



**Financial Services Agency  
Government of Japan**



*Bank of Japan*

Mr. John G. Walsh  
Acting Comptroller of the Currency  
Office of the Comptroller of the Currency

Mr. Daniel K. Tarullo  
Board of Governors of the Federal Reserve System

Mr. Martin J. Gruenberg  
Acting Chairman  
Federal Deposit Insurance Corporation

Ms. Mary L. Schapiro  
Chairman  
Securities and Exchange Commission

December 28, 2011

Re: Restrictions on Proprietary Trading and Certain Interests in, and Relationships with,  
Hedge Funds and Private Equity Funds

Dear Sirs / Madam

We are writing this letter to request your due consideration of our concerns about the implementation of the proposed Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds (hereinafter called "Restrictions"). We would like to make two points.

First, we would point out the importance of taking due account of the cross-border effect of financial regulations and the need to collaborate with the affected countries. We are sure that you would agree that regarding extraterritorial application of financial regulations the home authorities bear the primary regulatory and supervisory responsibilities. Considering the potentially serious negative impact on the Japanese markets and associated significant rise in the cost of related transactions for Japanese banks, we would appreciate your refraining from extraterritorial application of the Restrictions, or your amending the definition of "control" and "affiliate" so as not to include such foreign joint ventures and foreign subsidiaries which are controlled by foreign banking groups.

On our side, we are making strenuous efforts to improve the quality of supervision further, and assure you that we will continue to monitor closely and effectively the activities of Japanese financial groups in your country.

Second, we are concerned that the proposed Restrictions would have an adverse impact on Japanese Government Bonds (JGBs) trading. They would raise the operational and transactional costs of trading in JGBs and could lead to the exit from Tokyo of Japanese subsidiaries of US banks. Some of the Japanese banks might be forced to cease or dramatically reduce their US operations. Those reactions could further adversely affect liquidity and pricing of the JGBs. We could also see the same picture in sovereign bond markets worldwide at this critical juncture. We would appreciate your expanding the range of exempted securities substantially, to include JGBs.

For our comments in more detail, please find the Annex attached, describing the points that the proposed Restrictions would result in the following:

1. The imposition of the proposed Restrictions directly on foreign entities (i.e. entities established outside the US) owned by foreign financial groups.
2. A potentially serious negative impact on the JGB market and other sovereign debt markets, since exempted securities are limited to US-treasuries, etc.
3. The squeezing of US dollar funding through the Restrictions on short-term FX swap arrangements.
4. The creation of uncertainties about decisions on investment in non-US funds.

We would like to take this opportunity to remind you of a discriminatory treatment against domestic and foreign banks under the Swap Push-out Rule, Section 716 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The author of this clause made clear on the record of Congress that the exclusion of uninsured branches and agencies of foreign banks from the exemption and safe-harbor provisions of this rule was an unintended oversight. We request to clarify that, when applying this clause in your regulation, uninsured US branches and agencies of foreign banks are treated in the same way as insured depository institutions under the provision of the rule, including the safe-harbor application, as originally intended by lawmakers.

We look forward to hearing from you very soon, and would be more than willing to meet with your staff for further discussions in due course. Should you have any questions concerning the above, please do not hesitate to contact us, or our colleagues Mr. Jun MIZUGUCHI, Assistant Commissioner for International Affairs, Financial Services Agency at [jun.mizuguchi@fsa.go.jp](mailto:jun.mizuguchi@fsa.go.jp) +81-3-3506-6640, or Mr. Takeshi NAKAMURA, Head of planning division for financial stability, Bank of Japan at [takeshi.nakamura@boj.or.jp](mailto:takeshi.nakamura@boj.or.jp) +81-3-3277-1087.

Yours sincerely,

Masamichi Kono  
Vice Commissioner for International Affairs  
Financial Services Agency  
Government of Japan

Kenzo Yamamoto  
Executive Director  
Bank of Japan

Cc: Ms. Lael Brainard, Under Secretary for International Affairs, Department of the Treasury

(ANNEX)

1. Extraterritorial application to foreign entities owned by foreign financial groups

Extraterritorial application to foreign entities owned by foreign financial groups could adversely affect liquidity of the financial markets globally and their liquidity positions. This could also have negative impact on US financial stability, which the “Dodd-Frank Act” aims to achieve as a primary objective. As long as the groups are subject to appropriate group-wide supervision by foreign supervisors, such foreign entities should be exempted from the requirements.

2. Impact on the JGB market and other sovereign bond markets

According to the proposed Restrictions, not only US banking groups but also foreign banking groups (those that have a branch or a subsidiary in the US) would be subject to the Restrictions on their current positions of government bonds, except US treasuries. While market making and other less-risky trading are exempted, those Restrictions would impose a significant burden and higher costs on foreign banks, including major Japanese firms, and make sovereign bond trading less attractive and profitable. As a result, for example, some of the Japanese banks might be forced to cease or dramatically reduce their US operations, and Japanese subsidiaries of US banks may consider exiting from JGB trading. There is also a possibility that smooth functioning of the Bank of Japan's money market operations will be adversely affected by the Restrictions. We are concerned that such developments could occur on a global scale. This might exert extremely negative pressures on sovereign bond markets worldwide through reduced liquidity and a rise in volatility. Such a situation would be particularly worrisome under the current financial market condition.

3. Impact on global US dollar funding of financial institutions through Restrictions on short-term FX swap arrangements

We understand that short-term foreign exchange swaps would also be subject to the proposed Restrictions. In many jurisdictions, short-term foreign exchange swaps are used uniquely for the purpose of US-dollar funding by major foreign banking entities, including the Japanese Banking Groups, rather than tools for proprietary trading. If foreign exchange swaps are restricted by the new rules, branches and subsidiaries of US banks would not be able to provide USD liquidity to foreign counterparts through short-term FX swaps. This could squeeze USD funding significantly outside the US and could accelerate the deleveraging of European banks by liquidating foreign assets. In addition, it does not seem to be consistent to restrict short-term swaps while FX spot trading and long-term swaps, through which more risks could be assumed, are exempted. Therefore, we would strongly request that short-term foreign exchange swaps being exempted from the Restrictions.

#### 4. Impact on decisions on investment in non-US asset management funds

Our understanding is that non-US asset management funds would be subject to the Restrictions, except those which do not have US investors or those which would need registration under the US Investment Company Act. In practice, it would be almost impossible for an investor to judge whether a fund is exempted or not, and the Restrictions could create an uncertain investment climate for non-US funds, resulting in significantly reduced investments in those funds and reduced investment opportunities for US investors. We believe that it would be more appropriate to discuss with foreign regulators to find a clear objective definition of the funds in question.