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The Honorable Randal K. Quarles
Chair of the Financial Stability Board
Bank for International Settlements
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17 May, 2019

Re: ***Threats to financial stability resulting from widespread ring-fencing***

Dear Chairman Quarles:

Many jurisdictions around the world are now finalizing implementation of the post crisis regulatory reforms agreed to by the G20 nations. The IBFed[1] notes its concern that there are a growing number of instances where jurisdictions are introducing variations of the agreed reforms intended to protect their own jurisdiction, for example by ring-fencing. Such variations are drivers of market fragmentation, undermine the international cooperation of the last decade and inhibit the full, timely and consistent implementation of the post-crisis international agreements reached by G20 standard setting bodies.

Cross-border business activities and efficient movements of capital and liquidity are essential for long-term global economic growth. One of the key IBFed priorities is to support the cooperation between countries, with the goal of fostering a common supervisory framework for credit institutions. As such, we are particularly concerned with the public consultation issued on April 8th, 2019 by the Federal Reserve Board (FRB) of the United-States (U.S.) that was intended to better align rule for international banks relative to their risk profile in the U.S.[2] The consultation proposes changes to rules for foreign banking organizations (FBO) that are disproportionate to the risks these institutions pose to the U.S. financial system[3],

[1] The International Banking Federation (IBFed) was formed in 2004 to represent the combined views of our national banking associations. The IBFed collectively represents more than 18,000 banks, including more than two thirds of the largest 1000 banks in the world. IBFed member banks play a crucial role in supporting and promoting economic growth by managing worldwide assets of over 75 trillion Euros, by extending consumer and business credit of over 40 trillion Euros across the globe, and by collectively employing over 6 million people. The IBFed represents every major financial centre and its members' activities take place globally. This worldwide reach enables the IBFed to function as a key international forum for considering regulatory and other issues of interest to the global banking industry. For more information visit: www.ibfed.org

[2] Please see : https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190408a.htm

[3] Please see : https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190408a.htm

including with regards to their U.S. branches. As a result, the proposed changes do not properly balance home and host country regulations. Any measurement of the proposed risk-based thresholds needs to value and recognize the safety and soundness of the home-country regulation at parent level. Any approach that includes inter-affiliate transactions in the risk-categorization metrics as well as any additional branch liquidity requirements (including the use of branch data to determine a requirement for an intermediate holding company, or IHC) would only serve to accelerate the trend towards ring-fencing.

We understand the need for jurisdictions to have the ability to identify and respond to financial vulnerabilities in a timely manner. The capacity to address risks and to protect depositors, consumers and tax-payers is essential for financial stability. The IBFed fully supports promotion of international cooperation in order to increase financial stability. However, we are concerned that the rise of widespread ring-fencing, where jurisdictions require dedicated pools of local capital and liquidity, will not only dampen the progress of the G20 policies, but it may even harm economic resilience and financial stability. Moreover, we note that ring-fencing policies are much more costly as a whole for many stakeholders than a harmonized international regulatory framework which provides flexibility to deploy capital and liquidity resources where needed.

The fragmentation of the international supervisory framework might amplify financial instability as new digital competitors enter the market. The decade ahead is crucial for banks as fast-paced “fintechs”[4] will affect the banking industry and the activities of supervisors. The emerging fragmentation represented by various developments around the world is disappointing. This will not only result in the sub-optimal allocation of capital and liquidity, but it will also increase the cost of financing growth. We are also concerned that further knock-on effects will result when other jurisdictions such as Europe (through their proposed intermediate parent undertaking), or the UK (if Brexit were to become a reality), respond in kind to these measures.[5]

Cooperation between stakeholders, including both home and host country regulators and resolution authorities, is crucial for growth and the efficient use of capital and resources. International fora like the FSB and the Bank for International Settlements (BIS), facilitated by Memorandums of Understanding (MoUs), help to establish trust and cooperation - two foundational conditions that make finding a reasonable middle ground between regulators possible. Bypassing diplomacy and international cooperation in favor of developing a unilateral jurisdictional approach is counter-productive. An efficient allocation of resources to support growth and the need to minimize losses in a stress period are two worthy goals made possible by an internationally agreed set of standards which are cooperatively implemented by home and host regulators.

We also support the FSB’s drafting of a report on market fragmentation which will be delivered to G20 this June[6]. The report could be influential in promoting the balance between

[4] Also known as « technology-driven innovation in financial services »

[5] Please see the following speech (especially the reference of “the prisoner’s dilemma”) made by Ryozo HIMINO, Vice Minister for International Affairs of JFSA : https://www.fsa.go.jp/common/conference/danwa/20181026.pdf

[6] Please see : http://www.fsb.org/wp-content/uploads/P120219.pdf

the flexibility required by an internationally open economy, based on a multilaterally agreed supervisory framework, and the more prescriptive national requirements defined by each domestic authority, which, in our view, ultimately have the effect of reducing the sound allocation of capital and liquidity between the various jurisdictions. As you have noted, most recently in your letter[7] to the G20 Finance Ministers and Central Bank Governors, ahead of the meeting held in Washington DC in early April 2019, it is of the utmost importance to continue to engage in the reinforcement of an integrated and resilient global financial system. We also agree that market fragmentation is harmful to financial stability. This issue is a key priority for the Japanese G20 Presidency and we believe it should continue to be carefully explored.

We thank you for taking our comments into consideration, and look forward to future discussions on these issues.

Yours sincerely,

Hugh C Carney

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[7] Please see : http://www.fsb.org/2019/04/fsb-chair-writes-to-g20-finance-ministers-and-central-bank-governors/