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Northern Trust

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Secretariat
Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002
Basel, Switzerland

Re: Consultative Document: International Framework for Liquidity Risk Measurement, Standards and Monitoring

Ladies and Gentlemen:

Northern Trust Corporation appreciates the opportunity to comment on the Consultative Document: International Framework for Liquidity Risk Measurement, Standards and Monitoring (the "Document") to the Basel Committee on Banking Supervision within the Bank for International Settlements (the "Committee").

Northern Trust Corporation ("Northern Trust") is a U.S. multi-bank holding company with its headquarters in Chicago, Illinois. The corporation has a growing network of 79 offices in 18 U.S. states and 16 international offices in North America, Europe, the Middle East and the Asia-Pacific region. As of December 31, 2009, Northern Trust had assets under custody of \$3.7 trillion (including global custody assets of \$1.9 trillion), assets under management of \$627.2 billion and banking assets of \$82.1 billion. Northern Trust conducts its global activities through the Northern Trust Company (an Illinois-chartered bank with subsidiary banks and branches in the U.K., Europe and Asia-Pacific), Northern Trust N.A (a U.S. national bank headquartered in Florida), Northern Trust Bank, FSB (a federal thrift banking institution headquartered in Michigan), an investment advisory company, an Edge Act subsidiary, and a number of other non-bank subsidiaries. As a major international trust-processing bank, Northern Trust has long understood the importance of maintaining a strong liquidity position across all types of market and economic environments.

<u>General Comments:</u>

Northern Trust supports the development and implementation of a global framework for liquidity risk measurement in order to support a resilient global banking system, international competitive equality and efficient liquidity management practices. We believe that the absence of a global framework would lead to a variety of uneven national standards, trapping liquidity resources in some jurisdictions and creating deficits in others, with the overall impact of weakening the international banking system as a whole. However, a new liquidity framework must be carefully

designed not to advantage/disadvantage certain types of financial institutions or those from particular countries because of different business models, local banking regulations, prevailing types of financial instruments, central bank policies, accounting rules or various other differences. We fully understand how difficult a task this is and believe the Committee has made a substantial start. Even so, Northern Trust believes that U.S. banks in general, and major trust processing banks in particular, are disadvantaged by this proposal and that there is much needed work ahead to ensure that such a major change does not have significant unintended consequences to the international banking system, global financial markets and long-term economic growth.

Northern Trust also notes that the timing of the comment period related to the Document (responses due April 16, 2010) precedes the quantitative results associated with the Quantitative Impact Study (QIS) currently underway (submission date of April 30, 2010). Additional interpretive guidance related to the QIS continues to be issued, something that will persist after the Document's comment period had closed. Additionally, the Document calls for certain weighting factors to be established by national banking regulators. Since these have not yet been proposed in the US, a complete analysis of the potential impacts of this Document is not possible at the present time.

For all these reasons, Northern Trust recommends that after careful review of all comments received and after the results of the QIS have been analyzed, the Committee issue a revised framework document for further comment and additional quantitative analysis.

The balance of this letter provides a more detailed discussion what we believe are the most significant issues related to the calculation of the two liquidity ratios proposed in the Document.

Liquidity Coverage Ratio (LCR):

The LCR as proposed in the Document understates the liquidity resources available to U.S. banking companies while overstating the potential run-off of funds, resulting in a far too conservative ratio to use as a minimum liquidity standard. Adoption of this standard would trap excess liquidity in the banking sector and drive up lending costs worldwide as banks adjust their pricing to make up for lost earnings from holding large quantities of cash and government securities.

A. Liquid Assets Definition

Under the proposed rule, banks must hold a stock of unencumbered, high quality liquid assets sufficient to cover the cumulative net cash outflows (as defined) over a 30-day stress period. The definition of high quality liquid assets per the Document is overly restrictive, basically limited to cash maintained at central banks and direct government or central bank debt. In particular, U.S. Government agency securities, bank debt guaranteed by sovereigns and assets placed as potential collateral at the Federal Reserve discount window, which all provide substantial emergency liquidity for U.S. banks, are excluded from liquid asset totals.

U.S. agency securities are excluded from liquid assets since they are not assigned a zero risk-weight in the U.S. under the Basel II standardized approach. However, some of these securities are backed by the full faith and credit of the U.S. Government, just as are U.S. Treasury securities. During the recent international financial crisis, the markets for sale or repo of most of these securities remained open and functioned similarly to those for U.S. Treasuries. Finally, all of these securities are fully eligible to use as collateral at the Federal Reserve ("Fed") discount window, should the need arise, and are included as part of the liquid asset buffer as defined by

U.S. banking regulators in their March, 2010, Interagency Policy Statement on Funding and Liquidity Risk Management. Northern Trust believes these securities meet the criteria for inclusion as liquid assets, and that not doing so would not only disadvantage U.S. banks, but would drive up the costs of borrowings for these Government entities.

Similarly, bank debt guaranteed by Sovereigns, or the FDIC in the U.S., are also currently excluded from liquid assets. Northern Trust believes that these instruments are as secure as debt issued directly by these Sovereigns and that they should not be excluded simply because the underlying borrower is a financial institution.

Finally, U.S. banks go to great lengths to document and place various assets at the Federal Reserve discount window so that they can be pledged as collateral in the event of an unexpected liquidity demand. These assets include mortgage and commercial loans along with various types of debt securities, all appropriately discounted to match current market conditions. U.S. banks can receive same-day, good funds based on the amount of collateral placed, by following well documented discount window procedures. While Northern Trust is not suggesting that the Fed discount window should be considered a primary source of bank liquidity, excluding it completely as a source of emergency liquidity under a stress scenario is far too conservative. We recommend including unused collateral placed at the Fed, post-haircut, as a component of liquid assets when calculating the LCR.

B. Cash Outflows – Trust Deposit Run-off

As a major trust-processing bank, Northern Trust has a substantial amount of deposits originating from uninvested cash balances held in its corporate, institutional and personal clients' trust accounts. These balances are operational in nature, resulting from normal, recurring activities of our trust clients (asset reallocation, new investments, interest / dividend payments, planned distributions and many other transactions). These deposits are directly related to the large number of trust accounts and the substantial value of trust assets held. Northern Trust cultivates strong relationships with its trust clients and provides many services to them beyond the strict custody of their assets. We believe the operational and relationship nature of these balances exceeds those of a strictly banking relationship; however, this is not recognized by the treatment of these deposits under the LCR, which assumes a 100% run-off within 30 days. We believe this is not only too extreme, but would not be operationally possible given that the underlying trust assets can not be transitioned out in so short a time-frame. Northern Trust recommends that a distinction be made between financial institutions providing trust and custody service to its clients, from banks simply accepting a deposit from a third-party fiduciary account. We further recommend that a run-off factor of 25%, on a par with corporate banking relationships, be applied to these deposits.

Net Stable Funding Ratio (NSFR):

A long-term structural ratio as proposed in the Document can be an important component of a global framework for liquidity risk management. However, as is the case with the LCR, the NSFR is overly conservative and ignores potential management actions that could take place over a longer time horizon.

A. Available Stable Funding

As noted above, trust processing banks collect deposits resulting from the normal business activities of its trust clients. These deposits represent a stable source of funds which is excluded from the NSFR. Northern Trust recommends applying a 70% factor to these deposits, placing them on a par with uninsured, relationship based banking deposits.

B. Management Actions

In the case of a longer-term liquidity event, management would have the time and ability to significantly adjust its financial position to better meet its future obligations. For example, new lending and commitment activity could be curtailed, existing loans securitized and sold, long-term funding could be raised, etc. However, the NSFR requires stable funds for a large percentage of short-term loans (maturing within one year) while assuming management has no ability to develop additional funding sources or otherwise adjust to support these on-going business activities. Northern Trust believes that this ratio needs to better balance potential future business activities with management's ability to react in light of a longer-term economic event. We recommend eliminating or substantially reducing the weighting factors assigned to retail and corporate loans maturing within one year.

Conclusion:

Northern Trust appreciates the opportunity to present its comments on such an important proposal, and we thank you for considering our views. We look forward to working with the Committee going forward on an updated proposal and additional quantitative study. In the meantime, should you have any questions or comments on this response, please feel free to contact me.

Very Truly Yours,

William L. Morrison

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CC: Federal Reserve Bank
Office of the Controller of the Currency
Office of Thrift Supervision
State of Illinois
Financial Services Authority