3

Satterfield, Kevin

From: Gellasch, Tyler (Levin) [Tyler_Gellasch@levin.senate.gov]
Sent: Friday, August 28, 2009 9:50 AM
To: Regs.Comments
Cc: Bean, Elise (HSGAC)
Subject: Proposed Interagency Guidance - Funding and Liquidity Risk Management
Attachments: 8-28-09 comment to occ re liquidity risk.pdf

Please see the attached comment letter.

Ty Gellasch, Counsel
Office of Senator Carl Levin
269 Russell Senate Office Building

CARL LEVIN
MICHIGAN

United States Senate

WASHINGTON, DC 20510-2202

August 28, 2009

Filed via electronic mail at regs.comments@occ.treas.gov

Office of the Comptroller of the Currency
250 E Street, SW Mail Stop 2-3
Washington, DC 20219
Attn: OCC-2009-0009

Re: Proposed Interagency Guidance on Funding and Liquidity Risk Management
Docket ID No. OCC-2009-0009

Dear Sir or Madam:

The purpose of this letter is to express support for the Proposed Interagency Guidance on Funding and Liquidity Risk Management ("Guidance"). This proposed Guidance would help bring U.S. banking regulations in line with the Basel Committee on Banking Supervision's "Principles for Sound Liquidity Risk Management and Supervision" and promote uniform U.S. regulatory expectations on sound practices for managing liquidity and funding risks.

For the past nine months, the U.S. Senate Permanent Subcommittee on Investigations, which I chair, has been reviewing aspects of the financial crisis that damaged U.S. and world financial systems and economies last fall. This financial crisis was exacerbated by inadequate liquidity risk management practices at many U.S. financial institutions. Some institutions failed. Others would almost certainly have done so, if not for the unprecedented and costly intervention by the U.S. government. In too many cases, the losses arising from these financial institutions' inadequate risk management practices were picked up by the taxpayers.

Rather than allow financial institutions to continue to benefit from taxpayer-financed rescues, regulators should require these institutions to dramatically improve their risk management practices and internalize the costs associated with their risks. With respect to liquidity risks, the proposed Guidance would take important steps toward that end.

The proposed Guidance outlines eight "critical elements" to sound liquidity risk management:

- Effective corporate governance;
- Appropriate strategies, policies, procedures, and limits to manage liquidity risk;
- Comprehensive liquidity risk measurement and monitoring systems that are appropriate for the institutions' complexity and business;
- Active management of intraday liquidity and collateral;
- Diverse mix of existing and potential funding sources;

- Adequate levels of highly liquid securities that can be used to meet liquidity needs in times of stress;
- Comprehensive Contingency Funding Plans (CFPs) that address adverse liquidity events and emergency cash flow requirements; and
- Internal controls and audit processes to determine the adequacy of the liquidity risk management process.

These elements are unquestionably essential for sound liquidity risk management. Many prudent financial institutions may have already implemented some or all of them; others will need sustained regulatory oversight before they will make the necessary investments in time and resources.

While the application of each essential element should be appropriately tailored to the size and business of each financial institution, regulators will need to develop uniform, clear, and useful examination measures to gauge and track the extent to which each institution has complied with these elements. In addition, these measurements should be designed to enable regulators to evaluate local, regional, and system-wide liquidity risks.

The proposed Guidance could also be strengthened in several respects. First, to ensure its effectiveness, the proposed Guidance should be viewed, not as aspirational, but as providing essential minimum standards for U.S. financial institutions. The procedures specified in the Guidance should be viewed as a mandatory floor—not ceiling—in federal regulatory expectations for sound liquidity risk management.

Second, to the extent that the proposed Guidance would require financial institutions to have appropriate strategies, policies, procedures, and limits to manage liquidity risk, it should also require these financial institutions to appropriately match liquidity needs with funding sources and instrument types. The proposed Guidance correctly encourages financial institutions to diversify the timing and types of funding sources. But the Guidance should go a step further and instruct financial institutions to tailor their strategies, policies, and procedures, as appropriate, to match longer-term financial commitments and obligations with longer-term, stable funding sources. The Guidance should state explicitly that financial institutions should not be overly reliant on volatile short-term financing for long-term obligations.

Finally, the proposed Guidance should be viewed as addressing only one aspect of a risk management process that requires additional protective measures. In addition to instructing financial institutions to implement liquidity risk management policies and procedures, for example, regulators should take the next step and issue a rule or guidance requiring higher liquidity reserves for specified high risk activities. Higher liquidity reserves could be mandated, for example, for: (a) "naked" credit default swaps or other derivatives where the financial institution does not have an ownership interest in or financial exposure to the referenced assets; (b) derivatives that are not cleared or rely on non-cash collateral; (c) derivatives undertaken by a financial institution on a proprietary basis and not for a client; (d) derivatives that are novel or highly complex; and (e) transactions involving assets that are kept offshore. Pending issuance of such a rule or guidance, the Guidance being proposed here could be strengthened by providing specific examples of high risk activities and stating that the liquidity risk management policies and procedures being developed by financial institutions should be designed to require higher liquidity reserves for such higher risk activities. Requiring higher liquidity reserves for specified higher risk activities would help ensure that the risk management policies and procedures being put into place would be sufficient to protect the U.S. financial system against excessive liquidity risk.

Thank you for the opportunity to comment on these important issues.

Sincerely,

Carl Levin

Carl Levin