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March 20, 2008

Dr. Nout Wellink
Chairman
Basel Committee on Banking Supervision
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Re: Sound Practices for Managing Liquidity in Banking Organizations

Dear Dr. Wellink:

I am writing in connection with the announcement by the Basel Committee on Banking Supervision that your Working Group on Liquidity intends to update the February 2000 guidance entitled "Sound Practices for Managing Liquidity in Banking Organizations" in light of the recent market turmoil. I strongly agree with you that the events earlier this month leading up to the acquisition of Bear Stearns by JP Morgan Chase highlight the importance of liquidity management in meeting obligations during stressful market conditions.

I also strongly support your decision to update the guidance for managing liquidity in banking organizations.

To assist the Working Group in its task, this letter provides you with specific information regarding Bear Stearns' capital and liquidity positions in the days preceding its transaction with JP Morgan Chase. I hope this very recent data will prove valuable as the Working Group examines its guidance on liquidity management practices.

As you will see, the conclusion to which these data point is that the fate of Bear Stearns was the result of a lack of confidence, not a lack of capital. When the tumult began last week, and at all times until its agreement to be acquired by JP Morgan Chase during the weekend, the firm had a capital cushion well above what is required to meet supervisory standards calculated using the Basel II standard.

Specifically, even at the time of its sale on Sunday, Bear Stearns' capital, and its broker-dealers' capital, exceeded supervisory standards. Counterparty withdrawals and credit denials, resulting in a loss of liquidity – not inadequate capital – caused Bear's demise.

It is worth noting, however, that net capital rules are designed to preserve investors' funds and securities in times of market stress, and they served that purpose in this case. This investor protection objective was amply satisfied by the current net capital regime, which -- together with the protection provided by the Securities Investor Protection Corporation (SIPC) and the requirement that SEC-regulated broker-dealers segregate customer funds and fully-paid securities from those of the firm -- worked in this case to fully protect Bear's customers.

Data Concerning Bear Stearns' Liquidity and Broker-Dealer Regulatory Capital

The following data provided to our Division of Trading and Markets by Bear Stearns describe the firm's capital and liquidity position at the holding company level prior to and during last week's events, and the capital in the firm's two SEC-registered broker-dealers:

BSSC Net Capital (\$ billion)

	<u>Required</u>	<u>Excess</u>
31-Dec	1.26	3.38
31-Jan	1.30	2.92
14-Mar	1.27	>2.00 (estimated)

BS&Co. Net Capital (\$ billion)

	<u>Required</u>	<u>Excess</u>
31-Jan	0.56	2.71
14-Mar	0.58	> 2.00 (estimated)

Liquidity Pool (\$ billion)

31-Jan	8.4
4-Feb	12.8
5-Feb	15.8
6-Feb	17
7-Feb	16.1
22-Feb	15
23-Feb	15
24-Feb	15
25-Feb	18
26-Feb	19
27-Feb	19
28-Feb	19
29-Feb	19
1-Mar	19

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2-Mar	19
3-Mar	20
4-Mar	20.1
5-Mar	21
6-Mar	21
7-Mar	18
8-Mar	18
9-Mar	18
10-Mar	18.1 (15.1 adjusted for customer protection rule)
11-Mar	11.5 (15.8 adjusted for customer protection rule)
12-Mar	12.4
13-Mar	2

Holding Company Capital Ratio

31-Dec	13.7%
31-Jan	14.4%
29-Feb	13.5% (estimated)

The data above show that Bear Stearns' registered broker-dealers were comfortably in compliance with the SEC's net capital requirements, and in addition that Bear Stearns' capital exceeded relevant supervisory standards at the holding company level. Specifically, throughout the week of March 10 until the closing of the JP Morgan Chase transaction on Sunday March 16, Bear Stearns had a capital ratio of well in excess of the 10% level used by the Federal Reserve Board in its "well-capitalized" standard.

The data above also reflect the fact that the holding company had a pool of high quality, highly liquid assets of over \$18 billion as of the morning of March 11. This was consistent with what the SEC had seen over the preceding weeks, during which SEC staff – both on-site and at headquarters – monitored the capital and liquidity positions of all the CSEs, in the case of Bear Stearns on a daily basis.

In accordance with customary industry practice, Bear Stearns relied day-to-day on its ability to obtain short-term financing through borrowing on a secured basis. Beginning late Monday, March 10, and increasingly through the week, rumors spread about liquidity problems at Bear Stearns, which eroded investor confidence in the firm. Notwithstanding that Bear Stearns continued to have high quality collateral to provide as security for borrowings, market counterparties became less willing to enter into collateralized funding arrangements with Bear Stearns. This resulted in a crisis of confidence late in the week.

In particular, counterparties to Bear Stearns were unwilling to make secured funding available to Bear Stearns on customary terms.

This unwillingness to fund on a secured basis placed enormous stress on the liquidity of the firm. On Tuesday, March 11, the holding company liquidity pool declined from \$18.1 billion to \$11.5 billion. This improved on Wednesday, March 12, when Bear

