SG supports the detailed comment letters filed by the Institute for International Bankers[3] and the Global Financial Markets Association.[4] We have chosen not to repeat all the points made in those letters. Instead, we have focused mainly on the issues most important to SG. In this letter, we suggest modifications to the asset thresholds for determining which FBOs are included in the scope of the Proposed Rules, express our concerns on the Proposed Rules' liquidity provisions, discuss the treatment of our Newedge subsidiary (which will be particularly

1 Enhanced Prudential Standards and Early Remediation Requirements for Foreign Banking Organizations and Foreign Nonbank Financial Companies, 77 Fed. Reg. 76,628 (December 28, 2012).
2 12 U.S.C. §§ 5365 and 5366.
3 Comment of the Institute Of International Bankers on the Notice of Proposed Rulemaking on Enhanced Prudential Standards and Early Remediation Requirements for Foreign Banking Organizations and Foreign Nonbank Financial Companies (April 30, 2013) ("IIB Letter").
4 Global Financial Markets Association (April 26, 2013). GFMA is a group representing The Association for Financial Markets in Europe, the Asia Securities Industry & Financial Markets Association and the Securities Industry and Financial Markets Association.



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difficult to incorporate into an IHC structure) and review the anti-competitive nature of some of the Proposed Rules.

**Scope of Proposed Rules**

SG is a French bank with its headquarters in Paris, France. SG maintains a global network of well over 3,000 branches, only two of which are in the U.S: a branch in New York ("SGNY") and a small branch in Chicago.[5] SG also owns a number of other entities in the U.S., including: SG Americas Securities, LLC ("SGAS"), a registered broker-dealer and primary dealer; Lyxor Asset Management, Inc., a registered investment advisor; SG Equipment Finance USA Corp., an equipment finance company; CGI North America Inc., a boat finance company; and Societe Generale North America, Inc. ("SGNA"), a commercial paper issuer. In addition SG owns 50% of Newedge Group, a French entity that owns 100% of Newedge USA, LLC ("Newedge"), a U.S. registered futures commission merchant, swap dealer and broker-dealer. Based on the calculation methodology set out in the Proposed Rules, SG has more than $50 billion of assets in the U.S.

The Act requires the Board, in establishing enhanced prudential standards for FBOs, to take into account differences among financial institutions based on their business and risk profiles in the U.S.[6] Congress provided the Board several pages of considerations for prescribing prudential standards for FBOs[7] and, to be clear of its intent, entitled subsection 165(a)(2) of the Act "Tailored Application."[8] SG does not believe that the Proposed Rules are calibrated to follow these Congressional requirements. The Proposed Rules make only a cursory effort to identify the risk that each FBO poses to the U.S. financial system and therefore will unduly burden the majority of FBOs, including SG. Even among the largest of the global financial institutions, there are a variety of U.S. footprints and risk profiles, with some FBOs not being sufficiently large and active in the U.S. to warrant the level of intensive regulation created by the Proposed Rules. A rigorous analysis of FBOs' financial activities in the U.S. would show that only a few of those have activities so significant as to pose a systemic risk to the U.S. Instead of adopting a rigid, one-size-fits all approach, the Board should study the composition of the many FBOs that will be affected by the Proposed Rules and write regulations that impose the most onerous requirements only on systemically important nonbank financial institutions ("SIFIs") in the U.S. and FBOs that it determines are under-regulated in their home countries. This approach would be consistent with the current SOSA framework that allows the Board to assess specifically the historic and current strength of an FBO based on support from its parent company or head office.

SG urges the Board to make a number of scoping revisions to the Proposed Rules. First, we suggest that there be more than two categories of regulated entities. Currently, the Proposed Rules essentially divide FBOs into two groups: FBOs with more than $10 billion of global assets and FBOs with more than $50 billion of global assets. Yet there is no clear logic that correlates being a large bank outside of the U.S. with the need for additional regulation inside the

[5] SG also maintains an agency in Dallas and a representative office in Houston.
[6] See 12 U.S.C. 5365(b)(3).
[7] See 12 U.S.C. 5323.
[8] See 12 U.S.C. 5365(a)(2).

U.S., and the Proposed Rules provide no explanation. SG suggests that the Proposed Rules focus on asset ownership within the U.S., as this is what is most relevant to the safety and soundness of the U.S. financial system. Large banks with small operations in the U.S. should not be punished simply for being large if such banks do not have systemic presence in the U.S.

Second, the Board should not simply look at amounts of assets in the U.S. but the nature of such assets and the type of legal entity in which they are held. FBOs, such as SG, that do not maintain retail operations or an insured depositary institution in the U.S. should be inherently less of a concern to the Board than FBOs with retail operations, and this is one of the features that Congress requires the Board to review in imposing FBO regulation.[9] Assets held in heavily regulated entities like broker-dealers should not be counted in determining the amount of U.S. assets of an FBO, or at least should be weighted less prominently than assets held in non-regulated entities. Certain types of assets should not be counted in the U.S. asset calculation at all. For example, assets posted at the Federal Reserve discount window, assets held as part of a primary dealer operation and assets pledged to state banking regulators should be excluded from the calculations. Holdings of cash or U.S. treasury securities should also be excluded. Liquid, secured short-term financing outstanding with unaffiliated third parties should be encouraged by the Board under the same logic in the Proposed Rules that discourages inter-company transactions. Overall, the Proposed Rules should be sufficiently flexible to allow the Board to focus its supervisory resources on the largest FBOs that could pose systemic risk in the U.S.

Third, the Board should include a formal procedure that permits an FBO to demonstrate that certain of the provisions of the Proposed Rules are not required due to, among suggested factors, (a) the size, character or lack of systemic importance of the FBO's U.S. operations, (b) resolvability of the FBO's U.S. operations under U.S. insolvency law, (c) the extent to which the FBO's home country supervision addresses U.S. financial stability concerns, (d) historical strength of support from their home country's headquarters and (e) whether an FBO controls an insured depositary institution.[10]

In our case, SG is a large global bank with a modest U.S. footprint. As of December 31, 2012, our U.S. assets held outside SG's U.S. branches – in other words those that would go into the IHC – were $86 billion. Our U.S. assets constitute only 11% of SG's total global asset base of $1,651 billion. A breakdown of our assets that would comprise the IHC reveals that approximately 80% of are of a nature unlikely to cause serious or systemic risk to the U.S. financial system. SG therefore believes that, notwithstanding our large global footprint, our U.S. business presence does not warrant the most onerous application of the Proposed Rules.

SG understands that the Board wishes to require the largest foreign-owned broker dealers to maintain extra capital. Leaving aside whether the Board has the regulatory authority to set broker-dealer capital standards, we believe the Board should specifically assess and evaluate the assets and activities of individual broker-dealers before imposing the Proposed Rules upon all of them. With a total of $36 billion of assets. $12 billion of which are held for our Primary Dealer operation,[11] SGAS is hardly an entity that poses systemic risk to the U.S. Moreover, broker-

[9] See 12 U.S.C. 5365(b)(3)(A)(ii).

[10] This idea is further described in the IIB Letter at Part I(C)(1).

[11] As of December 31, 2012.

dealers are already sufficiently regulated entities in the U.S. If the Board is concerned that U.S. broker-dealer regulation is somehow insufficient, it should use the Financial Stability Oversight Council to resolve the issue rather than simply imposing additional regulatory burdens upon the parent companies of foreign-owned broker-dealers.

**Liquidity**

The Proposed Rules' liquidity provisions would require an FBO to maintain separate liquidity buffers for its IHC and U.S. branches. Each would be required to hold a liquidity buffer sufficient to meet its net stressed cash flow needs for 30 days. Internal and external stressed cash flows would be netted against one another; however, short-term funding to the home office would not be permitted to offset short-term obligations. The proposed buffer would result in the trapping of liquidity within the U.S. The liquidity requirements in the Proposed Rules inexplicably exceed those set forth in the Basel III framework, and will result in the excess (i.e., trapped) liquidity not counting as part of SG's global liquidity buffer.[12] SG will accordingly have to maintain a larger overall liquidity buffer. SG suggests that if the Board finally determines to impose separate liquidity measures over an IHC, the Board should do so consistent with Basel III liquidity coverage ratio standards.

However, SG believes that the assumptions underpinning the Proposed Rules' liquidity requirements should be reexamined. First, the Board's assumption that FBOs will not support their U.S. operations during a time of crisis simply does not ring true for SG. Not only is this assumption incorrect, we fear it will be damaging to United States-European regulatory relations as it sends a clear message of distrust from the Board to its European counterparts and to the Basel Committee, which the Board has participated as part of the G-20 group of banks. The assumption will have the effect of discouraging cross-border cooperation and further isolating U.S. regulators from their European counterparts. European regulators may respond with rules that lead to additional fragmentation of the global financial system.[13] The Act specifically requires the Board to consult with its foreign counterparts;[14] to SG it is clear that Congress did not intend for the Board to act unilaterally in setting prudential standards for FBOs.

Second, in our own case, SG did not abandon its U.S. operations during the most severe European financial crisis in recent memory, even when misleading press reports drove SG's five-year CDS spread as high as 440 bp in September 2011.[15] Instead, SG continued complete and full support of its U.S. operations. European FBOs generally had to manage their U.S. dollar businesses in a constrained economic environment, but remained in the U.S. SG is concerned that the Proposed Rules could actually cause FBOs to pull back from the U.S. to a greater extent than during the European financial crisis.

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[12] See Basel Committee, Basel III: The Liquidity Coverage Ratio and Liquidity Risk Monitoring Tools, at para. 36-37. The Basel III liquidity coverage ratio limits a bank's ability to take account of liquidity at regulated subsidiaries. Thus, SG will not be able to count the liquidity in the IHC as part of its overall global liquidity buffer.
[13] It has been estimated that increased fragmentation of the global financial industry will result in a 2-3% drag on return on equity. See Morgan Stanley, "Wholesale & Investment Banking Outlook; Global Banking Fractures: The Implications" (April 11, 2013), at 2.
[14] See 12 U.S.C. 5313(b)(2)(A).
[15] SG's 5-year CDS spread was at 192 as of April 29, 2013.

Third, to avoid trapping liquidity in the U.S., FBOs may seek to move business to non-U.S. booking locations and funding offshore, which is a result perhaps not intended by the Board. Especially for a bank like SG, where U.S. operations are such a small part of the global business plan, SG will be very careful to enter into business in the U.S. that could materially prohibit SG from prudent liquidity management elsewhere.

Finally, by setting stricter local rules on liquidity than those required by the Basel III framework, and indirectly raising the costs of dollars for FBOs, the Proposed Rules would interfere with SG's ability to manage liquidity on a global basis. Through SGNA, our U.S. commercial paper program, SG raises U.S. dollars in the U.S. to fund our global dollar-denominated lending and financing activities.[16] Some of these operations are based in Paris, which means that funds raised by SGNA are typically transferred to our Paris treasury operations. Funds held in Paris may be used to lend to U.S. customers, as we deal with many multinational U.S. customers through our Paris office. Prior to the 2011 financial crisis, SG's U.S. operations were, through SGNA, a net lender of dollars to the SG Paris. In 2011, SG's ability to raise dollar funding in the U.S. was impaired when some U.S. investors temporarily abandoned investments in FBOs. During this period, SG Paris supported its U.S. operations by helping to finance SGNY even though it was very costly to do so. If, due to the calculation of the Proposed Rules' liquidity coverage ratio policy, SG Paris is essentially deprived of its ability to raise dollar funding, the funding costs of our global U.S. dollar operations will be increased.[17] If funding our global business in the U.S. becomes too expensive, SG, like other FBOs, may be forced to limit its U.S. dollar needs to a minimum, which will inevitably decrease its operations in the U.S. and with U.S. customers. Faced with the prospect of a reduced footprint in the U.S. dollar market, a reduction in the size of SG's U.S. operations cannot be ruled out. Nor can the development of a robust Eurodollar market, which would not be beneficial to the U.S. economy.

**Newedge**

As noted, SG indirectly owns 50% of Newedge Group. Newedge Group operates as a consolidated, global company with Newedge USA, LLC ("Newedge") as it main operating subsidiary in the U.S. Newedge does not engage in traditional banking services; the large majority of its business is comprised of exchange-traded and cleared activities. As such, Newedge is a fully regulated U.S. broker-dealer, futures commission merchant and swap dealer, and, as a subsidiary of two FBOs, has regular meetings with bank supervisors as well.[18] These functional regulators already supervise, in detail, the fundamental risks related to Newedge's business: liquidity, customer protection, capital, risk management and supervision.

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[16] Currently, SGNA has $16 billion in outstanding issuances.

[17] Our analysis indicates that raising dollars in the Eurodollar market would be significantly more expensive than using the U.S. market, as SG currently does. Additionally, a recent J.P. Morgan research report estimated that FBOs required to fund dollar needs locally would cost FBOs 100 bps (45%) more than current costs. J.P. Morgan Global Equity Research Report, "Global Investment Banks: Can Universal Banking Model Survive the New Wave of Uncoordinated IB Regulations?" (April 11, 2013), at 13.

[18] The Board maintains oversight over Newedge through SG and Credit Agricole S.A., which owns the other 50% of Newedge Group, which is supervised by the French prudential regulator, *Autorité de contrôle prudentiel.* Newedge meets quarterly with examiners from the Federal Reserve Bank of New York and has been the subject of two examinations during the past three years. Adding another layer of prudential regulation would, at best, be duplicative.

Moving Newedge into one or more IHCs would break up Newedge Group's global operating model, as Newedge's U.S. operations would be severed from the Newedge Group. This would cause significant harm to Newedge's business, accounting, risk management and control functions, which currently operate on a consolidated basis within Newedge Group. Fitting Newedge into an IHC would require a complete de-consolidation between Newedge and Newedge Group. Newedge would, in essence, need to function as a stand-alone U.S. entity, thus losing the benefits it achieves by operating as a consolidated global entity. We believe this could actually erode risk management at Newedge rather than improve it.

Our 50% ownership of Newedge thus poses a special problem for inclusion in the IHC structure. It would be unfair to impose the full panoply of the Proposed Rules on Newedge twice but also incorrect to attribute 100% of Newedge's assets to each of its shareholders. Attributing only 50% of Newedge's assets to each shareholder is our preferred methodology, but we understand this is difficult to calculate. SG requests that the Board consider special arrangements for entities, like Newedge, that are only partially owned by an FBO. The Proposed Rules should give the Board flexibility to review, on a case-by-case basis, non-standard ownership structures and work with FBOs to design a plan of supervision that provides the Board the oversight it needs without being disruptive to the functioning of the businesses within the Board's supervision.

One potential solution, both for Newedge and more generally for well-capitalized FBOs operating in compliance with Basel standards, would be for the Board to not require an actual IHC. Instead, the Board should permit the establishment of a "virtual IHC,"[19] which would permit a prudential consolidation of SG's 50% stake in Newedge into SG's IHC. A virtual IHC, essentially a regulatory concept, would permit the Board to have the consolidated U.S. information that the Proposed Rules require without the problematic and costly structural changes of the IHC. While SG believes the Board already has sufficient supervisory authority over all entities that would be required to be placed in the IHC, SG suggests that the Board modify the Proposed Rules to permit a virtual IHC, at least for FBOs that are not designated as SIFIs.

**FBO Competitive Equality**

The Act requires the Board to give due regard to principles of national treatment and competitive equality, and to take into account the extent to which an FBO is, on a consolidated basis, subject to home country standards that are comparable to those applied to financial companies in the U.S.[20] It is hard to discern how the Proposed Rules meet this standard, as they discriminate in numerous ways against FBOs as compared to U.S. bank holding companies, creating significant competitive equality issues. The requirement to set up an IHC is at the source of many of these issues. U.S. banks, although subject to similar regulatory requirements as IHCs, are regulated on the basis of their global operations, while an FBO's IHC would be regulated on the basis of only its U.S. operations.

[19] This idea is further described in the IIB Letter at Part I(F).
[20] See 12 U.S.C. 5365(b)(2)(B).

SG is particularly concerned about the early remediation triggers imposed on FBOs and IHCs. These requirements apply not only to the IHC but to the FBO itself on a global level. FBOs will want to manage their capital to avoid ever triggering the Level 1 or 2 requirements. For SG, the Level 2 leverage requirement will have the effect of imposing on SG at Group level a leverage ratio requirement that is 40% higher than the Basel leverage ratio requirements. Maintaining such an extraordinary additional amount of capital would have a direct impact on the amount of credit SG could extend outside of the U.S., in France and elsewhere. The Proposed Rules would effectively require SG to cut back on home-country euro-financing in order to secure our relatively small U.S. activities and thus will have a material, unwarranted extra-territorial impact on SG. This is one of the many examples of costs that FBOs alone will face under the Proposed Rules. SG understands that the Board has a legitimate interest in protecting the U.S. financial system, but we ask that, as Congress intended, FBOs should be treated fairly.

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SG appreciates having the opportunity to comment on the Proposed Rules. We hope these comments have been constructive and will help the Board in the finalization of its important Proposed Rules. SG would be pleased to meet with the Board at any time to discuss our comments.

Respectfully,

Laura Schisgall
General Counsel