Northern Trust Corporation
50 South LaSalle Street
Chicago, Illinois 60603
(312) 630-6000

Northern Trust

October 15, 2009

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, DC 20219
Attn: ID OCC 2009-0012
RIN 1557-AD26

Ms. Jennifer J. Johnson
Secretary
Federal Reserve Board
20th Street and Constitution Avenue, NW
Washington, DC 20551
Docket No. R-1368

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Attn: RIN 3064-AD48

Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attn: ID OTS 2009-0015
RIN 1550-AC36

Re: Risk Based Capital Guidelines; Capital Adequacy Guidelines; Capital Maintenance: Regulatory Capital; Impact of Modification to Generally Accepted Accounting Principles: Consolidation of Asset-Backed Commercial Paper Programs; and Other Related Issues

Ladies and Gentlemen:

Northern Trust Corporation (Northern Trust) appreciates the opportunity to comment on the above mentioned proposal (Proposal) that would (1) modify the capital adequacy frameworks to eliminate the exclusion of certain consolidated asset-backed commercial paper programs from risk-weighted assets and (2) provide a reservation of authority to permit the Agencies to require banking organizations to treat entities that are not consolidated under accounting standards as if they were consolidated for risk-based capital purposes.

Northern Trust is a NASDAQ-listed financial holding company headquartered in Chicago, Illinois, with consolidated assets of approximately $75 billion and $559 billion in assets under management as of June 30, 2009. Northern Trust conducts business in the United States (U.S.) and internationally through its banking subsidiaries, trust companies and various other domestic and foreign nonbank subsidiaries. In Northern Trust's asset management business, the Corporation solely acts as asset manager for its clients (e.g. pension and 401k plans) through its institutional funds, which include collective defined benefit and defined contribution investment funds. For providing these services, Northern Trust receives management fees or, much less frequently, performance fees.

We appreciate the regulators proposing changes to the risk-based capital framework in order to clarify how accounting standards should apply to the banking industry. Our comments on certain issues raised by the Agencies within the Proposal in addition to other observations and comments are provided below.

Question 1: Which types of VIEs will banking organizations have to consolidate onto their balance sheets due to the 2009 GAAP modifications, which types are not expected to be subject to consolidation, and why? Which types are likely to be restructured to avoid consolidation?

As an asset manager and custodian, Northern Trust does not participate in the asset securitization market and therefore, is not the sponsor of such entities nor active in selling loans into such entities which would be expected to be subject to potential consolidation under the 2009 GAAP modifications within FAS 166 and FAS 167. Northern Trust is concerned, however, that the 2009 U.S. GAAP modifications could potentially result in the consolidation of certain types of sponsored funds onto an asset manager's balance sheet.

Under existing U.S. GAAP, FASB Interpretation No. 46 (R), asset managers were not required to consolidate sponsored funds onto their balance sheets unless they were deemed the primary beneficiary of the fund – meaning that they carried the majority of the risks and rewards, which is rarely the case. FAS 167 could potentially force asset managers to consolidate trillions of dollars of assets onto their balance sheets, even though fees are competitively market based and there is no associated risk of loss or where risk of loss is limited to a minimal seed capital investment in the fund. There are numerous interpretive issues that are currently being discussed within the industry which, depending on the ultimate outcome, could have significant bearing on the types of funds that ultimately end up being subject to consolidation under this guidance.

The types of sponsored funds at highest risk of consolidation for the asset management industry are those with performance fees or fee sharing arrangements which could include, but are not limited to, securities lending collateral pools and private equity funds or other commingled products with performance fees.

Requiring asset managers to consolidate sponsored funds under FAS 167 would not only obfuscate core operating results and likely force analysts and investors to rely on supplemental non-GAAP measures in order to determine core operations, but would also be inconsistent with the original intent of the revised accounting guidance. Based on preliminary assessments, we do not believe that FAS 167 will result in the consolidation of any significant sponsored funds. As discussed above, however, there are many open interpretive issues which, depending on their ultimate outcome, could result in the consolidation of material sponsored funds onto the balance sheets of asset managers. In the event that the consolidation of a material amount of sponsored funds were to be the ultimate outcome of FAS 167 and if the capital requirements as proposed by the Agencies were to become final, the asset management industry would have to take a hard look at all such structures to determine what changes could be made to allow these businesses to continue in a profitable manner.

Question 2: Are there features and characteristics of securitization transactions or other transactions with VIEs, other SPEs, or other entities that are more or less likely to elicit banking organizations' provision of non-contractual (implicit) support under stressed or other circumstances due to reputational risk, business model, or other reasons? Commenters should describe such features and characteristics and the methods of support that may be provided. The Agencies are particularly interested in comments regarding credit card securitizations, structured investment vehicles, money market funds, hedge funds, and other entities that are likely beneficiaries of non-contractual support.

During the recent financial crisis, various financial institutions, including Northern Trust, entered into capital support arrangements with certain registered investment companies, UCITS and unregistered short-term investment pools in order to maintain net asset values of $1.00 and provide financial stability to the entities and their investors.

Not all fund types carry the same level of potential for reputation risk and therefore, do not have the same likelihood of being provided non-contractual support. High alpha funds are viewed as having minimal reputation risk. In these funds, clients expect the asset manager to go further out on the risk curve in order to generate higher returns – the clients expect higher risk and accept that returns for these funds can be more volatile than for other funds.

Non constant dollar liquidity funds are viewed as having minimal to low reputation risk. These products serve as high-alpha cash products for some clients and securities lending collateral vehicles for other clients. For clients using these funds as cash vehicles, their decision to seek greater return helps to mitigate possible reputation risk issues. In the case of securities lending collateral, the reputation risk is higher, but is mitigated by the industry-wide experience with securities lending collateral over the last twelve months and the management of these funds within their stated investment guidelines.

Securities lending pools are viewed as having low to moderate reputation risk. Given market events of the last two years, clients in these pools are more educated about the potential volatility of the NAVs of the pools than they were historically and understand and accept that there is some level of volatility in the securities lending pools. In addition, based on the preference of the client, many securities lending pools are evolving toward a lower risk profile including shorter final maturity guidelines, reduced liquidity risk and reduced investment risk. Clients are expressing the desire to utilize lower risk collateral reinvestment vehicles for greater percentages of their securities lending activity. While these products do have a higher potential for reputation risk than do high alpha or non-constant dollar funds, they have less reputation risk than do cash investment sweep funds.

Cash investment sweep funds are viewed as having moderate to high reputation risk. These funds are viewed as having the highest potential for reputation risk across all types of funds and lending pools. These funds are as closely tied to the asset servicing business as they are to the asset management business. Clients expect minimal risk in their sweep vehicles and expect that both the NAV and liquidity levels of the sweep funds will be maintained.

Regardless of the level of reputation risk which may/may not be associated with a particular product type, any decision to provide non-contractual support must take into account any punitive accounting or capital consequences of such a decision. As a result, to the extent that a decision to provide non-contractual support would result in the consolidation of a fund or an increased capital requirement, which would obfuscate financial results or result in an undue burden on capital requirements or shareholders, asset managers would need to consider such aspects of the decision very carefully prior to making a decision to provide the support.

<u>Question 3</u>: What effect will the 2009 GAAP modifications have on banking organizations' financial positions, lending, and activities? How will the modifications impact lending typically financed by securitization and lending in general? How may the modifications affect the financial markets? What proportion of the impact is related to regulatory capital requirements? Commenters should provide specific responses and supporting data.

Absent a change to the Proposal, the 2009 GAAP modifications would increase capital requirements for any sponsored funds that an asset manager might be required to consolidate and would likely necessitate a higher level of common equity. In the short-term, this would constrain the asset manager's affiliated bank from being able to expand the balance sheet and from taking on additional risk, which would likely limit lending activities.

The modifications may affect the financial markets by reducing or slowing the credit available as the increased capital requirements (previously noted above) would likely limit a bank's ability to lend. The impact to the availability of credit is highly related to the regulatory capital requirements for any positions that are required to be consolidated. In order to maintain strong capital ratios as required by regulatory Agencies, which have recently been strongly re-emphasized by those Agencies, banks need to ensure that a sufficient capital level is maintained.

Requiring asset managers to consolidate sponsored funds under FAS 167 would not only obfuscate core operating results and likely force analysts and investors rely on supplemental non-GAAP measures in order to determine core operations, but would also be inconsistent with the original intent of the revised accounting guidance. In the event that the consolidation of a material amount of sponsored funds were to be the ultimate outcome of FAS 167 and if the capital requirements in the Proposal were to become final, the Proposal would result in an increase in capital requirements that could be significant which would restrict the industry's growth and ability to provide credit and liquidity products to the market.

Question 4: As is generally the case with respect to changes in accounting rules, the 2009 GAAP modifications would immediately affect banking organizations' capital requirements. The Agencies specifically request comment on the impact of immediate application of the 2009 GAAP modifications on the regulatory capital requirements of banking organizations that were not included in the SCAP. In light of the potential impact at this point in the economic cycle of the 2009 GAAP modifications on regulatory capital requirements, the Agencies solicit comment on whether there are significant costs and burdens (or benefits) associated with immediate application of the 2009 GAAP modifications to regulatory capital requirements. If there are significant costs and burdens, or other relevant considerations, should the Agencies consider a phase-in of the capital requirements that would result from the 2009 GAAP modifications? Commenters should provide specific and detailed rationales and supporting evidence and data to support their positions.

If this Proposal were to be strictly applied, financial institutions would need to build up capital at a time when financial institutions are being encouraged by regulators to increase lending. The procyclical effect of this Proposal should be reflected in the final rule. In addition, it would impact all affected financial institutions on the same day, potentially requiring a significant rush to the market to raise capital.

In the event that the consolidation of a material amount of sponsored funds were to be the ultimate outcome of FAS 167 and if the consolidated assets are required to be included in the regulatory capital ratios, the 2009 GAAP modifications would be immediately punitive to capital ratios, in particular the leverage and total risk-based capital ratios. Banks could be forced to address the increased capital burden through a capital raise. A capital raise such as a common equity or debt offering would be dilutive to earnings per share, which could negatively impact stock prices and change the competitive landscape in the industry. Additionally, there may be a significant operational burden to implement the accounting modifications as some of the data required to consolidate the assets in scope is not readily available. Companies would likely have to dedicate significant resources and incur substantial costs to implement an efficient solution.

We recommend that the Agencies consider a phase-in of the capital requirements that would result from the 2009 GAAP modifications over a period of three years at a minimum. This would provide time to make the appropriate operational, strategic and capital changes to meet the significant demands of the new accounting and the increased capital requirements. Alternatively, we suggest that the risk weighting of such assets be zero or assessed using a linked-presentation model as further discussed in the response to Question #7.

Question 5: The Agencies request comment on all aspects of this proposed rule, including the proposal to remove the exclusion of consolidated ABCP program assets from risk-weighted assets under the risk-based capital rules, the proposed reservation of authority provisions, and the regulatory capital treatment that would result from the 2009 GAAP modifications absent changes to the Agencies' regulatory capital requirements.

As Northern Trust does not participate in such programs, no comment is being included in response to this question.

Question 6: Does this proposal raise competitive equity concerns with respect to accounting and regulatory capital treatments in other jurisdictions or with respect to international accounting standards?

The Proposal does raise significant competitive equity concerns with respect to accounting and regulatory treatments outside of the United States. U.S. GAAP and IFRS accounting standards have not yet converged on this topic and the divergent treatment that results from the 2009 GAAP modifications could create competitive inequities for multi-national banks reporting on a U. S. GAAP basis. Additionally, the 2009

GAAP modifications could disproportionately impact certain banks and result in a lack of comparability across the industry for investors, rating Agencies, regulatory Agencies and investment analysts.

The Proposal also raises competitive concerns with respect to asset managers who are regulated by the Federal Reserve vs. those who are not. Asset management firms regulated by the Federal Reserve as a result of the Proposal would be required to hold capital against any consolidated funds while asset management firms solely regulated by the Securities Exchange Commission or a non-U.S. regulator would not. This result would lead to higher profitability within those asset management firms not regulated by the Federal Reserve and therefore not only a competitive advantage for those firms, but likely a shift in this business towards entities not regulated by the Federal Reserve.

<u>Question 7</u>: Among the structures that likely will be consolidated under the 2009 GAAP modifications, for which types, if any, should the Agencies consider assessing a different risk-based capital requirement than the capital treatment that will result from the implementation of the modifications? How are commenters' views influenced by proposals for reforming the securitization markets that require securitizers to retain a percentage of the credit risk on any asset that is transferred, sold or conveyed through a securitization? Commenters should provide a detailed explanation and supporting empirical analysis of why the features and characteristics of these structure types merit an alternative treatment, how the risks of the structures should be measured, and what an appropriate alternative capital treatment would be. Responses should also discuss in detail with supporting evidence how such different capital treatment may or may not give rise to capital arbitrage opportunities.

The Agencies should consider assessing a different risk-based capital requirement for any sponsored funds that would be required to be consolidated under the 2009 GAAP modifications where risk of loss is legally held by the investors in the fund rather than the consolidating entity. The assets related to these types of sponsored funds, if consolidated under FAS 167, would not represent on-balance sheet risk exposure to the consolidating entity, rather the risk exposure would remain with the third-party investors in these funds. To require the consolidating entity to hold capital against assets representing no risk to the organization would be inappropriate and punitive.

Alternative approaches to capital treatment for such assets would be to either assign a risk weighting of zero to such assets, which would be consistent with the true reflection of exposure's risk to the consolidating entity as discussed above, or to allow for a linked-representation model of risk weighting whereby the assets, less the offsetting liability to investors, would be risk weighted on a basis consistent with the original Proposal.

<u>Question 8:</u> Servicers of securitized residential mortgages who participate in the Treasury's Making Home Affordable Program (MHAP) receive certain incentive payments in connection with loans modified under the program. If a structure must be consolidated solely due to loan modifications under MHAP, should these assets be included in the leverage and risk-based capital requirements? Commenters should specify the rationale for an alternative treatment and what an appropriate alternative capital requirement would be.

As Northern Trust does not participate in such programs, no comment is being included in response to this question.

<u>Question 9</u>: Which features and characteristics of transactions that may not be subject to consolidation after the 2009 GAAP modifications become effective should be subject to risk-based capital requirements as if consolidated in order to more appropriately reflect risk?

The 2009 GAAP modifications not only expand the universe of transactions that are subject to consolidation but also significantly increase the scope of exposures that are potentially subject to risk-based capital requirements. We appreciate the Agencies proposing changes to the risk-based capital framework in order to clarify how accounting standards should apply to the banking industry. Northern Trust has not identified other risks specific to its business model that are not captured by the 2009 GAAP modifications or previous accounting changes.

<u>Question 10:</u> Will securitized loans that remain on the balance sheet be subjected to the same ALLL provisioning process, including applicable loss rates, as similar loans that are not securitized? If the answer is no, please explain. If the answer is yes, how would banking organizations reflect the benefits of risk sharing if investors in securitized, on-balance sheet loans absorb realized credit losses? Commenters should provide quantification of such benefits, and any other effects of loss sharing, wherever possible. Additionally, are there policy alternatives to address any unique challenges the pending change in accounting standards present with regard to the ALLL provisioning process including, for example, the current constraint on the amount of provisions that are includible in tier 2 capital? Commenters should provide quantification of the effects of the current limits on the includibility of provisions in tier 2 capital and the extent to which the 2009 GAAP modifications and the changes in regulatory capital requirements proposed in this NPR effect those limits.

As Northern Trust does not participate in such programs, no comment is being included in response to this question.

We appreciate the opportunity to comment on the Proposal. If you have any questions, please contact Richard Kukla, at (312) 444-7408 or Aileen Blake, at (312) 630-6694.

Sincerely,

/s/ Aileen Blake

Aileen B. Blake
Executive Vice President - Controller