BAFT-IFSA

May 16, 2013

His Excellency Anton Germanovich Siluanov
Minister of Finance
Ministry of Finance of the Russian Federation
9, Iljinka
Moscow, 103097, Russian Federation

Dear Minister Siluanov:

BAFT-IFSA is an international financial services trade association whose membership includes a broad range of financial institutions throughout the global community. As a worldwide forum for analysis, discussion, and advocacy in international financial services, BAFT-IFSA member banks have a high interest in preserving the safety and soundness of the global financial system.

BAFT-IFSA represents the transaction banking segment of financial institutions, including trade finance and cash management. As such, we are particularly concerned about the impact that disparate financial regulations propagated regionally could have on the provision of these crucial real economy financing products. We also remain concerned about unaddressed unintended consequences emanating from multilateral regulatory initiatives.

Background: The criticality of transaction banking products to cross-border financial services

Transaction banking, as a cross-border financial service, remains an integral facilitator for driving global economic recovery. Transaction banking businesses enable the management of short-term cash, payments, securities, custody and settlement, and cross-border trade for corporate and bank clients. The nature and scope of transaction banking varies across different banking organizations, but there are common components amongst banks. As an intermediary for the global commercial flows of corporates and financial institutions, bank transaction service businesses are the means by which trillions of dollars in global settlement flows travel. These payments naturally give rise to operating and reserve account balances maintained with a service provider or infrastructure in current and other depository accounts. In addition, transaction banks offer an array of linked liquidity management tools and short-term investment options to optimize working capital for commercial activity. Transaction banking also enables the domestic and cross-border settlement of securities trades.

Transaction banking is crucial for the provision of liquidity within banking systems and between national markets. Interbank payments and related interbank lending ensures the smooth functioning of national economies and has a direct influence on the safety and soundness of the global banking system.

Transaction banking is also historically less risky than other forms of financial services. This is particularly true of the trade finance business undertaken by banks worldwide. Trade finance is a critical transaction banking service and trade finance liabilities arise from trade-related obligations underpinned by the movement of goods or services and secured by commercial contracts that document the arrangements between buyer and seller. Trade finance exposures are also generally short term in nature and self-liquidating.

Transaction banking is fundamental to global commerce. It is crucial that clear and consistent regulations are designed at a multilateral level to ensure the cost for providing these services to corporations, governments and citizens does not increase or lead to a decrease in availability of critical real economy resources. The G-20 should specifically ensure these services are not hindered by regulatory fragmentation or unintended consequences from multilateral rulemaking.

Key recommendations to support transaction banking services for the real economy:

1. **Mitigate the risk of regionalization, protectionism, and extraterritoriality in regulating financial services**

The G-20 has promulgated a coordinated approach for financial regulation in order to strengthen the operations of the global financial system. Increasingly, however, individual jurisdictions are implementing regulations unilaterally that can have extraterritorial implications. This approach to financial oversight has consequences for the end-user of transaction banking services. According to the Bank for International Settlements (BIS), cross-border lending to non-banks decreased dramatically in recent years, with cross border lending in developed countries alone contracting by $630 billion up to the fourth quarter of 2011.[1] As market pressures continue to drive this phenomenon, BAFT-IFSA is increasingly concerned that financial protectionism and disparate regulatory initiatives will contribute to a continued decrease in cross-border financial flows. This will in turn create inefficiency and risk in the financial system and also drive up costs to the end-user, further reducing the ability of banks to support international transactions crucial to companies around the world.

Examples of extraterritorial regulatory approaches can be found across a number of financial market activities, including the OTC derivatives market. This globalized market is now being faced with conflicting US and EU rules with extraterritorial impacts in their own right. As such, cross-border trades are effectively hampered due to conflicts in law and the legal uncertainty created therein. The US implementation of the Foreign Account Tax Compliance Act (FATCA) and the European Union proposal for a Financial Transaction Tax (FTT) also have the potential of further triggering a reduction in financial market activity, despite international objectives for increased growth. Disparate proposals can create disincentives for competition and lead to regulatory arbitrage.

A number of cross border financial protectionist issues could be mitigated by increased regulatory cooperation. The G-20 should thus support the inclusion of sensible financial services provisions in free trade agreements and multilateral trade negotiations. The opening of global markets and coordinated financial services regulatory initiatives will help create a level playing field and will assist in increasing the availability of affordable financial products to the consumer.

2. **Address concerns with the emerging structural reform implications on transaction banking**

In order to maintain the continued flow of transaction banking services globally, BAFT-IFSA also encourages the G-20 to address the emergence of recent proposals by national regulators in the context of the structural reform of the banking sector. In the United Kingdom, for example, the government has endorsed recommendations of the Independent Commission on Banking, which called for global operations and investment banking divisions of UK banks to be ring-fenced from domestic retail operations. The High-level Expert Group on reforming the structure of the European banking sector has proposed similar changes at European Union level. In the United States, the Federal Reserve recently proposed that foreign banking organizations with a significant US presence create an international holding company of the US subsidiary, requiring foreign banks to maintain US regulated capital and liquidity positions for their US operations. These new structural proposals build upon older forms of national protection, including National Depositor Preference (NDP) schemes and asset-maintenance requirements. Potential side effects of these national approaches include the loss of diversification benefits for internationally active individual financial institutions, a reduction in the availability of a variety of financial instruments in the market, and the ultimate impact of increased costs for end-users, thereby reducing the feasibility of hedging their risks. In aggregate, a fragmentation of banking industry regulation will result in decreased international coordination and a localization of financial services and activities. This will likely lead to increased cost, the lowering of competition and innovation, and a reduction in the connectivity of financial flows across borders, all of which are needed to sustain growth and economic activity.

As such, the G-20 should assess the impact of structural reforms to ensure that the real economy is not impaired. The underlying objectives of these proposals - including the safety of the financial system - can be equally reached through harmonized global implementation of financial services rules, in combination with a practical and strengthened multilateral framework for regulatory coordination.

[1] BIS Quarterly Review, June 2012; http://www.bis.org/publ/qtrpdf/r_qt1206b.pdf

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3. **Resolve unintended consequences for transaction banking from multilateral regulatory proposals**

While the G-20 should recommit to an established program for financial services cooperation and avoid conflicting local regulation, the member states should also engage in a proactive examination of regulatory proposals to eliminate unintended consequences for the real economy.

BAFT-IFSA supports the goals of the G-20 to improve the resilience of the banking sector. We remain, however, concerned about the unintended impact of new international rules on companies that rely on transaction banking services. As an example, the Basel III capital and liquidity requirements do not reflect the risk profile of certain transaction banking products - specifically trade finance - nor do they take into account the adverse effects of the proposed changes on global trade and growth.[2] Policies which put at risk the affordable trade of essential goods, and hinder the trade and development goals of emerging markets, work at cross-purposes with the G-20 economic objectives. We note that the recent European Union implementation of Basel III through Capital Requirements Directive IV (CRDIV/CRR) addressed the concerns for trade finance in Basel III. However, in order to be truly effective for companies and consumers worldwide, the G-20 should encourage the Basel Committee to uniformly adopt these positive changes in all Committee jurisdictions to avoid any potential for regulatory arbitrage.[3]

Conclusion:

The growing trend toward the regionalization of international banking regulation complicates and increases the cost of providing cross-border financial products and has the potential to impair economic recovery and growth, while at the same time increasing systemic risk. BAFT-IFSA encourages the G-20 to limit regulatory fragmentation and commit to a balanced, multilateral agenda that recognizes the need to ensure international financial products, and transaction banking products specifically, are available and affordable to support jobs and growth. At the same time, the G-20 should also take steps to reduce any unintended consequences for transaction banking from cumulative, multinational regulatory reforms.

BAFT-IFSA looks forward to continuing to work closely with the G-20 on these and other issues critical to the stability of the financial system. A safe, secure, and well-functioning marketplace is in the best interest of all global citizens.

Very truly yours,

Tod R. Burwell

Tod R. Burwell
President and Chief Executive Officer

CC: G-20 Finance Ministers and Central Bank Governors

[2] For further information, please see Joint Industry Letter on Basel III and International Trade, December 1, 2011: http://www.baft-ifsa.com/eweb/docs/SecondJointIndustryLetter-TradeFinanceFinal.pdf

[3]BAFT-IFSA Letter to G-20 on CRDIV/CRR Trade Finance Harmonization; April 17, 2013: http://www.baft-ifsa.com/eweb/docs/BAFT-IFSAG20LetteronEUImplementation2013.04.17Final.pdf

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