Office of the Superintendent of Financial Institutions Canada
Bureau du surintendant des institutions financières Canada

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DEPARTMENT OF THE TREASURY
Office of the Comptroller of the Currency
12 CFR Part 44
Docket No. OCC-2011-0014
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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
12 CFR Part 248
Docket No. R-1432
RIN: 7100 AD 82]

FEDERAL DEPOSIT INSURANCE CORPORATION
12 CFR Part 351
RIN: 3064-AD85

SECURITIES AND EXCHANGE COMMISSION
17 CFR Part 255
Release No. 34-[•]; File No. [•]
RIN: 3235-AL07

Subject: **Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds**

The Office of the Superintendent of Financial Institutions Canada (OSFI) is the prudential regulator and supervisor of Canadian banks and federally-regulated non-bank deposit-taking institutions, insurance companies and pension funds. Given that Canadian banks have significant operations in the United States, OSFI welcomes the opportunity to comment on the above proposed restrictions, commonly known as the "Volcker Rule", whose aim is to restrict banking entities' ability to engage in proprietary trading and their relationships with hedge funds and private equity firms.

The global financial crisis and the ensuing failure of many financial institutions have left a legacy of trillions of dollars in lost economic output, millions of lost jobs and higher fiscal deficits in many countries around the world including the United States. G-20 leaders have in response agreed on a comprehensive package of financial sector reforms to reduce the risk of future crises and to strengthen banking systems around the world. These reforms are being supplemented by additional actions in many jurisdictions to strengthen their domestic banking systems including in the US. Thus, OSFI strongly supports the objectives of the proposed restrictions on banking entities, namely to ensure that the trading activities of banks operating in the US and their relationships with hedge funds and private equity firms do not undermine the financial condition of those banks, nor the stability of the US financial system as a whole.

The proposed restrictions could hinder foreign bank risk management practices...

Despite those laudable objectives OSFI is concerned that the current draft of the proposed restrictions could inadvertently hinder the ability of foreign financial institutions to efficiently manage their risks, thereby potentially undermining the financial condition of those entities and the systemic stability of foreign financial systems. This is an especially acute concern for Canadian banks and the Canadian financial system more broadly given the deep inter-linkages that have existed for many decades between the Canadian and US financial systems.

Canadian financial institutions use US-owned infrastructure to conduct financial transactions in support of their market-making activities in Canada, and in their risk management activities more broadly in support of their Canadian and US banking operations. Some obvious examples include:

- Active reliance on the systems operated by The Depository Trust & Clearing Corporation (DTCC) for clearing and settlement of transactions involving US securities;
- Regular use of US financial exchanges for transacting futures and options derivatives involving both Canadian dollar and other currencies to manage financial risk exposures; and
- The ubiquity of other US-owned infrastructure in global financial markets, such as Bloomberg and the custodial services provided by some major US banking groups.

US financial institutions and US-owned financial system infrastructure thus play critical roles in key global markets. As a result, OSFI is concerned that the draft regulations may have the unintended consequence of significantly impeding Canadian and other foreign financial institutions' ability to manage their risks in a cost-effective manner, which could give rise to prudential concerns in Canada and abroad. In other words, OSFI would not wish to see US regulators taking actions that may enhance the stability of their financial system at the cost of undermining the stability of other systems around the world.

... and they could undermine the ability of foreign banks to efficiently manage their liquidity

OSFI understands that the proposed restrictions would only allow proprietary trading by banking entities in US Treasury, state, and municipal general, limited, and pass-through obligations. However, Question 122 of the consultative document asks whether *US agencies should adopt an additional exemption for proprietary trading in the obligations of foreign governments and/or international and multinational development banks under section 13(d)(1)(J)of the BHC Act? If so, what types of obligations should be exempt? How would such an exemption promote and protect the safety and soundness of banking entities and the financial stability of the United States?*

OSFI strongly believes additional exemptions from the restrictions on proprietary trading should be given to foreign government securities, at least for banking groups whose parent bank is located outside of the US. Many foreign banks play important market-making roles in the trading of government securities in their home jurisdictions. They also actively rely on government securities of their home jurisdiction to efficiently manage their liquidity and funding requirements at a global enterprise-wide level; a practice that will be further reinforced in the future by new bank liquidity requirements that have been proposed by the Basel Committee on Banking Supervision. Thus, OSFI believes a failure to include these additional exemptions at least for banking entities whose parent bank is located outside of the US would undermine the liquidity of government debt markets outside of the US and could significantly impede the ability of foreign banks to efficiently manage their liquidity and funding requirements at an enterprise-wide level.

In closing, OSFI applauds the tremendous amount of work being done by US agencies to strengthen the US banking system and reduce the risk of it contributing to a future financial crisis. But in implementing reforms we urge the agencies to be mindful of the fact that US financial institutions and markets (and their supporting infrastructure) are deeply connected to the broader global financial system. Indeed, in many cases they represent core segments for global financial intermediation. Thus, when implementing reforms like the Volcker Rule it is important to not only focus on the implications for the US financial system, but also to take care that these restrictions do not give rise to prudential issues for other jurisdictions.

Yours very truly,

Mark Zelmer

For Julie Dickson
Superintendent
Office of the Superintendent of Financial Institutions Canada