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Northern Trust



STATE STREET

January 31, 2014

BY ELECTRONIC SUBMISSION

Robert deV. Frierson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551
Docket No. R-1466

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429
FDIC RIN 3064-AE04

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street SW
Suite 3E-218
Mail Stop 9W-11
Washington, DC 20219
Docket ID OCC-2013-0016

Re: **Liquidity Coverage Ratio: Liquidity Risk Measurement, Standards, and Monitoring; Proposed Rule**

Ladies and Gentlemen:

The Bank of New York Mellon Corporation, Northern Trust Corporation, and State Street Corporation (collectively, the “**Custody Banks**”) welcome the opportunity to comment on the proposed rulemaking, *Liquidity Coverage Ratio: Liquidity Risk Measurement, Standards, and Monitoring* (the “**Proposed Rule**”), issued by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation (collectively, “**the Agencies**”).¹ The Proposed Rule seeks to implement the liquidity coverage ratio agreed to by the Basel Committee on Banking Supervision (“**Basel Committee**”) as part of the Basel III Framework (the “**Basel III LCR**”)² for large, internationally active banking organizations and their consolidated subsidiary depository institutions, such as the Custody Banks.

¹ Liquidity Coverage Ratio: Liquidity Risk Measurement, Standards, and Monitoring; Proposed Rule, 78 Fed. Reg. 71,818 (Nov. 29, 2013).

² Basel Committee on Banking Supervision, *Basel III: The Liquidity Coverage Ratio and Liquidity Risk Monitoring Tools* (Jan. 2013).

The Custody Banks support the Basel Committee's and the Agencies' efforts to strengthen liquidity and improve the banking sector's ability to absorb shocks arising from financial and economic stress. We believe that such efforts should be appropriately tailored to reflect the different liquidity risk profiles of different business models and different financial services. To that end, we welcomed the Basel Committee's adoption of a 25 percent outflow rate for operational deposits (in contrast to wholesale deposits more generally) to recognize the stable nature of such deposits.

The operational deposit category is intended to cover deposits that are "truly operational in nature."³ To this end, the Proposed Rule establishes eight criteria, a definition of "operational deposits," and a definition of "operational services." While we are sensitive to the Agencies' concern that the criteria for operational deposits should be appropriately "restrictive," the proposed treatment of operational deposits substantially differs from the Basel III LCR and results in the exclusion of a significant proportion of deposits held by custody banks that are "truly operational in nature."⁴ As such, the proposed narrowing of the scope of "operational deposits" would substantially overstate the liquidity risk of custody banks.

We believe that the following revisions to the U.S. LCR rule would better capture the range of deposits that are "truly operational in nature,"⁵ more closely reflect the liquidity risk of custody deposits, and be more consistent with the Basel III LCR:⁶

- Modify § __.4(b)(1) to require that operational services, rather than operational deposits, are subject to a legally binding written agreement.
- Modify § __.4(b)(7) to exclude deposits in connection with prime brokerage services, rather than exclude all deposits in connection with all operational services provided to a broad range of customers.
- Revise the definition of "operational deposits" to include instances where the bank provides services as an "agent or administrator;" and clarify that a deposit that is functionally necessary to provide the operational service, rather than contractually required, satisfies the definition of "operational deposit."
- Revise the definition of "operational services" to include the administration of investment assets, collateral management services, and the settlement of foreign

³ Proposed Rule, 78 Fed. Reg. at 71,841.

⁴ *Id.*

⁵ *Id.*

⁶ This letter focuses solely on the operational deposit issues that are common to the Custody Banks. Each of the Custody Banks, either in individual letters or through industry groups, has provided additional comments on the Proposed Rule. *See, e.g.*, Letter from The Clearing House Association et al. to the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance System Re: Liquidity Coverage Ratio (Jan. 31, 2014).

exchange transactions in the list of enumerated activities, and to include the enumerated services performed in a “trustee” capacity.

The remainder of this letter proceeds in two parts. Part I provides a background on the operational services offered by custody banks and the reasons why such deposits are stable and predictable over time. Part II discusses the Proposed Rule’s treatment of operational deposits and the Custody Banks’ recommended revisions to better capture those deposits that are “truly operational in nature.”

I. Background on Operational Deposits at Custody Banks

Our collective status as among the largest providers of global custody services and our unique liquidity profile informs our perspective of the Proposed Rule. Custody banks specialize in the provision of safekeeping, settlement, asset administration, and trust and banking services to institutional investor customers. Regardless of the type of institution, these customers look to their respective custody bank to meet all of their custody-related needs.

As a necessary by-product of these services, custody banks hold customers’ residual cash in deposits. Unlike many other types of wholesale funding, custody deposits have proven to be stable, predictable, and a steady source of funding over the long term. It is this stable source of funding that guides the custody bank business model and defines its liquidity profile—and not the search for assets with particular yields or returns.

At least four particular characteristics of custody bank services drive the long-term, stable nature of custody deposits. First, custody deposits are a by-product of specialized and operationally complex services for which there are few substitutes. The time and costs involved to set-up and on-board custody services significantly reduce the risk that a customer will quickly withdraw its funds or switch to another entity for the same services. For example, the typical on-boarding process for an asset servicing relationship requires initial analysis, set-up, asset/cash transfer, account reconciliation, training, accounting, and performance. A typical process can take several months to complete and requires significant investments in technology, platforms, and staff; a more complex relationship may require over a year.

Moreover, customers are unlikely to significantly reduce their custody deposits, even while transitioning to another custody service provider, because these deposits are necessary to support ongoing, day-to-day activities for each fund customer. Thus, the complexity and switching costs of the operational services provided by custody banks—rather than the identity of the customer—drive the stability and predictability of custody deposits.

Second, the underlying custody service relationship is established by and subject to a legally enforceable contract. Many of these contracts are governed by strict limits on the use and movement of customer funds. For example, a bank as trustee holds deposits for the life of the transactions, which can extend for years. Custody contracts typically have minimum termination notification periods, ranging from 30 days to one year. Even after termination, the customer and the custody bank must develop and agree on a plan to transfer servicing responsibilities and

assets, which as discussed above, can range from several months to several years. These contractual terms also contribute to the long-term predictability and stability of customer deposits.

Third, the custody relationship is often a function of legal or other regulatory requirements. The Investment Company Act of 1940, for instance, requires U.S. mutual funds to ensure the proper segregation of fund assets.⁷ Although the Act permits various types of custody arrangements,⁸ nearly all U.S. mutual funds use a bank custodian for the safekeeping of securities.⁹ Mutual fund custody arrangements are “elaborate” and operationally complex to satisfy strict rules regarding custody and reconciliation of fund assets, which are designed to prevent theft and other instances of fraud.¹⁰ Thus, many U.S. mutual funds use a single custody bank to maintain centralized oversight and control over day-to-day investments, client subscriptions and redemptions, and other operational needs. Similarly, European Union rules regarding Undertakings for Collective Investments in Transferable Securities (“UCITS”) require the appointment of a single depository for each fund.¹¹

Finally, custody bank deposits come from a diverse range of sources that help even out possible funding shocks affecting a particular fund customer. Custody banks maintain operational relationships with thousands of individual funds in hundreds of jurisdictions across the pension fund, mutual fund, corporate, financial institution, and government sectors. Although there may be idiosyncratic events that cause a particular fund customer to terminate one or more contracts, it is highly unlikely that all customers will terminate all their contracts at the same time. And even if this unlikely event were to occur, it would be extremely difficult for a custody bank to transfer all of its fund services, assets, and associated deposits within 30 days. Thus, the diverse customer base of custody banks also drives the long-term stability of custody deposits in connection with these operational services.

In addition to these qualitative factors, there is extensive quantitative evidence that the operational deposits of custody banks are a stable source of funding, even during times of financial market and economic stress. For example, deposit data shows that the Custody Banks’

⁷ See 15 U.S.C. § 80a-17(f).

⁸ See *id.*

⁹ See Investment Company Institution, 2013 Investment Company Fact Book: A Review of Trends and Activities in the U.S. Investment Company Industry Appx. A, 222 (53 ed. 2013), available at http://www.icifactbook.org/pdf/2013_factbook.pdf.

¹⁰ See *id.*

¹¹ See European Commission, Proposal for a Directive of the European Parliament and of the Council Amending Directive 2009/65/EC on the Coordination of Laws, Regulations and Administrative Provisions Relating to UCITS as Regards the Depository Function, Remuneration Policies and Sanctions Art. 22 (July 3, 2012), available at http://ec.europa.eu/internal_market/investment/docs/ucits-directive/20120703-proposal_en.pdf; European Commission, Directive 2011/61/EU of the European Parliament and of the Council on Alternative Investment Fund Managers Art. 21 (June 8, 2011), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:174:0001:01:EN:PDF>.

deposit base significantly *increased* immediately following the Lehman Brothers crisis in 2008, the European sovereign debt crisis, and the recent instability resulting from the U.S. debt ceiling debates.

Recognizing the unique and stable nature of these deposits, the Basel Committee adopted a 25 percent outflow rate for “operational deposits generated by clearing, custody, and cash management activities” in the Basel III LCR.¹² The Proposed Rule likewise adopts this lower outflow rate, albeit in a far more restrictive manner.¹³

II. Treatment of Operational Deposits in the Proposed Rule

The Basel III LCR requires international banking organizations to maintain an amount of high quality liquid assets (“**HQLA**”) that is at least 100 percent of its total net cash outflows over a 30-day period.¹⁴ Funding that meets the criteria for “operational deposits” receives a 25 percent outflow rate.¹⁵ The Custody Banks believe that this 25 percent outflow rate represents a conservative estimate of the behavior of operational deposits in a stress event. Likewise, the Custody Banks acknowledge the LCR requirement to exclude excess balances from the 25 percent outflow rate for operational deposits¹⁶ because excess balances historically have been less stable than core operational deposits. In short, the Custody Banks view the Basel III LCR requirements as a conservative estimate of the observed behavior of custody-related operational deposits.

Unfortunately, the Proposed Rule deviates from the already conservative requirements of the Basel III LCR in several significant ways. First, the Proposed Rule substantially narrows the range of funding that qualifies for “operational deposits.” In practice, this proposal would unduly restrict and exclude a substantial proportion of custody deposits that are truly operational in nature. Custody deposits that do not meet these unduly restrictive requirements would receive an unwarranted 100 percent outflow rate. As a result, the Proposed Rule would substantially overstate an already conservative estimate of a custody bank’s liquidity risk.

Second, the Proposed Rule would require a covered company to calculate net cash outflows using a “peak-day” outflow methodology. That is, rather than calculate net cash outflows cumulatively over a 30-day period,¹⁷ the Proposed Rule would calculate the denominator using the “dollar amount on the day within a 30 calendar-day stress period that has

¹² Basel III LCR, at ¶¶ 93-104.

¹³ Proposed Rule, 78 Fed. Reg. at 71,841. Operational deposits fully covered by deposit insurance receive a 5 percent outflow rate.

¹⁴ Basel III LCR, at ¶ 22.

¹⁵ *Id.* at ¶¶ 93-104.

¹⁶ *Id.* at ¶ 96.

¹⁷ *Id.* at ¶ 69.

the highest amount of net cumulative cash outflows.”¹⁸ By presuming that operational deposits and other financial commitments with an indeterminate maturity are fully realized on day 1,¹⁹ this approach disproportionately impacts custody banks due to their high proportion of operational deposits. As such, the peak-day outflow methodology further overstates the liquidity risk profile of a custody bank.²⁰

These deviations from the already conservative Basel III LCR are unwarranted and unsupported by historical behavior. Below, the Custody Banks offer four recommendations on the criteria and definitions governing operational deposits. We believe that these revisions strike a better balance between the need for appropriately restrictive criteria and the actual liquidity risk profile of custody deposits.

a. Require a Written Agreement for Operational Services Rather than Deposits

To qualify as an operational deposit, the Proposed Rule provides that a “*deposit* must be held pursuant to a legally binding written agreement, the termination of which is subject to a minimum 30 calendar-day notice period, or significant termination costs are borne by the customer providing the deposit if a majority of the deposit balance is withdrawn from the operational deposit prior to the end of a 30 calendar-day notice period.”²¹

The Basel III LCR, by contrast, specifies that the “*services*” underpinning the operational deposit must be provided pursuant to a legally binding agreement.²² This approach better reflects actual industry practice because operational deposits are simply a by-product of the underlying operational services provided.²³ Indeed, the deposits are not held independently of the underlying operational service and are not subject to an independent contractual agreement.

Likewise, the customer bears the significant switching costs of ending the operational service rather than the costs of withdrawing the deposit. This focus on the operational service

¹⁸ Proposed Rule, 78 Fed. Reg. at 71,833.

¹⁹ *See id.* at 71,834.

²⁰ This letter focuses solely on the operational deposit issues that are common to the Custody Banks. Our concerns about the “peak-day” calculation are addressed in industry group letters. *See* Letter from The Clearing House Association et al. to the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance System Re: Liquidity Coverage Ratio (Jan. 31, 2014). In short, to the extent the Agencies pursue a net cash outflow calculation methodology that addresses maturity mismatches, we believe that such a methodology should be determined at the international, Basel Committee level following a quantitative study and analysis.

²¹ Proposed Rule, 78 Fed. Reg. at 71,859 (proposed § __.4(b)(1)) (emphasis added).

²² *See* Basel III LCR, at ¶ 94 (emphasis added). Other jurisdictions implementing the Basel III LCR also focus on the operational service rather than the deposit. *See, e.g.*, Prudential Standard APS 210, Liquidity Attachment A ¶ 48 (Jan. 2014), *available at* [http://www.apra.gov.au/adi/PrudentialFramework/Documents/Prudential-Standard-APS-210-Liquidity-\(January-2014\).pdf](http://www.apra.gov.au/adi/PrudentialFramework/Documents/Prudential-Standard-APS-210-Liquidity-(January-2014).pdf).

²³ *See* Basel III LCR at ¶ 95.

provided, rather than the deposit balance, better reflects the true costs of termination. A customer's deposit balance is intended to fluctuate in the normal course of business, and there are no "termination costs" associated with this ordinary activity. There are substantial costs, however, when a customer seeks to terminate the servicing contract and transfer the servicing functions to another custodial entity.²⁴

To reflect these operational realities, the Custody Banks recommend that the final U.S. LCR rule be revised as follows:

§__4 Certain Operational Requirements

....

(b)(1) The operational services to which the deposit relates are provided pursuant to a legally binding written agreement, the termination of which is subject to a minimum 30 calendar-day notice period or significant switching costs to be borne by the customer.

b. Exclude and Define Prime Brokerage Services

The Basel III LCR specifically excludes deposits arising out of correspondent banking and prime brokerage services from the definition of operational deposits.²⁵ In implementing the exclusion for deposits associated with prime brokerage services, the Proposed Rule deviates from the Basel III LCR by excluding *all* deposits from *all* operational services provided to an investment company, non-regulated fund, or investment adviser.²⁶ This broad-sweeping approach would exclude substantial amounts of deposit balances arising from ordinary custody activities wholly unrelated to prime brokerage services.

By focusing on the type of customer rather than the nature of the underlying activity, the Proposed Rule assumes that all "such balances, owned by hedge funds and other institutional investors, are at risk of margin and other immediate cash calls in stressed scenarios and have proven to be more volatile during stress periods."²⁷ The preamble goes on to state that "most prime brokerage customers maintain multiple prime brokerage relationships and are able to quickly shift from one covered company to another."²⁸ These assertions are overly broad and

²⁴ These operational and legal costs are described in greater detail in section I.

²⁵ Basel III LCR, at ¶ 99 & n. 42. As discussed above, this letter focuses solely on the operational deposit issues that are common to all the Custody Banks. Certain of the Custody Banks have additional concerns regarding the treatment of correspondent banking services, which are addressed in individual comment letters and through industry groups.

²⁶ Proposed Rule, 78 Fed. Reg. at 71,859-60 (proposed §__4(b)(7)).

²⁷ *Id.* at 71,841-42.

²⁸ *Id.* at 71,842.

based on mistaken assumptions, and we urge the Agencies to exclude only deposits provided in connection with prime brokerage *services*.

First, custody bank services differ from prime brokerage services in significant ways that materially affect the liquidity profile of the underlying deposit. Prime brokerage involves a package of services in which the prime broker finances customer trades executed by the customer with one or more third parties. The customer “maintains its funds and securities in an account with the prime broker,” and the prime broker “clears and finances the customer trades executed by one or more registered broker-dealers . . . at the behest of the customer.”²⁹ The prime broker may act as principal, and the prime brokerage agreement gives the prime broker the right to use custody assets for its own accounts.³⁰ Because the prime broker finances customer trades and has a right to make use of the customer’s assets, the customer is exposed to and dependent on the solvency of the prime broker.

By contrast, custody banks act as agents on behalf of their clients. Under a custody agreement, customer securities are held in a segregated account and are not on the bank’s balance sheet. The customer is significantly less exposed to the custody bank during periods of stress because the bank does not finance customer trades or have routine access to these customer securities. As a result, customers are far less likely to withdraw their deposits in connection with custody services than with prime brokerage services. Historical experience confirms these qualitative differences. Operational deposits arising from the provision of custody services have proven to be highly stable, and indeed such deposit balances are likely to increase during times of stress as investment funds liquidate their positions to hold cash balances.

In keeping with experience that the type of service rather than the type of client drives deposit stability, the Basel Committee and other regulators have defined prime brokerage in terms of specific services performed. The final U.S. LCR rule should align with this approach. For instance, the Basel III LCR defines prime brokerage as “a package of services offered to large active investors,” including “clearing, settlement and custody; consolidated reporting; financing (margin, repo or synthetic); securities lending; capital introduction; and risk analytics.”³¹ The Securities and Exchange Commission (“SEC”) has long characterized prime brokerage as a system in which the prime broker clears and finances customer trades executed by third parties.³² The United Kingdom’s Financial Conduct Authority and Prudential Regulatory

²⁹ Letter from Brandon Becker, Director of the Division of Market Regulation, Securities and Exchange Commission, to Jeffrey C. Bernstein, Prime Broker Committee, at 2 (Jan. 25, 1994), *available at* <http://www.sec.gov/divisions/marketreg/mr-noaction/pbroker012594-out.pdf>.

³⁰ *See* Financial Conduct Authority & Prudential Regulatory Authority Handbook, Glossary (April 2013), *available at* <http://www.fshandbook.info/FS/html/handbook/>.

³¹ Basel III LCR, at ¶ 99 n. 42.

³² *See* Letter from Brandon Becker, Director of the Division of Market Regulation, Securities and Exchange Commission, to Jeffrey C. Bernstein, Prime Broker Committee, at 2 (Jan. 25, 1994), *available at* <http://www.sec.gov/divisions/marketreg/mr-noaction/pbroker012594-out.pdf>.

Authority define “prime brokerage services” as “a package of services provided under a prime brokerage agreement which gives a prime brokerage firm a right to use safe custody assets for its own accounts.”³³

Consistent with other regulatory guidance, including the Basel III LCR, and observed customer behavior, the U.S. LCR should expressly define prime brokerage services when excluding deposits in connection with the provision of such services from the scope of operational deposits. To the extent the Agencies have particular concerns regarding a bank’s categorization of prime brokerage services as operational services, the Agencies should address these concerns through their supervisory powers rather than through a broad rule that unfairly sweeps across all custody bank services.

Accordingly, the U.S. LCR rule should provide:

§ __.3 Definitions.

....

Prime brokerage services means a package of services provided by a [BANK] under a contractual arrangement whereby the [Bank], among other services, clears, settles, carries, and finances transactions entered into by a client with the [BANK] or a third-party entity (such as an executing broker), and where the [BANK] has a right to use assets provided by the client, including in connection with the extension of margin and other similar financing of the client, subject to applicable law.

§ __.4 Certain Operational Requirements

....

(b)(7) The deposit must not be provided in connection with the [BANK’s] provision of prime brokerage services.

To the extent that the final U.S. LCR rule continues to exclude deposits based on the type of customer, then the rule should, at the very least, only exclude the primary users of prime brokerage services. This category would include mostly hedge funds and other similar private funds. Investment companies, such as mutual funds, should not be included in this category because they engage in little to no prime brokerage activities and are substantial users of custody services that are wholly unrelated to prime brokerage. Mutual funds are subject to strict limits on their ability to borrow funds, and therefore have little to no need for prime brokerage services. By contrast, hedge funds typically are leveraged and use prime brokers to finance their investment activities. Mutual funds generally have lower-risk investment strategies and a more

³³ Financial Conduct Authority & Prudential Regulatory Authority Handbook, Glossary (April 2013), available at <http://www.fshandbook.info/FS/html/handbook/>.

stable investor base (mostly owned by retail investors). By contrast, hedge funds have a higher risk trading strategy and a more volatile investor base. Moreover, mutual funds are subject to strict rules governing segregation, custody, and reconciliation of fund assets, and nearly all mutual funds use a bank custodian to meet these requirements.

Under this alternative approach, section 4(b)(7) should state:

§ __.4 Certain Operational Requirements

....

(b)(7) The deposit must not be provided in connection with the [BANK]’s provision of operational services to a non-regulated fund, or to an investment adviser when managing the assets of a non-regulated fund.

c. Revise the Definition of “Operational Deposit”

The Proposed Rule defines “operational deposit” as “unsecured wholesale funding that is required for the [BANK] to provide operational services as an independent third-party intermediary to the wholesale customer or counterparty providing the unsecured wholesale funding.”³⁴

This definition does not capture the various capacities in which custody banks provide operational services. In addition to providing services as an independent third-party intermediary, custody banks routinely provide operational services as agent or administrator, such as an ERISA plan administrator. This adjustment to the proposed definition of operational deposit would better encompass the range of services provided by custody banks.

In addition, the Custody Banks emphasize that the defining characteristic of an operational deposit is one that is necessary for the bank to provide operational services to the customer.³⁵ As discussed above, it is the operational service and not the deposit that is subject to the legally binding written agreement. Thus, we ask the Agencies to clarify either in the rule text or in the preamble that a deposit that is “required” is one that is necessary for the bank to provide operational services, even if the deposit is not expressly required by the agreement.

To better capture the scope of custody deposits that are “truly operational in nature,” the final definition of “operational deposits” should provide:

§ __.3 Definitions.

....

³⁴ Proposed Rule, 78 Fed. Reg. at 71,858 (proposed § __.3).

³⁵ Basel III LCR, at ¶ 93.

Operational deposit means unsecured wholesale funding that is necessary for the [BANK] to provide operational services as an independent third-party intermediary, agent, or administrator to the wholesale customer or counterparty providing the unsecured wholesale funding. . . .

d. Revise the Definition of “Operational Services”

The Proposed Rule defines “operational services” as a number of enumerated services, provided they are performed as part of “cash management, clearing, or custody services.”³⁶ While we appreciate the scope of the services listed, the proposed definition excludes several activities that are an important part of the suite of operational services provided by custody banks.

First, custody banks provide an extensive range of asset administration services as a core business. These administrative services include processing corporate action events and tax reclamations, receiving dividend and other investment income, and other general functions that are not specifically enumerated. The Basel III LCR expressly recognizes these general services within the definition of operational deposits.³⁷

Second, custody banks provide collateral management services as part of their general suite of operating services. This includes safekeeping and administration of cash and non-cash collateral, the exchange of cash margin, and access to financial market infrastructures. The Basel III LCR likewise recognizes these services.³⁸

Third, banks provide settlement services for foreign exchange transactions and not just securities transactions. As regulators have recognized, global custody services include executing foreign exchange transactions, which are a direct by-product of investment activities in global financial markets.³⁹ Thus, the settlement of foreign exchange transactions should be recognized as an enumerated operational service just like the settlement of securities transactions.

Finally, custody banks provide these and other enumerated services in a trustee capacity, and not just in a clearing, custody, and cash management capacity. Deposits in connection with trustee services have stable deposit profiles just like those in connection with cash management, clearing, and custody services. Corporate trust services, for example, are governed by contracts that limit the use and movements of customer funds. A bank trustee holds deposits for the life of

³⁶ Proposed Rule, 78 Fed. Reg. 71,858 (proposed § __.3).

³⁷ See Basel III LCR, at ¶ 102 (“A custody relationship, in this context, refers to . . . processing of assets or the facilitation of the operational and administrative elements of related activities on behalf of customers in the process of their transacting and retaining financial assets. . . . Also included are the receipt of dividends and other income, client subscriptions and redemptions.”).

³⁸ See *id.* at ¶¶ 101-03 (noting that custodial services include “the transfer of contractual payments, the processing of collateral,” and “payment and settlement services”).

³⁹ See Comptroller of the Currency, Comptroller’s Handbook: Custody Services 2 (Jan. 2002).

the transactions, which can extend for years. There are also high barriers to exit for corporate trust services, including bondholder approval and a lengthy, expensive onboarding process. We note, in this respect, that the Basel III LCR recognizes that custodial services can “extend to asset and corporate trust servicing.”⁴⁰

To recognize these operational services, consistent with the Basel III LCR, the final U.S. LCR rule should include the following:

§ __.3 Definitions.

....

Operational Services means the following services, provided they are performed as part of cash management, clearing, custody, or trustee services:

...

(6) Settlement of securities or foreign exchange transactions;

....

(12) Administration of investment assets; and

(13) Collateral management services.

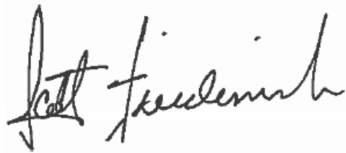
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⁴⁰ Basel III LCR, at ¶ 102.

January 31, 2014

The Custody Banks appreciate this opportunity to comment on the Agencies' critical work to strengthen liquidity requirements for U.S. banks. We would be happy to discuss any of these issues further. Should you have any question or need any additional information, please contact Eli Peterson, Managing Director and Senior Managing Counsel, the Bank of New York Mellon Corporation, at (202) 624-7925 or eli.peterson@bnymellon.com; David Charney, Senior Vice President, Northern Trust Corporation, at (312) 444-4782 or dhc1@ntrs.com; or Ed Novakoff, Senior Vice President, State Street Corporation, at (617) 664-9652 or enovakoff@statestreet.com.

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