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November 2011

The Volcker Rule Proposal – Many Questions, Few Answers

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Recently, the Securities and Exchange Commission ("SEC") joined the three federal banking agencies, the Federal Reserve Board ("FRB"), Federal Deposit Insurance Corporation ("FDIC") and the Office of the Comptroller of the Currency ("OCC") (collectively, the "Agencies"), in issuing an interagency proposal on the so-called "Volcker Rule" under the Dodd-Frank Act.[1] The proposal seeks comment on almost 400 questions (**see attached**) regarding all aspects of the Volcker Rule's restrictions on the ability of a bank to engage in proprietary trading and invest in hedge funds and private equity funds. In addition, the proposed rule seeks comment on a number of controversial recordkeeping, reporting and related compliance questions raised in the proposal. While there is some sentiment that only the very largest banks need to be concerned about the Volcker Rule, a survey of the questions in the proposed rule suggests all institutions should be carefully reviewing and considering commenting on the proposal by the January 13, 2012 comment deadline.

This is the first in a series of client alerts that will be issued by Paul Hastings over the upcoming weeks exploring various aspects, issues and challenges presented by the currently proposed rule to implement the Volcker Rule. This alert presents an overview of the structure and the Agencies' proposal and discusses the general parameters of the proposed rule and some of the important themes and issues raised by the proposal.

The attached questions raised by the Agencies in the proposed rule are sorted by subject area and numbered the same as in the proposal. Generally, the discussion and related questions are broken out into the following six categories:

- Subpart A – Authority and Definitions (13 questions)
- Subpart B – Proprietary Trading Restrictions (201 questions)
- Subpart C – Covered Fund Activities and Investments (103 questions)
- Subpart D – Compliance Program Requirement, and Appendix C, Minimum Standards for Programmatic Compliance (28 questions)
- Economic Impact Assessment, and Paperwork Reduction Act Analysis (40 questions, including five items under the Paperwork Reduction Act)
- SEC Additional Matters (12 questions)

While three-quarters of the questions address issues in the two core areas of the Volcker Rule – proprietary trading and investments in covered funds – the remaining questions raise equally important policy considerations for which the Agencies are seeking comment. There are numerous themes and key issues highlighted in the proposal, many of which have significant implications for banks, including banks that have no trading desk or that have effectively dissolved their trading operations. Trading desk or not, it appears that the Volcker Rule will require careful planning and execution to model a program to assure and maintain compliance.

Important Themes and Issues

Restriction on Proprietary Trading

The most prominent provision of the Volcker Rule and the proposal is the restriction on the ability of banks to engage in proprietary trading.[2] As noted above, issues and questions related to the prohibition on proprietary trading consume roughly one half of the discussion in the Agencies' proposal. Generally, the issues revolve around a number of key areas, including relevant definitions and the scope of various exemptions. In reviewing and in considering comments to the proposed rule, banks should pay particular attention to the following:

- **Definition of "Banking Entity"** – The rule would restrict proprietary trading by a "banking entity." As currently proposed, the term "banking entity" includes an insured depository institution, its holding company, subsidiaries and affiliates, a "covered fund" that is organized, offered and held by a banking entity, and an entity controlled by a covered fund.[3] Generally, any entity within a consolidated holding company structure of an FDIC-insured bank would be deemed a "banking entity." The term would also include the U.S. operations of foreign banks treated as bank holding companies and subject to oversight of the FRB with respect to their U.S. bank operations.

- **Definition of "Proprietary Trading"** – Under the proposal, "proprietary trading" generally means engaging *as principal* for the trading account of a covered banking entity in the purchase or sale of a covered financial position.[4] An important aspect of this definition is the concept of engaging "as principal," which is the subject of discussion in the proposal and forms the basis for several exemptions highlighted below.[5]

- **Definition of "Trading Account"** – The proposal defines a "trading account" as any account used by a covered banking entity to acquire one or more covered financial positions principally for short-term resale, short-term price movement, short-term arbitrage profits, or hedging a position in one of these. A "trading account" also includes acquiring a covered financial position (other than certain foreign exchange and commodity derivatives) by a banking entity subject to the market risk capital rule, and certain transactions entered into by banking entities that are government securities or swap dealers (and certain other exclusions).[6]

- **Definition of "Covered Financial Position"** – A "covered financial position" under the proposed rule includes any long, short, synthetic, other position in a security or derivative, or a commodity sale contract (or an option on any of these positions or contracts).[7] Excluded from a "covered financial position" are positions in a loan, commodity, or foreign exchange or currency (but not a position in a commodity or foreign exchange derivative).

- **Rebuttable Presumption of a Trading Account** – Another important concept embedded in the proposed rule is a rebuttable presumption that an account is a trading account if it is used to acquire or take a covered financial position (other than a market risk capital rule

covered position and certain positions by a banking entity acting as a government securities or swap dealers) that the banking entity holds for 60 days or less.[8] As currently proposed, the presumption can be rebutted where the banking entity can demonstrate, based on all the facts and circumstances, that the covered financial position was not acquired for short-term gain or to hedge a position for short-term gain. In effect, this presumes that positions held for 60 days or less are acquired with short-term trading intent, unless the banking entity can demonstrate otherwise.

Notable in the proposal's discussion of the rebuttable presumption is a statement that the "presumptions are designed to help determine whether a transaction is within the definition of 'proprietary trading,' not whether a transaction is permissible." The commentary further notes "a transaction may fall within the definition of 'proprietary trading' and yet be permissible if it meets one of the exemptions provided in the proposed rule." For example, certain underwriting and market making activities would qualify as proprietary trading but for an exemption provided in the rule. This ties back to the concept of trading "as principal," as discussed above and highlighted in the following discussion of the available exemptions to the general prohibition on proprietary trading.

Statutory Exemptions: Permitted Trading Activities

While the restrictions on proprietary trading provide one dimension of the general prohibition, the proposal is further defined by the exemptions for permitted trading activities. Generally, the proposed rule closely tracks the statutory exemptions of the Volcker Rule. The more prominent of these include the following:

- **Underwriting Exemption** – The prohibition on proprietary trading does not apply to the purchase or sale of a covered financial position by a banking entity in connection with its underwriting activities. Generally, a covered financial position is deemed to be made in connection with underwriting activities if all of the requirements are satisfied:[9]

  i. The banking entity has an established internal compliance program to ensure, among other things, that the subject activities are underwriting activities;

  ii. The covered financial positions is a security;

  iii. The purchase or sale is effected solely in connection with a distribution of securities for which the covered banking entity is acting as underwriter;

  iv. If the subject underwriting requires the banking entity to be registered as a "securities dealer," the banking entity has the appropriate dealer registration or otherwise is exempt or excluded from registration;

  v. The underwriting activities with respect to the covered position are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties;

  vi. The underwriting activities are designed to generate revenues primarily from fees, commissions, or income not attributable to price appreciation or hedging related to such activities; and

  vii. Compensation arrangements of persons performing the underwriting activities do not reward proprietary risk-taking.

- **Market Making Exemption** -- The prohibition on proprietary trading also does not apply to the purchase or sale of a covered financial position by a covered banking entity in connection with its market making-related activities. Generally, a purchase or sale of a covered financial

position shall be deemed to be made in connection with a banking entity's market making-related activities if all of the following requirements are met:[10]

i. The banking entity has an established internal compliance program to ensure, among other things, that the subject activities are market making-related activities;

ii. The activities are *bona fide* market making activities in that the banking entity holds itself out as being willing to buy and sell the covered financial position for its own account on a regular or continuous basis (i.e., it is actually making a market in the covered financial position);

iii. The market making-related activities are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties;

iv. The covered banking entity is registered as a dealer in the type of securities for the covered financial position in which it is making a market;

v. The activities are designed to generate revenues primarily from fees, commissions, bid/ask spreads or other income not attributable to price appreciation or the hedging of covered financial positions it holds in trading accounts;

vi. The activities are consistent with commentary in the proposed rule describing the features of permitted market making-related activities and distinctions between permitted market making-related activities and prohibited proprietary trading; and

vii. Compensation arrangements of persons performing the market making-related activities are designed not to reward proprietary risk-taking.

Importantly, a purchase or sale of a covered financial position taken as a hedge to reduce the specific risks to the covered banking entity from its market making activities will be covered by the market making exemption provided the hedging activity otherwise satisfies the requirements of and documentation for the hedging exemption described below.

- **Risk-Mitigating Hedging Exemption** – Another exemption to the prohibition on proprietary trading is the risk-mitigating hedging exemption. This exemption covers a banking entity's purchase or sale of a covered financial position designed to reduce specific risks in connection with or related to certain positions, contracts, or other holdings of the banking entity. The exemption is available provided certain requirements and documentation procedures are satisfied, including the following:[11]

i. The banking entity has an established internal compliance program to ensure, among other things, that the subject activities are risk-mitigating hedging activities, including written policies and procedures regarding the instruments, techniques and strategies that may be used for permissible hedging activities;

ii. The purchase or sale, among other things: (a) hedges or otherwise mitigates one or more specific risks arising from positions, contracts or holdings of the banking entity, (b) is reasonably correlated to the risk(s) the purchase or sale is intended to hedge or mitigate, (c) does not create significant exposures, (d) is subject to continuing review and monitoring by the banking entity; and (e) compensation arrangements of persons performing the risk-mitigating hedging activities do not reward proprietary risk-taking; and

iii. Documentation to establish, for any risk-mitigating hedging activities conducted at a level of organization different than the level in which the risk being hedged arose, at the time a purchase or sale is conducted: (a) the risk-mitigating purpose of the transaction; (b) the risks the hedging activity is designed to reduce, and (c) the level of organization establishing the hedge.

- **Trading on Behalf of Customers** – A final important proprietary trading exemption is a banking entity's permitted trading on behalf of its customers. Generally, the exemption covers three broad classes of customer-related trading activity:[12]

  i. A purchase or sale conducted by a banking entity acting as an investment adviser, trustee, or in a similar fiduciary capacity for a customer, that is conducted for the account of the customer involving solely covered financial positions of which the customer is beneficial owner;

  ii. Transactions in which the banking entity is acting as riskless principal pursuant to a customer order to purchase or sell a covered financial position; or

  iii. Transactions in which a banking entity that is a "Regulated Insurance Company" purchases or sells a covered financial position solely for the separate account of its insurance policyholders, and all profits of such transaction inure to the benefit (or detriment) of such policyholders.

Restriction on Covered Fund Investments

The general restriction on covered fund investments provides that a banking entity may not, as principal, directly or indirectly, acquire or retain any ownership interest in or sponsor a covered fund. While half as many questions (and pages) are dedicated in the proposal to this restriction compared to the prohibition on proprietary trading, the potential impact on this aspect of banks' activities is equally compelling. Also, as with the restriction on the prohibition on proprietary trading, the concept of engaging "as principal" is an important gating issue in the covered fund context. Following are some of the key issues, definitions and scope of various exemptions set forth in the proposed rule on which banks may want to consider commenting:[13]

- **Definition of "Covered Fund"** – The proposal closely tracks the statute by defining what is a "covered fund" by reference to the exclusions provided in the Investment Company Act for a "hedge fund" or "private equity fund" being treated as an "investment company."[14] As noted in the proposal, a wide variety of entities rely on these exclusions. As a consequence, the definition of "covered fund" could potentially include many entities and corporate structures not usually considered a "hedge fund" or "private equity fund." These include "joint ventures, acquisition vehicles, certain wholly-owned subsidiaries, and other widely-utilized corporate structures" that rely on the Investment Company Act exclusions, but are not typically used to engage in investment or trading activities. In addition, certain securitization vehicles could be pulled into the "covered fund" definition. Finally, pursuant to their authority to subject "similar funds" to the rule, the Agencies include commodity pools, and the foreign equivalent of any entity identified as a "covered fund" within the proposed "covered fund" definition.

- **Definition of "Ownership Interest"** – Under the proposal's covered fund investment provisions, the definition of "ownership interest" would include any equity, partnership, or other similar interest, *as principal*, in a covered fund, whether voting or nonvoting, as well as any derivative of such interest.[15] It would also include a debt security or other interest that exhibits substantially the same characteristics as an equity interest or other ownership interest in a covered fund.

  Perhaps the most significant aspect of the "ownership interest" definition is the exclusion of "carried interest," including an interest held in which the banking entity serves as an investment manager or adviser.[16] To be excluded, the sole purpose and effect of the carried interest must be to allow the banking entity to share in the profits of the covered fund as

performance compensation for services provided to the covered fund by the banking entity, subject to certain additional restrictions on acquiring and holding the carried interest.

- **Definition of "Sponsor"** – With respect to the restriction on covered fund sponsorship, the proposed rule defines the term "sponsor" as:[17]

  i. An entity serving as a general partner, managing member, trustee, or commodity pool operator of a covered fund;

  ii. An entity that selects or controls a majority of the directors, trustees, or management of a covered fund; or

  iii. An entity sharing the same name or a similar name (for various purposes) with a covered fund.

  As noted in the proposal, the definition of "sponsor" generally focuses on the ability to control the decision-making and operational functions of the fund. In this respect, the reference to the term "trustee" excludes a trustee that does not exercise investment discretion with respect to a covered fund, including a directed trustee under ERISA. Rather, a "trustee" includes "any banking entity that directs a directed trustee, or any person who possesses authority and discretion to manage and control the assets of a covered fund."

- **"As Principal" Determination** – As noted above, the concept of "as principal" is important to both the proprietary trading and covered fund provisions of the proposed rule. An important analysis of the "as principal" determination is set forth in the covered fund discussion where the Agencies note that the covered fund prohibition "applies solely to a banking entity's acquisition or retention of an ownership interest in or acting as sponsor to a covered fund 'as principal, directly or indirectly.'" Pursuant to the analysis, the acquisition of an ownership interest in a covered fund would be permissible by:

  i. A banking entity acting in good faith in a fiduciary capacity, except if the ownership interest is held under a trust treated as a bank holding company under the Bank Holding Company Act ("BHCA");

  ii. A banking entity acting in good faith in its capacity as a custodian, broker, or agent for an unaffiliated third party;

  iii. A "qualified plan," as that term is defined in section 401 of ERISA,[18] if the ownership interest is attributed to a banking entity because the plan is deemed an "affiliate" of the bank pursuant to section 2(g)(2) of the BHCA;[19] or

  iv. A director or employee of a banking entity who acquires the interest in his or her personal capacity and who is directly engaged in providing advisory or other services to the covered fund, except where the banking entity extended credit for the purchase of such ownership interest in the fund.

- **Restrictions on Transactions with a Covered Fund** – The proposal would also restrict the ability of a banking entity to enter into certain transactions with a covered fund that would be deemed "covered transactions" under the transactions with affiliate provisions of section 23A of the Federal Reserve Act ("FRA").[20] Certain other transactions under the proposal, including so-called "prime brokerage transactions," would be permissible but subject to the FRA § 23B requirements that the transaction be on "market terms or on terms at least as favorable to the banking entity as a comparable transaction by the banking entity with an unaffiliated third party."[21] Finally, a banking entity could engage in so-called "prime brokerage transactions" with a covered fund in which a covered fund managed, sponsored, or advised by the banking entity has taken an ownership interest.[22] Under the proposal, such "prime brokerage transactions" include "products or services provided by a covered banking

entity to a covered fund, such as custody, clearance, securities borrowing or lending services, trade execution, or financing, data, operational, and portfolio management support."[23]

Statutory Exemptions: Permitted Investments in Covered Funds

A considerable portion of the provisions of the proposal addressing the restrictions on covered funds involve the statutory permitted investments under the Volcker Rule. These include the following:

- **Permitted Organizing and Offering Exemption** – The organizing and offering exemption permits a banking entity to organize, offer and/or sponsor a covered fund if certain criteria are met. Generally, the exemption permits a banking entity to engage in certain traditional asset management and advisory businesses, subject to the following conditions:[24]

  i. The banking entity must provide *bona fide* trust, fiduciary, investment advisory or commodity trading advisory services to a covered fund organized and offered only in connection with the provision of such services to persons that are customers of such services of the banking entity;

  ii. The banking entity may not acquire or retain an ownership interest in the covered fund except as specifically permitted by the proposed rule;

  iii. The banking entity must comply with the restrictions governing transactions and relationships with covered funds under the proposed rule;

  iv. The banking entity may not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of the covered fund or of any covered fund in which such covered fund invests;

  v. The covered fund and banking entity may not share the same or a similar name and the fund may not use the word "bank" in its name;

  vi. No director or employee of the banking entity may take or retain an ownership interest in the covered fund (subject to certain exceptions); and

  vii. The banking entity must clearly and conspicuously disclose to investors that losses in the covered fund will be borne solely by investors and not by the banking entity, and comply with any agency rules designed to ensure the same.

- **Establishing/Seeding Exemption** – Under this exemption, a banking entity may invest in a covered fund to establish the fund and provide it with sufficient initial equity to permit the fund to attract unaffiliated investors, provided the following conditions are met:[25]

  i. The banking entity actively seeks unaffiliated investors to ensure that its investment ultimately conforms with the investment limits of the rule (as noted below);

  ii. The banking entity reduces through redemption, sale or other methods its aggregate investment in a single fund to three percent or less of the total outstanding ownership interests of the fund not later than one year after the date of establishment of the fund (subject to an additional two year extension, with prior approval); and

  iii. The aggregate value of all ownership interests of the banking entity in all covered funds does not exceed three percent of the tier 1 capital of the banking entity.

- **De Minimus Investment Exemption** – The "de minimum" exemption is similar to the preceding seeding exemption and generally imposes three limitations on a banking entity's investment in covered funds, subject to special rules on the method of calculation, as follows:[26]

i. First, the banking entity's investment in a single covered fund cannot exceed more than three percent of the total outstanding ownership interests of such fund (i.e., after the expiration of any seeding period noted above);

ii. Second, the banking entity's investment in a single covered fund cannot result in more than three percent of the losses of the covered fund being allocable to the banking entity's investment; and

iii. Third, the banking entity's aggregate investment in all covered funds cannot exceed three percent of its tier 1 capital.

- **Foreign Bank Exemption** – Another important exemption to the covered fund restrictions highlighted in the proposal is the foreign bank exemption.[27] Under this exemption, certain foreign banking entities may invest in or sponsor a covered fund, provided the activity occurs solely outside the U.S. and the investing entity qualifies under section 4(c)(9) or 4(c)(13) of the BHCA.[28] As noted in the proposal, this "limits the extraterritorial application of the statutory restrictions on covered fund activities and investments to foreign firms that, in the course of operating outside of the United States, engage in activities permitted under relevant foreign law outside of the United States, while preserving national treatment and competitive equality among U.S. and foreign firms within the United States." Specifically, the proposal notes that a banking entity cannot be, directly or indirectly, controlled by a banking entity organized under U.S. or State law. This includes U.S. subsidiaries and U.S. branches of foreign banking entities subject to FRB supervision under the BHCA.

  Under the "solely outside the U.S." requirement, a transaction or activity must satisfy three conditions to be deemed solely outside the U.S.:

  i. The transaction or activity must be conducted by a banking entity not organized under U.S. law or the laws of one or more States;

  ii. No subsidiary, affiliate, or employee of the banking entity involved in the offer or sale of an ownership interest in the covered fund can be incorporated or physically located in the U.S.; and

  iii. No ownership interest in the covered fund can be offered for sale or sold to a "U.S. resident" (as further defined in the proposal).

- **Loan Securitization Exemption** – The loan securitization exemption permits a banking entity to hold or sponsor an ownership interest in a covered fund that is an issuer of asset-backed securities, provided certain conditions are satisfied. These include that the fund assets consist solely of loans, contractual rights or assets directly arising from loans supporting the asset-backed securities, and/or a limited amount of interest rate or foreign exchange derivatives that materially relate to such loans if used for hedging purposes with respect to the securitization structure.[29] This would allow a banking entity to hold an ownership interest in excess of the rule's three percent limit in a loan securitization vehicle the banking entity organizes, offers or sponsors.

- **Other Available Exemptions** – Several additional exemptions set forth in the covered fund restriction are:

  i. Risk-Mitigating Hedging Exemption, which permits a banking entity to acquire an ownership interest in a covered fund to hedge certain obligations or liabilities arising from the banking entity acting on behalf of a customer to facilitate the customer's exposure to the profits and losses of the covered fund. It would also allow for a compensation arrangement with a banking entity's employee who directly provides

investment advisory or other services to the fund (both of which are subject to certain additional requirements).[30]

ii. SBIC and Public Welfare Investment Exemption, for investments in certain funds satisfying the requirements for such exemptions under the proposal.[31]

iii. Financial Stability Exemption, which is limited to three specific activities under the proposal that promote and protect the safety and soundness of banking entities. These relate to bank owned life insurance ("BOLI") accounts, certain asset-basked securitizations, and certain common corporate organizational vehicles.[32]

Volcker Rule Compliance Program Requirements

The final set of significant issues raised by the proposal involves the third major – and perhaps most controversial – aspect of the proposed rule, the compliance program requirements. Generally, these would require a banking entity engaged in covered trading or covered fund activities to develop and implement a compliance program reasonably designed to ensure and monitor compliance with the requirements of the Volcker Rule, including:

- Written policies and procedures reasonably designed to document, describe, and monitor covered trading and covered fund activities and investments;
- Internal controls reasonably designed to monitor and identify potential areas of noncompliance with the rule;
- A management framework that clearly delineates responsibility and accountability for compliance with the rule ;
- Independent testing for the effectiveness of the compliance program, conducted by qualified bank personnel or a qualified outside party;
- Training for trading personnel, managers and other personnel to implement and enforce the compliance program; and
- Recordkeeping sufficient to demonstrate compliance with the rule, which must be available to the Agencies (for five years) upon request.

For banking entities with significant covered trading or covered fund activities, the above compliance program requirements would have to satisfy a number of additional standards related to documenting, describing, and monitoring the covered trading and covered fund activities and risks to the banking entity, preventing activities prohibited by the rule, and various other requirements related to the program. These additional standards would not apply to smaller and less complex banking entities, but could be used as guidance in designing a compliance program for such institutions.

Timing and Implementation

The Volcker Rule is required to be implemented by July 21, 2012. With a comment deadline of January 13, 2012 for a proposed rule that poses almost 400 questions, this provides little time for the Agencies to finalize the proposal before the rule itself is scheduled to be effective. This imposes a significant imperative that comments on the proposed rule be effectively and carefully drafted to highlight commenters' specific issues and concerns with the proposal. Given the difficulties that the Agencies will confront in finalizing the numerous complex, difficult and controversial aspects of the Volcker Rule's restrictions on proprietary trading and covered fund investments, it appears likely that the industry may have little, if any, time to adjust to the final rule. This is a particular concern with the proposed compliance program requirements, if finalized in or similar to their current form. Thus,

timing and process, as well as substance, pose significant challenges for the industry and the Agencies with respect to implementation of the Volcker Rule.

Agency and Industry Challenges

Procedural and substantive issues present significant challenges for the Agencies and industry in connection with final implementation of the Volcker Rule. Complicating these challenges are an aggressive timeframe, a highly charged political climate, significant and broader policy implications, and numerous uncertainties with respect to interpretations, definitions and legislative and regulatory intent on a host of potential issues that agency staff are struggling with in implementing the requirements of the Volcker Rule. The impact of the new rule may also be particularly difficult for larger, more complex institutions that could be required to implement complicated compliance program requirements, as well as significant changes that may significantly alter certain fundamental aspects of their existing business operations.

Action Plan – Review Details of the Proposed Rule and Questions, and Provide Comments to Questions Having a Potentially Significant Impact on Your Banking Operations

The Volcker Rule is one of the most complicated provisions of the Dodd-Frank Act, and raises numerous novel questions and issues regarding the existing operations of covered banking entities. The rule is further hampered by a difficult political and regulatory environment, and a short implementation timeframe, among other problems and issues. All of this suggests an important, if not compelling need to provide guidance to the Agencies by way of comments to the questions posed in the proposed rule.

As a banking entity, you should be undertaking an entire review of your existing trading program, as well as your investment activities with respect to covered funds, to assess the overall potential impact of the Volcker Rule and, most immediately, the steps you may have to take to ensure compliance by July 21, 2012 (assuming this statutory deadline will remain the effective date of the rule). As with any new regulatory compliance requirement, an important challenge is to understand the nature of the underlying vulnerabilities of your existing programs and potential risks to your banking entity's ongoing operations, policies and programs. Certainly, one of the most important steps you can take will be to reach out to advisors, experts and regulators, as well as industry peers, when issues arise. Most importantly, you should inform yourself regarding what will be a dynamic discussion of the regulatory and supervisory issues and developments with the Agencies' implementation of the Volcker Rule over the coming months. In particular, you should pay attention to and consider participating in all opportunities to discuss issues with the regulators (which may be somewhat problematic during the pending comment period) and other industry advisers regarding new developments.

Finally, you should carefully review the attached questions compiled from the proposed rule to assess the potential impact on your existing programs to evaluate the operational, compliance, reputational, and other risks to your organization. Key areas to monitor throughout your organization include the following:

- *Identify all trading activities subject to the requirements of the Volcker Rule, as well as what activities and investments would be exempt from these requirements under the rule;*
- *Identify all covered fund activities subject to the requirements of the Volcker Rule; as well as what activities and investments would be exempt from these requirements under the rule;*

- *Determine the steps you must take, if any, with respect to each of the activities and investments subject to the restrictions on proprietary trading and covered fund investments under the proposal, including compliance program requirements under the rule;*
- *Initiate discussions with legal advisors and consultants to determine what steps you may have to take to be in compliance with the rule by the July 21, 2012 effective date;*
- *Identify services, products and programs upon which you rely on third party service providers to assess and communicate regarding what steps would be necessary to ensure their and your compliance with the rule, as currently proposed, on the applicable effective date;*
- *Provide comments, and raise issues and questions both to inform the regulators regarding potential problems and concerns, and to ensure adequate time to make any required adjustments to your programs under the rule, as currently proposed;*
- *Conduct an assessment of the potential operational, compliance, reputational, and other risks to your organization arising from the rule, as currently proposed;*
- *Work closely with third party service providers to understand compliance expectations and certifications that will be required on their part to ensure compliance with the rule's proposed compliance program requirements; and*
- *Most importantly, fully understand all of the requirements with which your organization may be expected to comply with, including the restriction on proprietary trading and investments in covered funds under the proposed rule.*

Paul Hastings attorneys are actively working with clients to identify and address the issues and risks related to implementation of the Volcker Rule, including the ban on proprietary trading, restrictions on investing in or sponsoring a hedge fund or private equity fund, and the proposed compliance program requirements of the proposal. We are available to advise you with respect to the potential applicability and impact of the rule on these programs at your institution.

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If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

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[1] Section 619, Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (July 21, 2010).

[2] Proposed Rule, Subpart B.

[3] Proposed Rule § .2(e).

[4] Proposed Rule § .3(b)(1).

[5] As noted below, the "as principal" concept is also relevant to the rule's restriction on covered fund activities and investments.

[6] Proposed Rule § .3(b)(2).

[7] Proposed Rule § .3(b)(3).

[8] Proposed Rule § .3(b)(2)(ii).

[9] Proposed Rule § .4(a).

[10] Proposed Rule § .4(b)

[11] Proposed Rule § .5.

[12] Proposed Rule § .6(b).

[13] Proposed Rule, Subpart C.

[14] Proposed Rule § .10(b)(1). The exclusions are set forth in sections 3(c)(1) and 3(c)(7) of the Investment Company Act, 15 USC § 80a-3(c)(1) and (c)(7).

[15] Proposed Rule § .10(b)(3)(i).

[16] Proposed Rule § .10(b)(3)(ii).

[17] Proposed Rule § .10(b)(5).

[18] 26 USC § 401.

[19] The reference to BHCA § 2(g)(2) provides that shares held directly or indirectly by trustees for the benefit of the employees of a company are deemed to be controlled by such company. Thus, the reference excluding attribution (and control) under BHCA § 2(g)(2) appears to support the conclusion that a bank-sponsored pension plan's investment would not be deemed to be made "as principal" by the banking entity. We note, however, that caution should be exercised to ensure the plan trustee is acting within its fiduciary capacity and not at the direction, control, or in the interest of the banking entity. Otherwise, plan assets could be aggregated with other investments of the banking entity in the covered fund. In this regard, there is language later in the discussion noting that a "trustee" includes any banking entity that directs a directed trustee (as that term is used in ERISA § 403(a)(1)), or any person who possesses authority and discretion to manage and control the assets of a covered fund. This could be problematic where a bank and its pension fund are invested in the same fund and the bank is able to influence the pension fund trustee.

[20] 12 USC § 371c.

[21] 12 USC § 371c-1.

[22] Proposed Rule § .16.

[23] Proposed Rule § .10(b)(4).

[24] Proposed Rule § .11.

[25] Proposed Rule § .12(a)(1)(i) and (2).

[26] Proposed Rule § .12(a)(1)(ii), (b),(c) and (d).

[27] Proposed Rule § .13(c).

[28] 12 USC § 1843(c)(9) or (c)(13).

[29] Proposed Rule § .13(d).

[30] Proposed Rule § .13(b).

[31] Proposed Rule § .13(a).

[32] Proposed Rule § .14.

Subpart A – Authority and Definitions

To help assess the effects and impact of the proposed effective date and any alternative compliance dates, the Agencies request comment on the following:

Question 1. Does the proposed effective date provide banking entities with sufficient time to prepare to comply with the prohibitions and restrictions on proprietary trading and covered fund activities and investments? If not, what other period of time is needed and why?

Question 2. Does the proposed effective date provide banking entities with sufficient time to implement the proposal's compliance program requirement? If not, what are the impediments to implementing specific elements of the compliance program and what would be a more effective time period for implementing each element and why?

Question 3. Does the proposed effective date provide banking entities sufficient time to implement the proposal's reporting and recordkeeping requirements? If not, what are the impediments to implementing specific elements of the proposed reporting and recordkeeping requirements and what would be a more effective time period for implementing each element and why?

Question 4. Should the Agencies use a gradual, phased in approach to implement the statute rather than having the implementing rules become effective at one time? If so, what prohibitions and restrictions should be implemented first? Please explain.

With respect to the proposed rule's definition of "banking entity," the Agencies request comment on the following:

Question 5. Is the proposed rule's definition of banking entity effective? What alternative definitions might be more effective in light of the language and purpose of the statute?

Question 6. Are there any entities that should not be included within the definition of banking entity since their inclusion would not be consistent with the language or purpose of the statute or could otherwise produce unintended results? Should a registered investment company be expressly excluded from the definition of banking entity? Why or why not?

Question 7. Is the proposed rule's exclusion of a covered fund that is organized, offered and held by a banking entity from the definition of banking entity effective? Should the definition of banking entity be modified to exclude any covered fund? Why or why not?

Question 8. Banking entities commonly structure their registered investment company relationships and investments such that the registered investment company is not considered an affiliate or subsidiary of the banking entity. Should a registered investment company be expressly excluded from the definition of banking entity? Why or why not? Are there circumstances in which such companies should be treated as banking entities subject to section 13 of the BHC Act? How many such companies would be covered by the proposed definition?

Question 9. Under the proposed rule, would issuers of asset-backed securities be captured by the proposed definition of "banking entity"? If so, are issuers of asset-backed securities within certain asset classes particularly impacted? Are particular types of securitization vehicles (trusts, LLCs, etc.) more likely than others to be included in the definition of banking entity? Should issuers of asset-

backed securities be excluded from the proposed definition of "banking entity," and if so, why? How would such an exclusion be consistent with the language and purpose of the statute?

Question 10. What would be the potential impact of including existing issuers of asset-backed securities83 in the proposed definition of "banking entity" on existing issuers of asset-backed securities and the securitization market generally? How many existing issuers of asset-backed securities might be included in the proposed definition of "banking entity"? Are there ways in which the proposed rule could be amended to mitigate or eliminate potential impact, if any, on existing asset-backed securities84 without compromising the intent of the statute?

Question 11. What would be the legal and economic impact to an issuer of asset-backed securities of being considered a "banking entity"? What additional costs would be incurred in the establishment and implementation of a compliance program related to the provisions of the proposed rule as required by § __.20 of the proposed rule (including Appendix C, where applicable)? Who would pay those additional costs?

Question 12. If the ownership requirement under the proposed rule for credit risk retention (section 15G of the Exchange Act) combined with the control inherent in the position of servicer or investment manager means that more securitization vehicles would be considered affiliates of banking entities, would fewer banking entities be willing to (i) serve as the servicer or investment manager of securitization transactions and/or (ii) serve as the originator or securitizer (as defined in section 15G of the Exchange Act) of securitization transactions? What other impact might the potential interplay between these rules have on future securitization transactions? Could there be other potential unintended consequences?

Question 13. Are the proposed rule's definitions of buy and purchase and sale and sell appropriate? If not, what alternative definitions would be more appropriate? Should any other terms be defined? If so, are there existing definitions in other rules or regulations that could be used in this context? Why would the use of such other definitions be appropriate?

Subpart B – Proprietary Trading Restrictions

The Agencies request comment on the following with respect to the proposed rule's approach to defining "trading account":

Question 14. Is the proposed rule's definition of trading account effective? Is it over- or under-inclusive in this context? What alternative definition might be more effective in light of the language and purpose of the statute? How would such definition better identify the accounts that are intended to be covered by section 13 of the BHC Act?

Question 15. Is the proposed rule's approach for determining when a position falls within the definition of "trading account" for purposes of the proposed rule from when it must be reported in the "trading account" for purpose of filing the Call Report effective? What additional guidance could the Agencies provide on this distinction? Are there alternative approaches that would be more effective in light of the language and purpose of the statute? Is this approach workable for affiliates of bank holding companies that are not subject to the Federal banking agencies' market Risk Capital Rules (e.g., affiliated investment advisers)? If not, why not? Are affiliates of bank holding companies familiar with the concepts from the Market Risk Capital Rules that are being incorporated into the proposed rule? If not, what steps would an affiliate of a bank holding company have to take to become familiar with

these concepts and what would be the costs and/or benefits of such actions? Is application of the trading account concept from the Federal banking agencies' Market Risk Capital Rules to affiliates of bank holding companies necessary to promote consistency and prevent regulatory arbitrage? Please explain. Question 16. Is the manner in which the Agencies intend to take into account, and substantially adopt, the approach used in the Market Risk Capital Rules and related concepts for determining whether a position is acquired with short-term trading intent effective?

Question 17. Should the proposed rule's definition of trading account, or its use of the term "short-term," be clarified? Are there particular transactions or positions to which its application would be unclear? Should the proposed rule define "short-term" for these purposes? What alternative approaches to construing the term "short-term" should the Agencies consider and/or adopt?

Question 18. Are there particular transactions or positions to which the application of the proposed definition of trading account is unclear? Is additional regulatory language, guidance, or clarity necessary?

Question 19. Is the exchange of variation margin as a potential indicator of short-term trading in derivative or commodity future transactions appropriate for the definition of trading account? How would this impact such transactions or the manner by which banking entities conduct such transactions? For instance, would banking entities seek to avoid the use of variation margin to avoid this rule? What are the costs and benefits of referring to the exchange of variation margin to determine if positions should be included in a banking entity's trading account? Please explain.

Question 20. Are there particular transactions or positions that are included in the definition of trading account that should not be? If so, what transactions or positions and why?

Question 21. Are there particular transactions or positions that are not included in the definition of trading account that should be? If so, what transactions or positions and why?

Question 22. Is the proposed rule of construction for positions acquired or taken by dealers, swap dealers and security-based swap dealers appropriate and consistent with the purpose and language of section 13 of the BHC Act? Is its application to any particular type of entity, such as an insured depository institution engaged in derivatives dealing activities, sufficiently clear and effective? If not, what alternative would be clearer and/or more effective?

Question 23. Is the rebuttable presumption included in the proposed rule appropriate and effective? Are there more effective ways in which to provide clarity regarding the determination of whether or not a position is included within the definition of trading account? If so, what are they?

Question 24. Are records currently created and retained that could be used to demonstrate investment or other non-trading purposes in connection with rebutting the presumption in the proposed rule? If yes, please identify such records and explain when they are created and whether they would be useful in connection with a single transaction or a category of similar transactions. If no, we seek commenter input regarding the manner in which banking entities might demonstrate investment or other non-trading intent. Should the Agencies require banking entities to make and keep records to demonstrate investment or non-trading intent with respect to their covered financial positions?

Question 25. How should the proposed trading account definition address arbitrage positions? Should all arbitrage positions be included in the definition of trading account, unless the timing of such profits is long-term and established at the time the arbitrage position is acquired or taken? Please explain in

detail, including a discussion of different arbitrage trading strategies and whether subjecting such strategies to the proposed rule would be consistent with the language and purpose of section 13 of the BHC Act.

Question 26. Is the holding period referenced in the rebuttable presumption appropriate? If not, what holding period would be more appropriate, and why?

Question 27. Should the proposed rule include a rebuttable presumption regarding positions that are presumed not to be within the definition of trading account? If so, why, and what would the presumption be?

Question 28. Should any additional accounts be included in the proposed rule pursuant to the authority granted under section 13(h)(6) of the BHC Act? If so, what accounts and why? For example, should accounts used to acquire or take certain long-term positions be included in the definition? If so, how would subjecting such accounts to the proposed rule's prohibitions and restrictions be consistent with the language and purpose of section 13 of the BHC Act?

Question 29. Do any of the activities currently engaged in by issuers of asset-backed securities that would be considered a banking entity constitute proprietary trading as defined by §__.3(b) of this rule proposal? Would any activities relating to investment of funds in accounts held by issuers of asset-backed securities (e.g., reserve accounts, prefunding accounts, reinvestment accounts, etc.) or the purchase and sale of securities as part of the management of a collateralized debt obligation portfolio be considered proprietary trading under the proposed rule? What would be the potential impact of the prohibition on proprietary trading on the use of such accounts in (i) existing securitization transactions and (ii) future securitization transactions? Would any of the securities typically acquired and retained using these accounts be considered an ownership interest in a covered fund under the proposed rule? Does the exclusion of trading in certain government obligations in § __.6(a) of the proposed rule mitigate the impact of the proposed rule on such issuers of asset-backed securities and their activities? Why or why not?

The Agencies request comment regarding the following with respect to the proposed exclusions from the definition of "trading account" and any other types of activity or transactions that should be excluded:

Question 30. Are the proposed clarifying exclusions for positions under certain repurchase and reverse repurchase arrangements and securities lending transactions over- or under-inclusive and could they have unintended consequences? Is there an alternative approach to these clarifying exclusions that would be more effective? Are the proposed clarifying exclusions broad enough to include bona fide arrangements that operate in economic substance as secured loans and are not based on expected or anticipated movements in asset prices? Are there other types of arrangements, such as open dated repurchase arrangements, that should be excluded for clarity and, if so, how should the proposed rule be revised? Alternatively, are the proposed clarifying exclusions narrow enough to not inadvertently exclude from coverage any similar arrangements or transactions that do not have these characteristics?

Question 31. Are repurchase and reverse repurchase arrangements and securities lending transactions sufficiently similar that they should be treated in the same way for purposes of the proposed rule? Are there aspects of repurchase and reverse repurchase arrangements or securities lending transactions that should be highlighted in considering the application of the proposed rule? Do repurchase and

reverse repurchase arrangements or securities lending transactions raise any additional or heightened concerns regarding risk? Please identify and explain how these concerns should be reflected in the proposed rule.

Question 32. Are the proposed exclusions for repurchase and reverse repurchase arrangements and securities lending transactions appropriate or are there conditions that commenters believe would be appropriate as a pre-requisite to relying on these exclusions? Please identify such conditions and explain. Alternatively, we seek commenter input regarding why repurchase and reverse repurchase arrangements and securities lending transactions do not present the potential for abuse, namely, that a banking entity might attempt to improperly mischaracterize prohibited proprietary trading as activity that qualifies for the proposed exclusions.

Question 33. Is the proposed clarifying exclusion for liquidity management transactions effective and appropriate? If not, what alternative would be more effective and appropriate, and why? Is the proposed exclusion under- or over-inclusive? Does the proposed clarifying exclusion place sufficient limitations on liquidity management transactions to prevent abuse of the clarifying exclusion? If not, what additional limitations should be specified? Are any of the limitations contained in the proposed rule inappropriate or unnecessary? If so, how could such limitations be eliminated or altered in way that does not permit abuse of the clarifying exclusion?

Question 34. Is the proposed exclusion for liquidity management positions necessary? If not excluded, would such activity otherwise qualify for an exemption contained in the proposed rule (e.g., the exemptions contains in §§ __.5 and __.6(a) of the proposed rule)? What types of banking entities are likely to engage in the liquidity management activities described in the proposed exclusion?

Question 35. What types of instruments do particular types of banking entities currently use in connection with liquidity management activities (e.g., Treasuries)? Why are such instruments chosen for liquidity management purposes? Would such instruments meet the proposed requirement that the position be highly liquid and limited to financial instruments the market, credit and other risk of which are not expected to give rise to appreciable profits or losses as a result of short-term price movements? Why or why not?

Question 36. What methodologies do banking entities currently use for estimating deviations from normal operations in connection with liquidity management programs?

Question 37. Which unit or units within a banking entity are typically responsible for liquidity management? What is the typical reporting line structure used to control and supervise that unit or units? Are the responsibilities of personnel in the unit limited to liquidity management or do they perform other functions in addition to liquidity management? How is compensation determined for personnel in the unit of the banking entity responsible for liquidity management?

Question 38. Would current liquidity management programs meet the five proposed criteria for liquidity management programs? If not which criteria would not be met, and why? What effect would the proposed liquidity management exclusions have on current liquidity management programs and banking entities in general?

Question 39. Are liquidity management programs used for purposes other than ensuring the banking entity has sufficient assets available to it that are readily marketable to meet expected short-term liquidity needs? If so, for what purposes, and why?

Question 40. What costs or other burdens would arise if the proposal did not contain an exclusion for positions acquired or taken for liquidity management purpose? Please explain and quantify these costs or other burdens in detail.

Question 41. Is the proposed liquidity management exclusion sufficiently clear? If not, why is the exclusion unclear and how should the Agencies clarify the terms of this exclusion?

Question 42. Is the proposed clarifying exclusion for certain positions taken by derivatives clearing organizations and clearing agencies effective and appropriate? If not, what alternative would be more effective and appropriate, and why?

Question 43. Are any additional clarifying exclusions warranted? If so, what clarifying exclusion, and why?

Question 44. Should the proposed definition exclude any position the market risk of which cannot be hedged by the banking entity in a two-way market? If so, what would be the basis for concluding that such positions are clearly not within the statutory definition of trading account?

Question 45. Should the proposed definition include a clarifying exclusion for any position in illiquid assets? If so, what would be the basis for concluding that such positions are clearly not within the statutory definition of trading account? How should "illiquid assets" be defined for these purposes? Should the definition be consistent with the definition given that term in the Board's Conformance Rule under section 13 of the BHC Act (12 CFR 225.180 et seq.)?

The Agencies request comment on the following questions with respect to the proposed rule's definition of "covered financial position":

Question 46. Is the proposed rule's definition of covered financial position effective? Is the definition over- or under-inclusive? What alternative approaches might be more effective in light of the language and purpose of section 13 of the BHC Act, and why?

Question 47. Are there definitions in other rules or regulations that might inform the proposed definition of covered financial position? If so, what rule or regulation? How should that approach be incorporated into the proposed definition? Why would that approach be more appropriate?

Question 48. Are there particular transactions or positions to which the application of the proposed definition of covered financial position is unclear? Is additional regulatory language, guidance, or clarity necessary?

Question 49. The proposal would apply to long, short, synthetic, or other positions in one of the listed categories of financial instruments. Does this language adequately describe the type of positions that are intended to fall within the proposed definition of covered financial position? If not, why not? Are there different or additional concepts that should be specified in this context? Please explain.

Question 50. Should the Agencies expand the scope of covered financial positions to include other transactions, such as spot commodities or foreign exchange or currency, or certain subsets of transaction (e.g., spot commodities or foreign exchange or currency traded on a high frequency basis)? If so, which instruments and why?

Question 51. What factors should the Agencies consider in deciding whether to extend the scope of the proprietary trading restriction to other financial instruments under the authority granted in section 13(h)(4) of the BHC Act? Please explain.

Question 52. Is the proposed exclusion of any position that is a loan, a commodity, or foreign exchange or currency effective? If not, what alternative approaches might be more effective in light of the language and purpose of section 13 of the BHC Act? Should additional positions be excluded? If so, why and under what authority?

The Agencies request comment on the following questions with respect to the proposed rule's definition of terms used in the definition of "covered financial position":

Question 53. Are the proposed rule's definitions of commodity and contract of sale of a commodity for future delivery appropriate? If not, what alternative definitions would be more appropriate?

Question 54. Is the proposed definition of derivative effective? If not, what alternative definition would be more effective? Should the proposed rule expressly incorporate the definition of "swap" and security-based swap" under the Federal commodities and securities laws? If not, what alternative approach should be taken? Are there transactions included in those incorporated definitions that should not be included in the proposed rule's definition? If so, what transactions and why? Are there transactions excluded from those incorporated definitions that should be included within the proposed rule's definition? If so, what transactions and why?

Question 55. Is the proposed inclusion of foreign exchange forwards and swaps in the definition of derivative effective? If not, why not? On what basis would the Agencies conclude that such transactions are not derivatives? Are these transactions economically or functionally more similar to secured loans or repurchase arrangements than to commodity forwards and swaps? Would there be any unintended consequences to banking entities if such transactions are included in the proposal's definition of derivative? What effect is including foreign exchange swaps and forwards in the definition of derivative likely to have on banking entities, participants in the foreign exchange markets, and the liquidity and efficiency of foreign exchange markets generally? If included within the definition of derivative, should transactions in foreign exchange swaps and forwards be permitted under section 13(d)(1)(J) of the BHC Act? If so, why and on what basis? Please quantify your responses, to the extent feasible.

Question 56. Is the proposed inclusion of any purchase or sale of a nonfinancial commodity for deferred shipment or delivery that is intended to be physically settled in the definition of derivative effective? If not, why not? Would there be any unintended consequences to banking entities if such transactions are included in the proposal's definition of derivative?

Question 57. Is the proposed inclusion of foreign currency transactions described in section 2(c)(2)(C)(i) of the Commodity Exchange Act in the definition of derivative effective? If not, why not? Would there be any unintended consequences to banking entities if such transactions are included in the proposal's definition of derivative?

Question 58. Is the proposed inclusion of commodity transactions described in section 2(c)(2)(D)(i) of the Commodity Exchange Act in the definition of derivative effective? If not, why not? Would there be any unintended consequences to banking entities if such transactions are included in the proposal's definition of derivative?

Question 59. Is the proposed inclusion of any transaction authorized under section 19 of the Commodity Exchange Act (7 U.S.C. 23(a) or (b)) in the definition of derivative effective? If not, why not? Would there be any unintended consequences to banking entities if such transactions are included in the proposal's definition of derivative?

Question 60. Is the manner in which the proposed definition of derivative excludes any transaction that the CFTC or SEC exclude by joint regulation, interpretation, guidance, or other action from the definition of "swap" or "security-based swap" effective? If not, what alternative approach would be more appropriate? Should such exclusions be restated in the proposed rule's definition? If so, why?

Question 61. Is the proposed rule's definition of loan appropriate? If not, what alternative definition would be more appropriate? Should the definition of "loan" exclude a security? Should other types of traditional banking products be included in the definition of "loan"? If so, why?

The Agencies request comment on the following questions related to certain other terms related to "proprietary trading" in the proposed rule:

Question 62. Are the proposed rule's definitions of other terms in § __.3(d) appropriate? If not, what alternative definitions would be more appropriate?

Question 63. Is the definition of additional terms for purposes of subpart B of the proposed rule necessary? If so, what terms should be defined? How should those terms be defined?

The Agencies request comment on the following questions with respect to the proposed rule's implementation of an "underwriting exemption":

Question 64. Is the proposed rule's implementation of the underwriting exemption effective? If not, what alternative approach would be more effective? For example, should the exemption include other transactions that do not involve a distribution of securities for which the banking entity is acting as underwriter?

Question 65. Are the seven requirements included in the underwriting exemption effective? Is the application of each requirement to potential transactions sufficiently clear? Should any of the requirements be changed or eliminated? Should other requirements be added in order to better provide an exemption that is not susceptible to abuse through the taking of speculative, proprietary positions in the context of, or mischaracterized as, underwriting? Alternatively, are any of the proposed requirements inappropriately restrictive in that they would be inconsistent with the statutory exemption for certain underwriting activities? If so, how?

Question 66. Do underwriters currently have processes in place that would prevent or reduce the likelihood of taking speculative, proprietary positions in the context of, or mischaracterized as, underwriting? If so, what are those processes?

Question 67. Would any of the proposed requirements cause unintended consequences? Would the proposed requirements alter current underwriting practices in any way? Would any of the proposed requirements trigger an unwillingness to engage in underwriting? What impact, if any, would the proposed exemption have on capital raising? Please explain.

Question 68. What increased costs, if any, would underwriters incur to satisfy the seven proposed requirements of the underwriting exemption? Would underwriters pass the increased costs onto issuers, selling security holders, or their customers in connection with qualifying for the proposed exemption?

Question 69. In addition to the specific activities highlighted above for purposes of evaluating whether a banking entity is acting as an underwriter as part of distribution of securities (e.g., assisting an issuer in capital raising, performing due diligence, etc), are there other or alternative activities that should be considered? Please explain.

Question 70. Should the requirement that a covered financial position be a security be expanded to include other financial instruments? If so, why? How are such other instruments underwritten within the meaning of section 13(d)(1)(B) of the BHC Act?

Question 71. Is the proposed definition of a "distribution" of securities appropriate, or over- or under-inclusive in this context? Is there any category of underwriting activity that would not be captured by the proposed definition? If so, what are the mechanics of that underwriting activity? Should it be permitted under the proposed rule, and, if so, why? Would an alternative definition better identify offerings intended to be covered by the proposed definition? If so, what alternative definition, and why?

Question 72. Is the proposed definition of "underwriter" appropriate, or over- or under-inclusive in this context? Would an alternative definition, such as the statutory definition of "underwriter" under the Securities Act, better identify persons intended to be covered by the proposed definition? If so, why?

Question 73. How accurately can a banking entity engaging in underwriting predict the near-term demands of clients, customers, and counterparties with respect to an offering? How can principal risk that is retained in connection with underwriting activities to support near-term client demand be distinguished from positions taken for speculative purposes?

Question 74. Is the requirement that the underwriting activities of a banking entity relying on the underwriting exemption be designed to generate revenues primarily from fees, commissions, underwriting spreads or similar income effective? If not, how should the requirement be changed? Does the requirement appropriately capture the type and nature of revenues typically generated by underwriting activities? Is any further clarification or additional guidance necessary?

Question 75. Is the requirement that the compensation arrangements of persons performing underwriting activities at a banking entity be designed not to reward proprietary risk taking effective? If not, how should the requirement be changed? Are there other types of compensation incentives that should be clearly referenced as consistent, or inconsistent, with permitted underwriting activity? Are there specific and identifiable characteristics of compensation arrangements that clearly incentivize prohibited proprietary trading?

Question 76. Are there other types of underwriting activities that should also be included within the scope of the underwriting exemption? If so, what additional activities and why? How would an exemption for such additional activities be consistent with the language and purpose of section 13 of the BHC Act? What criteria, requirements, or restrictions would be appropriate to include with respect to such additional activities to prevent misuse or evasion of the prohibition on proprietary trading?

Question 77. Does the proposed underwriting exemption appropriately accommodate private placements? If not, what changes are necessary to do so?

Question 78. The creation, offer and sale of certain structured securities such as trust preferred securities or tender option bonds, among others, may involve the purchase of another security and repackaging of that security through an intermediate entity. Should the sale of the security by a banking entity to an intermediate entity as part of the creation of the structured security be permitted under one of the exemptions to the prohibition on proprietary trading currently included in the proposed rule (e.g., underwriting or market making)? Why or why not? For purposes of determining whether an exemption is available under these circumstances, should gain on sale resulting from the sale of the purchased security to the intermediate entity as part of the creation of the structured security be considered a relevant factor? Why or why not? What other factors should be considered in connection with the creation of the structured securities and why? Would the analysis be different if the banking entity acquired and retained the security to be sold to the intermediate entity as part of the creation of the structured securities as part of its underwriting of the underlying security? Why or why not?

Question 79. We seek comment on the application of the proposed exemption to a banking entity retaining a portion of an underwriting. Please discuss whether or not firms frequently retain securities in connection with a distribution in which the firm is acting as underwriter. Please identify the types of offerings in which this may be done (e.g., fixed income offerings, securitized products, etc.). Please identify and discuss any circumstances which can contribute to the decision regarding whether or not to retain a portion of an offering. Please describe the treatment of retained securities (e.g., the time period of retention, the type of account in which securities are retained, the potential disposition of the securities). Please discuss whether or not the retention is documented and, if so, how. Should the Agencies require disclosure of securities retained in connection with underwritings? Should the Agencies require specific documentation to demonstrate that the retained portion is connected to an underwriting pursuant to the proposed rule? If so, what kind of documentation should be required? Please discuss how you believe retention should be addressed under the proposal.

The Agencies request comment on the following questions relating to the proposed rule's approach to implementing the exemption for permitted market making-related activities:

Question 80. Is the proposed rule's approach to implementing the exemption for permitted market making-related activities (i) appropriate and (ii) likely to be effective? If not, what alternative approach would be more appropriate or effective?

Question 81. Does the proposed multi-faceted approach appropriately take into account and address the challenges associated with differentiating prohibited proprietary trading from permitted market making-related activities? Should the approach include other elements? If so, what elements and why? Should any of the proposed elements be revised or eliminated? If so, why and how?

Question 82. Does the proposed multi-faceted approach provide banking entities and market participants with sufficient clarity regarding what constitutes permitted market making related activities? If not, how could greater clarity be provided?

Question 83. What impact will the proposed multi-faceted approach have on the market making-related services that a banking entity provides to its customers? How will the proposed approach impact market participants who use the services of market makers? How will the approach impact the

capital markets at large, and in particular the liquidity, efficiency and price transparency of capital markets? If any of these impacts are positive, how can they be amplified? If any of these impacts are negative, how can they be mitigated? Would the proposed rule's prohibition on proprietary trading and exemption for market making-related activity reduce incentives or opportunities for banking entities to trade against customers, as opposed to trading on behalf of customers? If so, please discuss the benefits arising from such reduced incentives or opportunities.

Question 84. What burden will the proposed multi-faceted approach have on banking entities, their customers, and other market participants? How can any burden be minimized or eliminated in a manner consistent with the language and purpose of the statute?

Question 85. Are there particular asset classes that raise special concerns in the context of market making-related activity that should be considered in connection with the proposed market-making exemption? If so, what asset class(es) and concern(s), and how should the concerns be addressed in the proposed exemption?

Question 86. Are there other market making-related activities that the rule text should more clearly permit? Why or why not?

The Agencies request comment on the following questions regarding proposed criteria that must be met in order to rely on the market-making exemption from proprietary trading:

Question 87. Are the seven criteria included in the market-making exemption effective? Is the application of each criterion to potential transactions sufficiently clear? Should any of the criteria be changed or eliminated? Should other criteria be added?

Question 88. Is incorporation of concepts from the definition of "market maker" under the Exchange Act useful for purposes of section 13 of the BHC Act and consistent with its purposes? If not, what alternative definition would be more useful or more consistent?

Question 89. Is the proposed exemption overly broad or narrow? For example, would it encompass activity that should be considered prohibited proprietary trading under the proposed rule? Alternatively, would it prohibit forms of market making or market making-related activities that are permitted under other rules or regulations?

Question 90. We seek commenter input on the types of banking entities and forms of activities that would not qualify for the proposed market-making exemption but that commenters consider to otherwise be market making. Please discuss the impact of not permitting such activities under the proposed exemption (e.g., the impact on liquidity).

Question 91. Is the requirement that a trading desk or other organizational unit relying on the market-making exemption hold itself out as being willing to buy and sell, or otherwise enter into long and short positions in, the relevant covered financial position for its own account on a regular or continuous basis effective? If not, what alternative would be more effective? Does the proposed requirement appropriately differentiate between market making-related activities in different markets and asset classes? If not, how could such differences be better reflected? Should the requirement be modified to include certain arbitrage trading activities engaged in by market makers that promote liquidity or price transparency, but do not serve customer, client or counterparty demands, within the scope of market making-related activity? If so why? How could such liquidity- or price transparency-promoting activities be meaningfully identified and distinguished from prohibited proprietary trading

practices that also may incidentally promote liquidity or price transparency? Do particular markets or instruments, such as the market for exchange-traded funds, raise particular issues that are not adequately or appropriately addressed in the proposal? If so, how could the proposal better address those instruments, markets or market features?

Question 92. Do the proposed indicia of market making in liquid markets accurately reflect the factors that should generally be used to analyze whether a banking entity is engaged in market making-related activities for purposes of section 13 of the BHC Act and the proposed rule? If not, why not? Should any of the proposed factors be eliminated or modified? Should any additional factors be included? Is reliance on the SEC's indicia of bona fide market making for purposes of Regulation SHO under the Exchange Act and the equity securities market appropriate in the context of section 13 of the BHC Act and the proposed rule with respect to liquid markets? If not, why not?

Question 93. Do the proposed indicia of market making in illiquid markets accurately reflect the factors that should generally be used to analyze whether a banking entity is engaged in market making-related activities for purposes of section 13 of the BHC Act and the proposed rule? If not, why not? Should any of the proposed factors be eliminated or modified? Should any additional factors be included?

Question 94. How accurately can a banking entity predict the near-term demands of clients, customers, and counterparties? Are there measures that can distinguish the amount of principal risk that should be retained to support such near-term client, customer, or counterparty demand from positions taken for speculative purposes? How is client, customer, or counterparty demand anticipated in connection with market making-related activities, and how does such approach vary by asset class?

Question 95. Is the requirement that a banking entity relying on the market-making exemption be registered as a dealer (or in the case of a financial institution that is a government securities dealer, has filed notice of that status as required by section 15C(a)(1)(B) of the Exchange Act), or exempt from registration or excluded from regulation as a dealer under relevant securities or commodities laws effective? If not, how should the requirement be changed? Does the requirement appropriately take into account the particular registration requirements applicable to dealing in different types of financial instruments? If not, how could it better do so? Does the requirement appropriately take into account the various registration exemptions and exclusions available to certain entities, such as banks, under the securities and commodities laws? If not, how could it better do so?

Question 96. Is the requirement that a trading desk or other organizational unit of a banking entity relying on the market-making exemption be designed to generate revenues primarily from fees, commissions, bid/ask spreads or similar income effective? If not, how should the requirement be changed? Does the requirement appropriately capture the type and nature of revenues typically generated by market making-related activities? Is any further clarification or additional guidance necessary? Can revenues primarily from fees, commissions, bid/ask spreads or similar income be meaningfully separated from other types of revenues?

Question 97. Is the requirement that the compensation arrangements of persons performing market making-related activities at a banking entity not be designed to encourage proprietary risk-taking effective? If not, how should the requirement be changed? Are there other types of compensation incentives that should be clearly referenced as consistent, or inconsistent, with permitted market making-related activity? Are their specific and identifiable characteristics of compensation arrangements that clearly incentivize prohibited proprietary trading?

Question 98. Is the inclusion of market making-related hedging transactions within the market-making exemption effective and appropriate? Are the proposed requirements that certain hedging transactions must meet in order to be considered to have been made in connection with market making-related activity effective and sufficiently clear? If not, what alternative requirements would be more effective and/or clearer? Should any of the proposed requirements be eliminated? If so, which ones, and why?

Question 99. Should the terms "client," "customer," or "counterparty" be defined for purposes of the market-making exemption? If so, how should these terms be defined? For example, would an appropriate definition of "customer" be: (i) a continuing relationship in which the banking entity provides one or more financial products or services prior to the time of the transaction; (ii) a direct and substantive relationship between the banking entity and a prospective customer prior to the transaction; (iii) a relationship initiated by the banking entity to a prospective customer to induce transactions; or (iv) a relationship initiated by the prospective customer with a view to engaging in transactions?

Question 100. Are there other types of market making-related activities that should also be included within the scope of the market-making exemption? If so, what additional activities and why? How would an exemption for such additional activities be consistent with the language and intent of section 13 of the BHC Act? What criteria, requirements, or restrictions would be appropriate to include with respect to such additional activities? How would such criteria, requirements, or restrictions prevent circumvention or evasion of the prohibition on proprietary trading?

Question 101. Do banking entities currently have processes in place that would prevent or reduce the likelihood of taking speculative, proprietary positions in the context of, or mischaracterized as, market making-related activities? If so, what processes?

The Agencies request comment on the following with respect to implementation of the risk-mitigating hedging exemption with respect to proprietary trading:

Question 102. Is the proposed rule's approach to implementing the hedging exemption effective? If not, what alternative approach would be more effective?

Question 103. Does the proposed multi-faceted approach appropriately take into account and address the challenges associated with differentiating prohibited proprietary trading from permitted hedging activities? Should the approach include other elements? If so, what elements and why? Should any of the proposed elements be revised or eliminated? If so, why and how?

Question 104. Does the proposed approach to implementing the hedging exemption provide banking entities and market participants with sufficient clarity regarding what constitutes permitted hedging activities? If not, how could greater clarity be provided?

Question 105. What impact will the proposed approach to implementing the hedging exemption have on the hedging and risk management activities of a banking entity and the services it provide to its clients? If any of these impacts are positive, how can they be amplified? If any of these impacts are negative, how can they be mitigated?

Question 106. What burden will the proposed approach to implementing the hedging exemption have on banking entities? How can any burden be minimized or eliminated in a manner consistent with the language and purpose of the statute?

Question 107. Are the criteria included in the hedging exemption effective? Is the application of each criterion to potential transactions sufficiently clear? Should any of the criteria be changed or eliminated? Should other requirements be added?

Question 108. Is the requirement that a transaction hedge or otherwise mitigate one or more specific risks, including market risk, counterparty or other credit risk, currency or foreign exchange risk, interest rate risk, basis risk, or similar risks, arising in connection with and related to individual or aggregated positions, contracts, or other holdings of a banking entity effective? If not, what requirement would be more effective? Does the proposed approach sufficiently articulate the types of risks that a banking entity typically hedges? Does the proposal sufficiently address application of the hedging exemption to portfolio hedging strategies? If not, how should the proposal be changed?

Question 109. Does the manner in which section __.5 of the proposal would implement the risk-mitigating hedging exemption effectively address transactions that hedge or otherwise mitigate specific risks arising in connection with and related to aggregated positions, contracts, or other holdings of a banking entity? Do certain hedging strategies or techniques that involve hedging the risks of aggregated positions (e.g., portfolio hedging) (i) create the potential for abuse of the hedging exemption or (ii) give rise to challenges in determining whether a banking entity is engaged in exempt, risk-mitigating hedging activity or prohibited proprietary trading? If so, what hedging strategies and techniques, and how? Should additional restrictions, conditions, or requirements be placed on the use of the hedging exemption with respect to aggregated positions so as to limit potential abuse of the exemption, assist banking entities and the Agencies in determining compliance with the exemption, or otherwise improve the effectiveness of the rule? If so, what additional restrictions, conditions, or requirements, and why?

Question 110. Is the requirement that the transaction be reasonably correlated to the risk or risks the transaction is intended to hedge or otherwise mitigate effective? If not, how should the requirement be changed? Should some specific level of correlation and/or hedge effectiveness be required? Should the proposal specify in greater detail how correlation should be measured? Should the proposal require hedges to be effective in periods of financial stress? Does the proposal sufficiently reflect differences in levels of correlation among asset classes? If not, how could it better do so?

Question 111. Is the requirement that the transaction not give rise, at the inception of the hedge, to significant exposures that are not themselves hedged in a contemporaneous transaction effective? Does the requirement establish an appropriate range for legitimate hedging while constraining impermissible proprietary trading? Is this requirement sufficiently clear? If not, what alternative would be more effective and/or clearer? Are there types of risk-mitigating hedging activities that may give rise to new and significant exposures that should be permitted under the hedging exemption? If so, what activities? Should the requirement that no significant exposure be introduced be extended for the duration of the hedging position? If so, why?

Question 112. Is the requirement that any transaction conducted in reliance on the hedging exemption be subject to continuing review, monitoring and management after the transaction is established effective? If not, what alternative would be more effective?

Question 113. Is the requirement that the compensation arrangements of persons performing risk-mitigating hedging activities at a banking entity be designed not to reward proprietary risk-taking effective? If not, how should the requirement be changed? Are there other types of compensation incentives that should be clearly referenced as consistent, or inconsistent, with permitted risk-

mitigating hedging activity? Are there specific and identifiable characteristics of compensation arrangements that clearly incentivize prohibited proprietary trading?

Question 114. Is the proposed documentation requirement effective? If not, what alternative would be more effective? Are there certain additional types of hedging transactions that should be subject to the documentation requirement? If so, what transactions and why? Should all types of hedging transactions be subject to the documentation requirement? If so, why? Should banking entities be required to document more aspects of a particular transactions (e.g., all of the criteria applicable to § __.5(b) of the proposed rule)? If so, what aspects and why? What burden would the proposed documentation requirement place on banking entities? How might such burden be reduced or eliminated in a manner consistent with the language and purpose of the statute?

Question 115. Aside from the required documentation, do the substantive requirements of the proposed risk-mitigating hedging exemption suggest that additional documentation would be required to achieve compliance with the proposed rule? If so, what burden would this additional documentation requirement place on banking entities? How might such burden be reduced or eliminated in a manner consistent with the language and purpose of the statute?

The Agencies request comment on the proposal's approach to implementing the statutory exemptions to the proprietary trading provisions set forth in section 13(d)(1) of the BHC Act:

Question 116. Is the proposed rule's approach of identifying which of the statutory exemptions contained in section 13(d)(1) of the BHC Act apply to the proposed rule's proprietary trading provisions effective and/or consistent the language and purpose of the statute? If not, what alternative would be more effective and/or consistent with the language and purpose of the statute?

Question 117. Are there statutory exemptions that should apply to the proposed rule's proprietary trading provisions that were not included? If so, what exemptions and why?

Question 118. Are there statutory exemptions that were included in the proposed rule's proprietary trading provisions that should not have been included? If so, what exemptions and why?

Regarding the proposed rule's approach to implementing the government obligation exemption, the Agencies request comment on the following:

Question 119. Is the proposed rule's application to trading in government obligations sufficiently clear? Should such obligations expressly include, for example, instruments issued by third parties but insured or guaranteed by an enumerated government entity or otherwise backed by its full faith and credit?

Question 120. Should the Agencies adopt an additional exemption for proprietary trading in State or municipal agency obligations under section 13(d)(1)(J) of the BHC Act? If so, how would such an exemption promote and protect the safety and soundness of banking entities and the financial stability of the United States?

Question 121. Should the Agencies adopt an additional exemption for proprietary trading in options or other derivatives referencing an enumerated government obligation under section 13(d)(1)(J) of the BHC Act? For example, should the Agencies provide an exemption for options or other derivatives with respect to U.S. government debt obligations? If so, how would such an exemption promote and protect the safety and soundness of banking entities and the financial stability of the United States?

Question 122. Should the Agencies adopt an additional exemption for proprietary trading in the obligations of foreign governments and/or international and multinational development banks under section 13(d)(1)(J) of the BHC Act? If so, what types of obligations should be exempt? How would such an exemption promote and protect the safety and soundness of banking entities and the financial stability of the United States?

Question 123. Should the Agencies adopt an additional exemption for proprietary trading in any other type of government obligations under section 13(d)(1)(J) of the BHC Act? If so, how would such an exemption promote and protect the safety and soundness of banking entities and the financial stability of the United States?

Question 124. Are the definitions of "government security" and "municipal security" in sections 3(a)(42) and 3(a)(29) of the Exchange Act helpful in determining the proper scope of this exemption? If so, please explain their utility and how incorporating such definitions into the exemption would be consistent with the language and purpose of section 13 of the BHC Act.

The Agencies request comment on the following with respect to the proposed rule's approach to implementing the exemption for trading on behalf of customers:

Question 125. Is the proposed rule's articulation of three categories of transactions on behalf of customers effective and sufficiently clear? If not, what alternative would be more effective and/or clearer? Should any of the categories be eliminated? Should any additional categories be added? Please explain.

Question 126. Is the proposed rule's exemption of certain investment adviser, commodity trading advisor, trustee or similar fiduciary transactions effective? What other types of relationships are or should be captured by the proposed rule's reference to "similar fiduciary relationships," and why? Is application of this part of the exemption to particular transactions sufficiently clear? Should any other specific types of fiduciary or other relationships be specified in the rule? If so, what types and why? What impact will the proposed rule's implementation of the exemption have on the investment adviser, commodity trading advisor, trustee or similar fiduciary activities of banking entities? If such impacts are negative, how could they be mitigated or eliminated in a manner consistent with the purpose and language of the statute?

Question 127. Is the proposed rule's exemption of riskless principal transactions effective? If not, what alternative would be more appropriate? Is the description of qualifying riskless principal activity sufficiently clear? If not, how should it be clarified? Should the riskless principal transaction exemption include a requirement that the banking entity must purchase (or sell) the covered financial position as principal at the same price to satisfy the customer buy (or sell) order, exclusive of any explicitly disclosed markup or markdown, commission equivalent, or other fee? Why or why not? Should the riskless principal exemption include a requirement with respect to the timeframe in which the principal transaction must be allocated to a riskless principal or customer account? Why or why not?

Question 128. Is the proposed rule's exemption of trading for separate accounts by insurance companies effective? If not, what alternative would be more appropriate? Does the proposed exemption sufficiently address the variety of customer-driven separate account structures typically used? If not, how should it address such structures? Does the proposed exemption sufficiently address the variety of regulatory or supervisory regimes to which insurance companies may be subject?

Question 129. What impact will the proposed rule's implementation of the exemption have on the insurance activities of insurance companies affiliated with banking entities? If such impacts are negative, how could they be mitigated or eliminated in a manner consistent with the purpose and language of the statute?

Question 130. Should the term "customer" be defined for purposes of the exemption for transactions on behalf of customers? If so, how should it be defined? For example, would an appropriate definition be (i) a continuing relationship in which the banking entity provides one or more financial products or services prior to the time of the transaction, (ii) a direct and substantive relationship between the banking entity and a prospective customer prior to the transaction, or (iii) a relationship initiated by the banking entity to a prospective customer for purposes of the transaction?

Question 131. Is the exemption for trading on behalf of customers in the proposed rule over- or under-inclusive? If it is under-inclusive, please discuss any additional activities that should qualify as trading on behalf of customers under the rule. What are the mechanics of the particular trading activity and how does it qualify as being on behalf of customers? Are there certain requirements or restrictions that should be placed on the activity, if permitted by the rule, to prevent evasion of the prohibition on proprietary trading? How would permitting the activity be consistent with the purpose and language of section 13 of the BHC Act? If the proposed exemption is over-inclusive, please explain what aspect of the proposed exemption does not involve trading on behalf of customers within the language and purpose of the statute.

The Agencies request comment on the following regarding the proposal's approach to implementing the exemption for general account trading by insurance companies:

Question 132. Should any of the statutory requirements for the exemption be further clarified in the proposed rule? If so, how? Should any additional requirements be added? If so, what requirements and why?

Question 133. Does the proposed rule appropriately and clearly define a general account for these purposes? If not, what alternative definition would be more appropriate?

Question 134. For purposes of the exemption, are the insurance company investment laws, regulations, and written guidance of any particular State or jurisdiction insufficient to protect the safety and soundness of the banking entity, or of the financial stability of the United States? If so, why?

Question 135. What impact will the proposed rule's implementation of the exemption have on the insurance activities of insurance companies affiliated with banking entities? If such impacts are negative, how could they be mitigated or eliminated in a manner consistent with the purpose and language of the statute?

Regarding the proposed rule's approach to implementing the foreign trading exemption, the Agencies request comment on the following:

Question 136. Is the proposed rule's implementation of the foreign trading exemption effectively delineated? If not, what alternative would be more effective and/or clearer?

Question 137. Are the proposed rule's provisions regarding when an activity will be considered to have been conducted pursuant to section 4(c)(9) of the BHC Act effective and sufficiently clear? If not, what

alternative would be more effective and/or clearer? Do those provisions effectively address the application of the foreign trading exemption to foreign banking entities not subject to the BHC Act generally? If not, how should the proposed rule apply the exemption?

Question 138. Are the proposed rule's provisions regarding when an activity will be considered to have occurred solely outside the United States effective and sufficiently clear? If not, what alternative would be more effective and/or clearer? Should any requirements be modified or removed? If so, which requirements and why? Should additional requirements be added? If so, what requirements and why?

Question 139. Is the proposed rule's definition of "resident of the United States" effective and sufficiently clear? If not, what alternative would be more effective and/or clearer? Is the definition over- or under-inclusive? If so, why? Should the definition more closely track, or incorporate by reference, the definition of "U.S. person" under the SEC's Regulation S under the Securities Act? If so, why?

Question 140. Does the proposed rule effectively define a resident of the United States for these purposes? If not, how should the definition be altered?

Question 141. Should the Agencies use the authority provided in section 13(d)(1)(J) of the BHC Act to allow U.S.-controlled banking entities to engage in proprietary trading pursuant to section 4(c)(13) of the BHC Act outside of the United States under certain circumstances? If so, under what circumstances should this be permitted and how would such activity promote and protect the safety and soundness of banking entities and the financial stability of the United States?

Regarding the Agencies' authority to grant discretionary exemptions from the prohibition on proprietary trading, the Agencies request comment on the following:

Question 142. Should the Agencies adopt any exemption from the prohibition on proprietary trading under section 13(d)(1)(J) of the BHC Act? If so, what exemption and why? How would such an exemption promote and protect the safety and soundness of banking entities and the financial stability of the United States?

The Agencies request comment on the following questions regarding the proposed approach to implementing reporting requirements for proprietary trading:

Question 143. Is the use of the proposed reporting requirements as part of the multifaceted approach to implementing the prohibition on proprietary trading appropriate? Why or why not?

Question 144. Is the proposed gradual approach to implementing reporting requirements effective? If not, what approach would be more effective? For example, should the Agencies defer reporting of quantitative measurements until banking entities have developed and refined their compliance programs through the supervision and examination process? What would be the costs and benefits of such an approach?

Question 145. What role, if any, could or should the Office of Financial Research ("OFR") play in receiving and analyzing banking entities' reported quantitative measurements? Should reporting to the OFR be required instead of reporting to the relevant Agency, and would such reporting be consistent with the composition and purpose of OFR? In the alternative, should reporting to either (i) only the relevant Agency (or Agencies) or (ii) both the relevant Agency (or Agencies) and OFR be required? If

so, why? What are the potential costs and benefits of reporting quantitative measurements to the OFR? Please explain.

Question 146. Is there an alternative manner in which the Agencies should develop and propose the reporting requirements for quantitative measurements? If so, how should they do so?

Question 147. Does the proposed approach provide sufficient time for the development and implementation of effective reporting requirements? If not, what alternative approach would be preferable?

Question 148. Should a trading unit be permitted not to furnish a quantitative measurement otherwise required under Appendix A if it can demonstrate that the measurement is not, as applied to that unit, calculable or useful in achieving the purposes of the Appendix with respect to the trading unit's covered trading activities? How might a banking entity make such a demonstration?

Question 149. Is the manner in which the Agencies propose to utilize the conformance period for review of collected data and refinement of the reporting requirements effective? If not, what process would be more effective?

Question 150. Is the proposed $1 billion trading asset and liability threshold, which is also currently used in the Market Risk Capital Rules for purposes of identifying which banks and bank holdings companies must comply with those rules, an appropriate standard for triggering the reporting and recordkeeping requirements of the proposed rule? Why or why not? If not, what alternative standard would be a better benchmark for triggering the reporting and recordkeeping requirements?

Question 151. What are the typical trading activities (e.g., market making-related activities) of a banking entity with less than $1 billion in gross trading assets and liabilities? How complex are those trading activities?

Question 152. Should the proposed $1 billion trading and asset liability threshold used for triggering the reporting and recordkeeping requirements adjust each time the thresholds for complying with the Market Risk Capital Rules adjust, or otherwise be adjusted over time? If not, how and when should the numerical threshold be adjusted?

Question 153. Should all banking entities be required to comply with the reporting and recordkeeping requirements set forth in Appendix A in order to better protect against prohibited proprietary trading, rather than only those banking entities that meet the proposed $1 billion trading asset and liability threshold? Why or why not?

Question 154. Should banking entities that fall under the proposed $1 billion trading asset and liability threshold be required to comply with the reporting and recordkeeping provisions for a pilot period in order to help inform judgment regarding the levels of quantitative measurements at such entities and the appropriate frequency and scope of examination by the relevant Agency for such banking entities? Why or why not?

The Agencies request comment on the following with respect to the proposed reporting requirements under the rule:

Question 155. Are the ways in which the proposed rule would make use of reported quantitative measurements effective? If not, what uses would be more effective? Should the proposed rule instead

use quantitative measurements as a dispositive tool for identifying prohibited proprietary trading? If so, what types of quantitative measurements should be employed, what numerical amount would indicate impermissible proprietary trading activity, and why? Should the quantitative measurements play a less prominent role than proposed in identifying prohibited proprietary trading and why?

Question 156. Are the proposed definitions of terms provided in Appendix A effective? If not, how should the definitions be amended?

Question 157. Is the proposed definition of "trading unit" effective? Is it sufficiently clear? If not, what alternative definition would be more effective and/or clearer? Should the definition include more or less granular levels of activity? If so, what specific criteria should be used to determine the appropriate level of granularity?

Question 158. If you are a banking entity, how would your trading activity be categorized, in terms of quantity and type, under the proposed definition of trading unit in Appendix A? For each trading unit type, what categories of quantitative measurements (e.g., risk-management measurements) or specific quantitative measurements (e.g., Stressed Value-at- Risk ("Stress VaR")) are best suited to assist in distinguishing prohibited proprietary trading from permitted trading activity?

Question 159. Is the proposed rule's requirement that quantitative measurements be reported at multiple levels of organization, including for quantitative measurements historically reported on an aggregate basis (e.g., Value-at-Risk ("VaR") or Stress VaR) appropriate? If not, what alternative would be more effective? What burdens are associated with such a requirement? How might those burdens be reduced or limited? Please quantify your answers, to the extent feasible.

Regarding the frequency of required calculations and reporting of quantitative measurements, and associated recordkeeping requirements for verifying required quantitative measurements for each trading day, the Agencies request comment on the following:.

Question 160. Is the proposed tiered approach to identifying which banking entities and trading units must comply with the reporting requirements effective? If not, what alternative would be more effective? Does the proposal strike the appropriate balance between the potential benefits of the reporting requirements for monitoring and assuring compliance and the potential costs of those reporting requirements? If not, how could that balance be improved? Should the relevant gross trading assets and liabilities threshold for any category be increased or reduced? If so, why?

Question 161. Should the $1 billion and $5 billion gross trading assets and liabilities thresholds used to identify the extent to which a banking entity is required to furnish quantitative measurements be increased or reduced? If so, why? Should the thresholds be indexed in some way to account for fluctuations in capital markets activity over time? If so, what would be an appropriate method of indexation?

Question 162. Is the proposed $5 billion trading asset and liability threshold an appropriate standard for triggering enhanced reporting requirements under the proposed rule? Why or why not? If not, what alternative standard would be a better benchmark for triggering enhanced reporting requirements?

Question 163. Should the proposed $5 billion trading and asset liability threshold used for triggering enhanced reporting requirements under the proposed rule be subject to adjustment over time? If so, how and when should the numerical threshold be adjusted?

Question 164. Is there a different criterion other than gross trading assets and liabilities that would be more appropriate for identifying banking entities that must furnish quantitative measurements? If so, what is the alternative criterion, and why would it be more appropriate? Are worldwide gross trading assets and liabilities the appropriate criterion for foreign-based banking entities? If not, what alternative criterion would be more appropriate, and why?

Question 165. Are the quantitative measurements specified for the various types of banking entities and trading units effective? If not, what alternative set of measurements would be more effective? For each type of trading unit, does the proposal strike the appropriate balance between the potential benefits of the reporting requirements for monitoring and assuring compliance and the potential costs of those reporting requirements? If not, how could that balance be improved?

Question 166. Should banking entities with gross trading assets and liabilities between $1 billion and $5 billion also be required to calculate and report some of the quantitative measurements proposed for banking entities meeting the $5 billion threshold for purposes of assessing whether the banking entity's underwriting, market making, risk-mitigating hedging, and trading in certain government obligations activities involve a material exposure to high-risk assets or high-risk trading strategies? If so, which quantitative measurements and why? If not, why not?

Question 167. Is the proposed frequency of reporting effective? If not, what frequency would be more effective? Should the quantitative measurements be required to be reported quarterly, annually, or upon the request of the applicable Agency and why?

The Agencies request comment on the proposed quantitative measurements, and particularly request comment on the following:

Question 168. Are the proposed quantitative measurements appropriate in general? If not, what alternative(s) would be more appropriate, and why? Should certain quantitative measurements be eliminated, and if so, why? Should additional quantitative measurements be added? If so, which measurements and why? How would those additional measurements be described and calculated?

Question 169. How many of the proposed quantitative measurements do banking entities currently utilize? What are the current benefits and costs associated with calculating such quantitative measurements? Would the reporting and recordkeeping requirements proposed in Appendix A for such quantitative measurements impose any significant, additional benefits or costs?

Question 170. Which of the proposed quantitative measurements do banking entities currently not utilize? What are the potential benefits and costs to calculating these quantitative measurements and complying with the proposed reporting and recordkeeping requirements? Please quantify your answers, to the extent feasible.

Question 171. Is the scope and frequency of required reporting appropriate? If not, what alternatives would be more appropriate? What burdens would be associated with reporting quantitative measurements on that basis, and how could those burdens be reduced or eliminated in a manner consistent with the purpose and language of the statute? Please quantify your answers, to the extent feasible.

Question 172. For each of the categories of quantitative measurements (e.g., quantitative measurements relating to risk management), what factors should be considered in order to further refine the proposed category of quantitative measurements to better distinguish prohibited proprietary trading from permitted trading activity? For example, should the timing of a calculation be considered significant in certain contexts (e.g., should specific quantitative measurements be calculated during the middle of a trading day instead of the end of the day)? Please quantify your answers, to the extent feasible.

Question 173. In light of the size, scope, complexity, and risk of covered trading activities, do commenters anticipate the need to hire new staff with particular expertise in order to calculate the required quantitative measurements (e.g., collect data and make computations)? Do commenters anticipate the need to develop additional infrastructure to obtain and retain data necessary to compute the proposed quantitative measurements? Please explain and quantify your answers, to the extent feasible.

Question 174. For each individual quantitative measurement that is proposed:

- Is the use of the quantitative measurement to help distinguish between permitted and prohibited trading activities effective? If not, what alternative would be more effective? Does the quantitative measurement provide any additional information of value relative to other quantitative measurements proposed?

- Is the use of the quantitative measurement to help determine whether an otherwise-permitted trading activity is consistent with the requirement that such activity must not result, directly or indirectly, in a material exposure by the banking entity to high-risk assets and high-risk trading strategies effective? If not, what alternative would be more effective?

- What factors should be considered in order to further refine the proposed quantitative measurement to better distinguish prohibited proprietary trading from permitted trading activity? For example, should the timing of a calculation be considered significant in certain contexts (e.g., should specific quantitative measurements be calculated during the middle of a trading day instead of at the end of the day)?

- If the quantitative measurement is proposed to be applied to a trading unit that is engaged in activity pursuant to §§ __.4(a), __.5, or __.6(a) of the proposed rule, is the quantitative measurement calculable in relation to such activity? Is the quantitative measurement useful for determining whether underwriting, risk-mitigating hedging, or trading in certain government obligations is resulting, directly or indirectly, in a material exposure by the banking entity to high-risk assets or high-risk trading strategies?

- Is the description of the quantitative measurement sufficiently clear? What alternative would be more appropriate or clearer? Is the description of the quantitative measurement appropriate, or is it overly broad or narrow? If it is overly broad, what additional clarification is needed? Should the Agencies provide this additional clarification in the appendix's description of the quantitative measurement? If the description is overly narrow, how should it be modified to appropriately describe the quantitative measurement, and why?

- Is the general calculation guidance effective and sufficiently clear? If not, what alternative would be more effective or clearer? Is more or less specific calculation guidance necessary? If

so, what level of specificity is needed to calculate the quantitative measurement? What are the different calculation options and methodologies that could be used to reach the desired level of specificity? What are the costs and benefits of these different options? If the proposed calculation guidance is not sufficiently specific, how should the calculation guidance be modified to reach the appropriate level of specificity? For example, rather than provide this level of specificity in proposed Appendix A, should the Agencies instead make each banking entity responsible for determining the best method of calculating the quantitative measurement at this level of specificity, based on the banking entity's business and profile, which would then be subject to supervision, review, or examination by the relevant Agency? If the proposed calculation guidance is overly specific, why is it too specific and how should the guidance be modified to reach the appropriate level of specificity?

- Is the general calculation guidance for the measurement consistent with how banking entities currently calculate the quantitative measurement, if they do so? If not, how does the proposed guidance differ from methodology currently used by banking entities? What is the purpose of the current calculation methodology used by banking entities?

- What operational or logistical challenges might be associated with performing the calculation of the quantitative measurement and obtaining any necessary informational inputs?

- Is the quantitative measurement not calculable for any specific type of trading unit? If so, what type of trading unit, and why is the quantitative measurement not calculable for that type of trading unit? Is there an alternative quantitative measurement that would reflect the same trading activity but not pose the same calculation difficulty? Are there particular challenges to documenting that a specific quantitative measurement is not calculable?

- Is the quantitative measurement substantially likely to frequently produce false negatives or false positives that suggest that prohibited proprietary trading is occurring when it is not, or vice versa? If so, why? If so, what alternative quantitative measurement would better help identify prohibited proprietary trading?

- Should the quantitative measurement better account for distinctions among trading activities, trading strategies, and asset classes? If so, how? For example, should the quantitative measurements better account for distinctions between trading activities in cash and derivatives markets? If so, how? Are there any other distinctions for which the quantitative measurements may need to account? If so, what distinctions, and why?

- Does the quantitative measurement provide useful information as applied to all types of trading activities, or only a certain subset of trading activities? If it only provides useful information for a subset of trading activities, how should this issue be addressed? How beneficial is the information that the quantitative measurement provides for this subset of trading activities? Do any of the other quantitative measurements provide the same level of beneficial information for this subset of trading activities? Should the quantitative measurement be required to be reported for all trading activities, only a relevant subset of trading activities, or not at all?

- Does the quantitative measurement provide useful information as applied to all asset classes, or only a certain subset of asset classes? If it only provides useful information for a subset of asset classes, how should this issue be addressed? How beneficial is the information the

quantitative measurement provides for this subset of asset classes? Do any of the other quantitative measurements provide the same level of beneficial information for this subset of asset classes? Should the quantitative measurement be required to be reported for all asset classes, only a relevant subset of asset classes, or not at all?

- Is the calculation period effective and sufficiently clear? If not, what alternative would be more effective or clearer?

- How burdensome and costly would it be to calculate the measurement at the specified calculation frequency and calculation period? Are there any difficulties or costs associated with calculating the measurement for particular trading units? How significant are those potential costs relative to the potential benefits of the measurement in monitoring for impermissible proprietary trading? Are there potential modifications that could be made to the measurement that would reduce the burden or cost? If so, what are those modifications? Please quantify your answers, to the extent feasible.

Question 175. In light of the size, scope, complexity, and risk of covered trading activities, are there certain types of quantitative measurements that will not be appropriate for some types of banking entities, desks, or levels? If so, would it be appropriate to require only certain quantitative measurements for such banking entities, desks, or levels?

Question 176. How might the number of quantitative measurements impact behavior of banking entities? Is there a cost of requiring more quantitative measurements, such as the cost of increased uncertainty regarding the combined results of such quantitative measurements? To what extent and in what ways might uncertainty as to how the quantitative measurements are applied and evaluated impact behavior?

In connection with the proposed commentary regarding identification of permitted market making-related activities, the Agencies request comment on the following:

Question 177. Is the overview of permitted market making-related activities and prohibited proprietary trading proposed in Appendix B accurate? If not, what alternative overview would be more accurate? Does the overview appropriately account for differences in market making-related activities across different asset classes? If not, which type of market making-related activity does the overview not sufficiently describe or account for?

Question 178. Is the requirement that a market maker engaged in market making that is executed on an exchange or an organized trading facility must be a registered market maker, provided the relevant exchange or organized trading facility provides the ability to register, appropriate, or is it over- or under-inclusive? Please discuss and provide detailed examples of any such markets where registering as a market maker is not feasible or should not be required for purposes of this rule, and unregistered market makers provide similar services or perform similar functions.

Question 179. With respect to market making that is executed on an exchange or an organized trading facility, what potential impact or unintended consequences might result from limiting the market making exemption to registered market makers when the relevant exchange or organized trading facility registers market makers? Would such a requirement result in any potential decrease in the passive provision of liquidity by the submission of resting orders? Do you anticipate that any such decrease would be exacerbated in times of market stress? If yes, please describe the impact on

liquidity and the marketplace in general. Please discuss whether and how any potential decrease in liquidity could be mitigated. In addition, would such a requirement result in additional costs that would be borne by market participants purchasing and selling on an exchange or organized trading facility? Please identify and discuss any other additional costs. Please discuss whether and how any such consequences can be mitigated.

Question 180. In addition to benefits discussed in the Supplementary Information, are there other benefits that would be achieved by requiring that a market maker be registered with respect to market making on an exchange or an organized trading facility? Is there a way to amplify these benefits? Could these benefits be realized through alternative means? If so, how?

Question 181. In addition to registered market makers on exchanges or organized trading facilities, what other classes of liquidity providers exist? Are their obligations and activities similar to, or different than those of registered market makers? If so, how? Are the compensated in a different manner?

Question 182. How much liquidity is provided by registered market makers versus other liquidity providers by asset class (e.g., equities, etc.) with respect to trading on an exchange or an organized trading facility? The Agencies encourage commenters to provide data in support of comments.

Question 183. Is there any specific element of market making-related activity that the overview does not take into account in its description of market making? If so, how should the overview account for this element? Are there any descriptions of market making-related activity in the overview that should not be considered to be market making-related activity? If so, why? Is there any specific element of prohibited proprietary trading activity that the overview does not take into account in its description of prohibited proprietary trading? If so, how should the overview account for this element? Are there any descriptions of prohibited proprietary trading activity in the overview that should not be considered to be prohibited proprietary trading? If so, why?

Question 184. Are each of the six factors specified for helping to distinguish permitted market making-related activity from prohibited proprietary trading appropriate? If not, how should they be changed, and why? Should any factors be eliminated or added? If so, which ones and why? Could any of the proposed factors occur as a result of the banking entity engaging in one of the other permitted activities (e.g., underwriting, trading on behalf of customers)? If so, would the facts and circumstances that the Agencies propose to consider be sufficient to determine and verify that the banking entity is not engaged in prohibited proprietary trading? If not, how should this issue be addressed?

Question 185. Are the facts and circumstances that would be used to determine whether a banking entity's activities satisfy a certain factor appropriate? If not, how should they be changed, and why? Should any be eliminated or added? If so, which ones, and why?

Question 186. Are the identified quantitative measurements that the Agencies would use to help assess a particular factor appropriate? If not, how should they be changed, and why? Should any be eliminated or added? If so, which ones, and why?

The Agencies are requesting comment on the following questions regarding whether numeric thresholds for trading activities are desirable under the rule and, if so, what form such thresholds should take and what specific numerical thresholds are appropriate:

Question 187. What are the potential benefits and costs of incorporating into the proposed rule one or more numerical thresholds for certain quantitative measurements that, if reported by a banking entity, would require the banking entity to review its trading activities for compliance and summarize that review to the relevant Agency? Would such thresholds provide useful clarity to banking entities and/or market participants regarding the types of trading activities that merit additional scrutiny? Should numerical thresholds be used for any purposes other than highlighting trading activities that should be reviewed, the results of which would be reported to the relevant Agency? If so, for what purpose, and how and why?

Question 188. For which of the relevant quantitative measurements might it be appropriate and effective to include a numerical threshold that would trigger banking entity review and explanation? How should a numerical threshold be formulated, and why? Should a numerical threshold for a single quantitative measurement be applied individually, or should the threshold instead be triggered by exceeding some combination of numerical thresholds for different measurements? For any particular threshold, what numerical amount should be used, and why? How would such numerical amount be consistent with a level at which further review and explanation is warranted? Should the amount vary by asset class or other characteristic? If so, how?

Question 189. For each of the following illustrative examples of potential thresholds, is the threshold formulated effectively? If not, what alternative formulation would be more effective? Should the threshold formulation vary by asset class or other characteristic? If so, how and why? If the threshold was utilized, what actual numerical amount should be specified, and why? How would such numerical amount be consistent with a level at which further review and explanation is warranted? Should the numerical amount vary by asset class or other characteristic? If so, how and why?

- "If a trading unit reports an increase in VaR, Stress VaR, or Risk Factor Sensitivities greater than [__] over a period of [__] months, or such other threshold as [Agency] may require, the banking entity must (i) promptly review and investigate the trading unit's activities to verify whether the trading unit is operating in compliance with the proprietary trading restrictions and (ii) report to [Agency] a summary of such review, including any explanatory circumstances."

- "If a trading unit reports an average Comprehensive Profit and Loss that is less than [__] times greater than the Portfolio Profit and Loss, exclusive of Spread Profit and Loss, for [__] consecutive months, or such other threshold as [Agency] may require, the banking entity must (i) promptly review and investigate the trading unit's activities to verify whether the trading unit is operating in compliance with the proprietary trading restrictions and (ii) report to [Agency] a summary of such review, including any explanatory circumstances."

- "If a trading unit reports a Comprehensive Profit and Loss to Volatility Ratio that is less than [__] times greater than that trading desk's Portfolio Profit and Loss to Volatility Ratio over a period of [__] months, or such other threshold as [Agency] may require, the banking entity must (i) promptly review and investigate the trading unit's activities to verify whether the trading unit is operating in compliance with the proprietary trading restrictions and (ii) report to [Agency] a summary of such review, including any explanatory circumstances."

- "If a trading unit reports a number of Unprofitable Trading Days Based on Portfolio Profit and Loss that is less than [__] greater than the number of Unprofitable Trading Days Based on Comprehensive Profit and Loss for [__] consecutive months, or such other threshold as

[Agency] may require, the banking entity must (i) promptly review and investigate the trading unit's activities to verify whether the trading unit is operating in compliance with the proprietary trading restrictions and (ii) report to [Agency] a summary of such review, including any explanatory circumstances."

- "If a trading unit reports a Pay-to-Receive Spread Ratio that is less than **[__]** over a period of **[__]** months, or such other threshold as [Agency] may require, the banking entity must (i) promptly review and investigate the trading unit's activities to verify whether the trading unit is operating in compliance with the proprietary trading restrictions and (ii) report to [Agency] a summary of such review, including any explanatory circumstances."

The Agencies request comment on the following with respect to proposed limitations on permitted trading activities:

Question 190. Is the manner in which the proposed rule implements the limitations of section 13(d)(2) of the BHC Act effective and sufficiently clear? If not, what alternative would be more effective and/or clearer?

Question 191. Is the proposed rule's definition of material conflict of interest effective and sufficiently clear? If not, what alternative would be more effective and/or clearer?

Question 192. Is the proposed definition of material conflict of interest over-or underinclusive? If so, how should the definition be broader or narrower? Is there an alternative definition that would be appropriate? If so, what definition? Why would that alternative definition better define material conflict of interest for purposes of implementing section 13 of the BHC Act?

Question 193. Would the proposed definition of material conflict of interest have any unintended chilling effect on underwriting, market making, risk-mitigating hedging or other permitted activities? If so, what alternatives might limit such an effect?

Question 194. Would the proposed definition of material conflict of interest lead to unintended consequences? If so, what unintended consequences and why? Please suggest modifications to the proposed definition that would mitigate those consequences.

Question 195. Is it likely that the proposed definition of material conflict of interest would anticipate all future material conflicts of interest, particularly as the financial markets evolve and change? If not, what alternative definition would better anticipate future material conflicts of interest?

Question 196. Does the proposed rule provide sufficient guidance for determining when a material conflict of interest exists? If not, what additional detail should be provided? Should the Agencies adopt an approach similar to that under the securities laws, in which a material conflict of interest is not specifically defined?

Question 197. Are there transactions, classes or types of transactions, or activities inherent in underwriting, market-making, risk-mitigating hedging or other permitted activities that should not be prohibited but may be captured by the proposed definition of material conflict of interest? If so, what transactions and activities? Should they be permitted under the proposed rule? If so, why and under what conditions, if any? Conversely, are there transactions or activities that would be permitted under

the proposed rule that should be prohibited? If so, what transactions and activities? Why should they be prohibited under the proposed rule?

Question 198. Please discuss the inherent conflicts of interest that arise from bona fide underwriting, market making-related activity, risk-mitigating hedging, or any other permitted activity, and provide specific examples of such inherent conflicts. Do you believe that such conflicts ever result in a materially adverse interest between a banking entity and a client, customer, or counterparty? How should the proposal address inherent conflicts that result from otherwise-permitted activities?

Question 199. Is the manner in which the proposed rule permits the use of disclosure in certain cases to address and mitigate conflicts of interest appropriate? Why or why not? Should additional or alternative requirements be placed on the use of disclosure to address and mitigate conflicts? If so, what additional and alternative requirements, and why? Is the level of detail and specificity required by the proposed rule with respect to disclosure appropriate? If not, what alternative level of detail and specificity would be more appropriate?

Question 200. Should the proposed rule require written disclosure to a client, customer, or counterparty regarding a material conflict of interest? If so, please explain why written disclosure should be required. Are there certain circumstances where written disclosure should be required, but others where oral disclosure should be sufficient? For example, should oral disclosure be permitted for transactions in certain fast-moving markets or transactions with sophisticated clients, customers, or counterparties? If oral disclosure is permitted under certain circumstances, should subsequent written disclosure be required? Please explain.

Question 201. Should the proposed rule provide further detail regarding the types of conflicts of interest that cannot be addressed and mitigated through disclosure? If so, what type of additional detail would be helpful, and why? Should the proposed rule enumerate an exhaustive or non-exhaustive list of conflicts that cannot be addressed and mitigated through disclosure? If so, what conflicts should that list include, and why?

Question 202. Should the proposed rule provide further detail regarding the frequency at which disclosure must be made? Should general disclosure be permitted for certain types of transactions, classes of transactions, or activities? For example, should a banking entity be permitted to make a one-time, written disclosure to a client, customer, or counterparty prior to engaging in a certain type of transaction or activity? Should general disclosure be permitted for certain types of clients, customers, or counterparties (e.g., highly sophisticated parties)? Please explain why specific disclosure (i.e., prior to each transaction, class of transaction, or activity) would not be necessary under the identified circumstances. Are there any clients, customers, or counterparties that should be able to waive a material conflict of interest under certain circumstances? If so, under what circumstances would a waiver approach be appropriate and consistent with the statute? Please explain.

Question 203. Should the proposed definition of material conflict of interest deem certain potential conflicts of interest to not be material conflicts of interest if a banking entity establishes, maintains, and enforces policies and procedures (other than information barriers) reasonably designed to prevent transactions, classes of transactions, or activities that would involve or result in a material conflict of interest? If so, for what types of potential conflicts? What policies and procedures would be appropriate? How would this approach be consistent with the purpose and language of the statute?

Should such policies and procedures only be considered effective if they prevent the banking entity from receiving an advantage to the disadvantage of the client, customer, or counterparty?

Question 204. Are there any particular types of clients, customers, or counterparties for whom disclosure of a material conflict of interest should not be required under the proposal, consistent with the statute? Please identify the types of clients, customers, or counterparties for whom disclosure might not be necessary and explain. Why might disclosures be useful for some clients, customers, or counterparties, but not others? Please explain. What characteristics should a firm use in determining whether or not a client, customer, or counterparty needs a particular disclosure?

Question 205. Are there additional steps that a banking entity that seeks to manage conflicts of interest through the use of disclosure should be required to take with regard to disclosure? If so, what steps?

Question 206. Are there circumstances in which disclosure might be impracticable or ineffective? If so, what circumstances, and why?

Question 207. Is the manner in which the proposed rule permits the use of information barriers to address and mitigate conflicts of interest appropriate? Why or why not? Should additional or alternative requirements be placed on the use of information barriers to address and mitigate conflicts? If so, what additional and alternative requirements, and why?

Question 208. Should the proposed rule mandate the use of other means of managing potential conflicts of interest? If so, what specific means should be considered? How effective are any such methods as currently used? Can such methods be circumvented? If so, in what ways?

Question 209. What burdens or costs might be associated with the disclosure-related or information barrier-related requirements contained in the proposed definition of material conflict of interest? How might these burdens or costs be eliminated or reduced in a manner consistent with the purpose and language of section 13 of the BHC Act?

Question 210. Are there specific transactions, classes of transactions or activities that should be managed through consent? If so, what transactions or activities, and why? What form of consent should be required? What level of detail should any such consent include? Should consent only apply to certain conflicts and not others? If so, which conflicts? Are there circumstances in which obtaining consent might be impracticable or ineffective? Should consent be limited to certain types of clients, customers, or counterparties? If so, which clients, customers, or counterparties? Are there certain types of clients, customers, or counterparties for whom consent would never be sufficient? Are there additional steps that a banking entity that seeks to manage conflicts of interest through the use of consent should be required to take? Please specify such steps.

Question 211. What is the potential relationship between, and interplay of, the proposed rule and Section 621 of the Dodd-Frank Act regarding conflicts of interest relating to certain securitizations which contains a prohibition on material conflicts of interest?

Question 212. Should the proposed rule provide for specific types of procedures that would be more effective in managing and mitigating conflicts of interest than others? Do banking entities currently use certain procedures that effectively manage and mitigate material conflicts of interest? If so, please describe such procedures and explain why such procedures are effective. Is the proposed rule

consistent with such procedures? Why or why not? What are the costs and benefits of modifying your current procedures in response to the proposed rule?

Question 213. Is the proposed rule's definition of a high-risk asset effective and sufficiently clear? If not, what alternative would be more effective and/or clearer? Should the proposed rule specify particular assets that are deemed high-risk per se? If so, what assets and why?

Question 214. Is the proposed rule's definition of a high-risk trading strategy effective and sufficiently clear? If not, what alternative would be more effective and/or clearer? Should the proposed rule specify particular trading strategies that are deemed high-risk per se? If so, what trading strategies and why?

Subpart C - Covered Fund Activities and Investments

The Agencies request comment on the proposed rule's approach to defining the terms "covered fund", "ownership interest", and other related terms, including with respect to the following:

Question 215. Is the proposed rule's approach to applying section 13 of the BHC Act's restrictions related to covered fund activities and investments to those instances where a banking entity acts "as principal or beneficial owner" effective? If not, why? What alternative approach might be more effective in light of the language and purpose of the statute?

Question 216. Does the proposed rule effectively address the circumstances under which an investment by a director or employee of a banking entity in a covered fund would be attributed to a banking entity? If not, why? What alternative might be more effective?

Question 217. Does the proposed rule's definition of "covered fund" effectively implement the statute? What alternative definitions might be more effective in light of the language and purpose of the statute?

Question 218. Is specific inclusion of commodity pools within the definition of "covered fund" effective and consistent with the language and purpose of the statute? Why or why not?

Question 219. The proposed definition of "sponsor" focuses on "the ability to control the decision-making and operational functions of the fund." In the securitization context, is this an appropriate manner to determine the identity of the sponsor? If not, what factors should be used to determine the identity of the sponsor in the securitization context for purposes of the proposed rule and why? Is the definition of "sponsor" set forth in the SEC's Regulation AB233 an appropriate party to treat as sponsor for purposes of the proposed rule? Is additional guidance necessary with respect to how the proposed definition of "sponsor" should be applied to a securitization transaction?

Question 220. Should the application of the proposed definition of "sponsor" mean that the servicer or investment manager in a securitization transaction would be considered the sponsor for purposes of the proposed rule? What impact would this interpretation of the proposed definition have on existing securitizations?

Question 221. Should the definition of "covered fund" focus on the characteristics of an entity rather than whether it would be an investment company but for section 3(c)(1) or 3(c)(7) of the Investment Company Act? If so, what characteristics should be considered and why? Would a definition focusing

on an entity's characteristics rather than its form be consistent with the language and purpose of the statute?

Question 222. Instead of adopting a unified definition of "covered fund" for those entities included under section 13(h)(2) of the BHC Act, should the Agencies consider having separate definitions for "hedge fund" and "private equity fund"? If so, which definitions and why?

Question 223. Should the Agencies consider using the authority provided under section 13(d)(1)(J) of the BHC Act to exempt the acquisition or retention of an ownership interest in a covered fund with certain attributes or characteristics, including, for example: (i) a performance fee or allocation to an investment manager's equity account calculated by taking into account income and realized and unrealized gains; (ii) borrowing an amount in excess of one-half of its total capital commitments or has gross notional exposure in excess of twice its total capital commitments; (iii) sells securities or other assets short; (iv) has restricted or limited investor redemption rights; (v) invests in public and non-public companies through privately negotiated transactions resulting in private ownership of the business; (vi) acquires the unregistered equity or equity-like securities of such companies that are illiquid as there is no public market and third party valuations are not readily available; (vii) requires holding those investments long-term; (viii) has a limited duration of ten years or less; or (ix) returns on such investments are realized and the proceeds of the investments are distributed to investors before the anticipated expiration of the fund's duration? Which, if any, of these characteristics are appropriate to describe a hedge fund or private equity fund that should be considered a covered fund for purposes of this rule? Are there any other characteristics that would be more appropriate to describe a covered fund? If so, which characteristics and why?

Question 224. Is specific inclusion of certain non-U.S. entities as a "covered fund" under § __.10(b)(1)(iii) of the proposed rule necessary, or would such entities already be considered to be a "covered fund" under § __.10(b)(1)(i) of the proposed rule? If so, why? Does the proposed rule's language on non-U.S. entities correctly describe those non-U.S. entities, if any, that should be included in the definition of "covered fund"? Why or why not? What alternative language would be more effective? Should we define non-U.S. funds by reference to the following structural characteristics: whether they are limited in the number or type of investors; whether they operate without regard to statutory or regulatory requirements relating to the types of instruments in which they may invest or the degree of leverage they may incur? Why or why not?

Question 225. Are there any entities that are captured by the proposed rule's definition of "covered fund," the inclusion of which does not appear to be consistent with the language and purpose of the statute? If so, which entities and why?

Question 226. Are there any entities that are not captured by the proposed rule's definition of "covered fund," the exclusion of which does not appear to be consistent with the language and purpose of the statute? If so, which entities and why?

Question 227. Do the proposed rule's definitions of "covered fund" and/or "ownership interest" pose unique concerns or challenges to issuers of asset-backed securities and/or securitization vehicles? If so, why? Do certain types of securitization vehicles (trusts, LLCs, etc.) typically issue asset-backed securities which would be included in the proposed definition of ownership interest? What would be the impact of the application of the proposed rules to these securitization vehicles? Are certain asset classes (collateralized debt obligations, future flows, corporate debt repackages, etc.) more likely to

be impacted by the proposed definition of "covered fund" because the issuer cannot rely on an exemption other than 3(c)(1) or 3(c)(7) of the Investment Company Act?

Question 228. How many existing issuers of asset-backed securities would be included in the proposed definition of "covered fund?" What would be the legal and economic impact of the proposed rule on holders of asset-backed securities issued by existing securitization vehicles that would be included in the proposed definition of covered fund?

Question 229. Are there entities that issue asset-backed securities (as defined in Section 3(a) of the Exchange Act) that should be exempted from the requirements of the proposed rule? How would such an exemption promote and protect the safety and soundness of the banking entity and the financial stability of the United States as required by section 13(d)(1)(J) of the BHC Act?

Question 230. Since certain existing asset-backed securities may have a term that exceeds the conformance or extended transition periods provided for under section 13(c) of the BHC Act, should the Agencies consider using the authority contained in section 13(d)(1)(J) of that Act to exclude those existing asset-backed securities from the proposed definition of "ownership interest" and/or should the rule permit a banking entity to acquire or retain an ownership interest in existing asset-backed issuers? If so, how would either approach be consistent with the language and purpose of the statute?

Question 231. Many issuers of asset-backed securities have features and structures that resemble some of the features of hedge funds and private equity funds (e.g., CDOs are managed by an investment adviser that has the discretion to choose investments, including investments in securities). If the proposed definition of “covered fund” were to exempt any entity issuing asset-backed securities, would this allow for interests in hedge funds or private equity funds to be structured as asset-backed securities and circumvent the proposed rule? If this approach is taken, how should the proposal address this concern?

Question 232. Are the structural similarities between an entity that issues asset-backed securities and hedge funds and private equity funds of sufficient concern that the Agencies should not exclude any entity that issues asset-backed securities from the definition of covered fund?

Question 233. Should entities that rely on a separate exclusion from the definition of investment company other than sections 3(c)(1) or 3(c)(7) of the Investment Company Act be included in the definition of “covered fund”? Why or why not?

Question 234. Do the proposed rule’s definitions of “ownership interest” and “carried interest” effectively implement the statute? What alternative definitions might be more appropriate in light of the language and purpose of the statute? Are there other types of instruments that should be included or excluded from the definition of “ownership interest”? Does the proposed definition of ownership interest capture most interests that are typically viewed as ownership interests? Is the proposed rule’s exemption of carried interest from the definition of ownership interest with respect to a covered fund appropriate? Does the exemption adequately address existing compensation arrangements and the way in which a banking entity becomes entitled to carried interest? Is it consistent with the current tax treatment of these arrangements?

Question 235. In the context of asset-backed securities, the distinction between debt and equity may be complicated (e.g., trust certificates issued in a residential mortgage backed security transaction) and the legal, accounting and tax treatment may differ for the same instrument. Is guidance

necessary with respect to the application of the definition of ownership interest for asset-backed securitization transactions?

Question 236. In many securitization transactions, the residual interest represents the “equity” in the transaction. As this often constitutes the portion of the securitization transaction with the most risk, because it may absorb any losses experienced by the underlying assets before any other interests issued by the securitization vehicle, should the Agencies instead use their authority under section 13(d)(1)(J) of the BHC Act to exempt the buying and selling of any ownership interest in a securitization vehicle that is a covered fund other than the residual interest?

Question 237. For purposes of limiting either an exclusion for issuers of asset-backed securities from the proposed definition of “covered fund” and/or an exclusion of asset-backed securities from the proposed definition of "ownership interest," what definition of asset-backed security most effectively implements the language of section 13 of the BHC Act? Section 3(a)(77) of the Exchange Act and the SEC’s Regulation AB234 provide two possible definitions. Is either of these definitions sufficient, and if so why? If one of the definitions is too narrow, what additional entities/securities should be included and why? If one of the definitions is too broad, what entities/securities should be excluded and why? Would some other definition of asset-backed security be more consistent with the language and purpose of section 13 of the BHC Act?

Question 238. Are there special concerns raised by not including as an ownership interest the residual interests in a securitization vehicle? Should the Agencies instead exempt the buying and selling of any ownership interest in a securitization vehicle that is a covered fund other than the residual interest?

Question 239. Should the legal form of a beneficial interest be a determining factor for deciding whether a beneficial interest is an “ownership interest”? For example, should pass-through trust certificates issued as part of a securitization transaction be excluded from the definition of “ownership interest”? Should the definition of ownership interest explicitly include debt instruments with equity features (e.g., voting rights, profit participations, etc.)?

Question 240. How should the proposed rule address those instances in which both debt and equity interests are issued, and the debt interests receive all of the economic benefits and all of the control rights? Should the debt interests (other than the residual interest) be counted as ownership interests even though they are not legally ownership and do not receive any profit participation? Should the equity interests be counted as ownership interests even though the holder does not receive economic benefits or have any control rights? Should the residual interest be considered the only "ownership interest" for purposes of the proposed rule? Should mezzanine interests that lack both control rights and profit participation be considered an ownership interest? If the mezzanine interests obtain control rights (because more senior classes have been repaid), should they become "ownership interests" at that time for purposes of the proposed rule? If both debt and equity interests are counted as ownership interests, how should percentages of ownership interests be calculated when the units of measurement do not match (e.g., a single trust certificate, a single residual certificate with no face value and multiple classes of currency-denominated notes)?

Question 241. Does the proposed rule’s definition of “prime brokerage transaction” effectively implement the statute? What other types of transactions or services, if any, should be included in the definition? Should any types of transactions or services be excluded from the definition? Would an alternative definition be more effective, and if so, why?

Question 242. Do the proposed rule's definitions of "sponsor" and "trustee" effectively implement the statute? Is the exclusion of "directed trustee" from the definition of "trustee" appropriate?

Question 243. Do the proposed rule's other definitions in § __.10(b) effectively implement the statute? What alternative definitions might be more effective in light of the language and purpose of the statute? Are additional definitions needed, and if so, what definition(s)?

The Agencies request comment on the proposed rule's approach and the following questions with respect to implementing the exemption permitting banking entities to organize and offer a covered fund:

Question 244. Is the proposed rule's approach to implementing the exemption for organizing and offering a covered fund effective? If not, what alternative approach would be more effective and why?

Question 245. Should the approach include other elements? If so, what elements and why? Should any of the proposed elements be revised or eliminated? If so, why and how?

Question 246. Is the proposed rule's approach to implementing the scope of bona fide trust, fiduciary, investment advisory and commodity trading advisory services consistent with the statute? If not, what alternative approach would be more effective? Should the scope of such services be broader or, in the alternative, more limited? Are there specific services which should be included but which are not currently under the proposed rule?

Question 247. Does the proposed rule effectively implement the "customers of such services" requirement? If not, what alternative approach would be more effective and why? Is the proposed rule's approach consistent with the statute? Why or why not? How do banking entities currently sell or provide interests in covered funds? Do banking entities rely on a concept of "customer" by reference to other laws or regulations, and if so, what laws or regulations?

Question 248. Does the proposed rule effectively and clearly recognize the manner in which banking entities provide trust, fiduciary, investment advisory, or commodity trading advisory services to customers? If not, how should the proposed rule be modified to be more effective or clearer?

Question 249. Should the Agencies consider adopting a definition of "customer of such services" for purposes of implementing the exemption related to organizing and offering a covered fund? If so, what criteria should be included in such definition? For example, should the customer requirement specify that the relationship be pre-existing? Should the Agencies consider adopting an existing definition related to "customer" and if so, what definitions (for instance, the SEC's "pre-existing, substantive relationship" concept applicable to private offerings under its Regulation D) would provide for effective implementation of the customer requirement in section 13(d)(1)(G) of the BHC Act? If so, why and how? How should the customer requirement be applied in the context of non-U.S. covered funds? Is there an equivalent concept used for such non-U.S. covered fund offerings?

Question 250. Should the Agencies distinguish between direct and indirect customer relationships for purposes of implementing section 13(d)(1)(G) of the BHC Act? Should the rule differentiate between a customer relationship established by a customer as opposed to a banking entity? If so, why?

Question 251. Does the proposed rule effectively implement the prohibition on a banking entity guaranteeing or insuring the obligations or performance of certain covered funds? If not, what alternative approach would be more effective, and why?

Question 252. Does the proposed rule effectively implement the requirement that a banking entity comply with the limitation on certain relationships with a covered fund contained in § __.16 of the proposed rule? If not, what alternative approach would be more effective, and why?

Question 253. Does the proposed rule effectively implement the prohibition on a covered fund sharing the same name or variation of the same name with a banking entity? If not, what alternative approach would be more effective and why? Should the prohibition on a covered fund sharing the same name be limited to specific types of banking entities (e.g., insured depository institutions and bank holding companies) or only to the banking entity that organizes and offers the fund, and if so why?

Question 254. Does the proposed rule effectively implement the limitation on director or employee investments in a covered fund organized and offered by a banking entity? If not, what alternative approach would be more effective and why? Should the agencies provide additional guidance on what "other services" should be included for purposes of satisfying § __.11(g)? Why or why not?

Question 255. Are the disclosure requirements related to organizing and offering a covered fund appropriate? If not, what alternative disclosure requirement(s) should the proposed rule include? Should the Agencies consider adoption of a model disclosure form related to this requirement? Does the timing of the proposed disclosure requirement adequately address disclosure to secondary market purchasers?

The Agencies request comment on the following with respect to the proposed rule's approach to implementing the exemption for a banking entity to make or retain a permitted investment in a covered fund that it organizes and offers:

Question 256. Is the proposed rule's approach to implementing the exemption that allows a banking entity to make or retain a permitted investment in a covered fund effective? If not, what alternative approach would be more effective and why?

Question 257. Should the approach include other elements? If so, what elements and why? Should any of the proposed elements be revised or eliminated? If so, why and how?

Question 258. Should the proposed rule specify at what point a covered fund will be considered to have been "established" for purposes of commencing the period in which a banking entity may own more than 3 percent of the total outstanding ownership interests in such fund? If so, why and how?

Question 259. Does the proposed rule effectively implement the requirement that a banking entity comply with the limitations on an investment in a single covered fund? If not, what alternative approach would be more effective and why?

Question 260. Does the proposed rule effectively implement the requirement that a banking entity comply with the limitations on the aggregate of all investments in all covered funds? If not, what alternative approach would be more effective and why?

Question 261. Is the proposed rule's approach to calculating a banking entity's investment in a covered fund effective? Should the per-fund calculation be based on committed capital, rather than invested capital? Why or why not? Is the timing of the calculation of a banking entity's ownership interest in a single covered fund appropriate? If not, why not, and what alternative approach would be more effective and why? For example, should the per-fund calculation be required on a less-frequent

basis (e.g., monthly) for funds that compute their value and allow purchases and redemptions on a daily basis (e.g., daily)? Why or why not?

Question 262. Is the proposed rule's approach to parallel investments effective? Why or why not? Should this provision require a contractual obligation and/or knowing participation? Why or why not? How else could the proposed rule define parallel investments? What characteristics would more closely achieve the scope and intended purposes of section 13 of the BHC Act?

Question 263. Is the proposed rule's treatment of investments in a covered fund by employees and directors of a banking entity effective? If not, what alternative approach would be more effective and why?

Question 264. Is the proposed rule's approach to differentiating between controlled and noncontrolled investments in a covered fund unduly complex or burdensome? If so, what alternative approach, if any, would be more effective and why?

Question 265. Is the proposed rule's approach to valuing an investment in a covered fund according to the same standards utilized by the covered fund for determining the aggregate value of its assets and ownership interests effective? If not, what alternative valuation approach would be more effective and why? Should the rule specify one methodology for valuing an investment in a covered fund?

Question 266. Is the proposed rule's approach regarding when to require the calculation of a banking entity's aggregate investments in all covered funds effective? What is the potential impact of calculating a banking entity's aggregate investment limit under the proposed rule on a quarterly basis as opposed to solely at the time an investment in a covered fund is made? Would calculation of the aggregate investment limit solely at the time an investment in a covered fund is made be consistent with the language and purpose of the statute? Does the proposed rule provide sufficient guidance for an issuer of asset-backed securities about how and when to make such calculation? Why or why not?

Question 267. Is the proposed rule's approach to determining and calculating a banking entity's relevant tier 1 capital limit effective? If not, what alternative approach would be more effective and why? With respect to applying the aggregate funds limitation to a banking entity that is not affiliated with an entity that is required to hold and report tier 1 capital, is total shareholder equity on a consolidated basis as of the last day of the most recent calendar quarter that has ended an effective proxy for tier 1 capital? If not, what alternative approach would be more effective and why?

Question 268. Should the proposed rule be modified to permit a banking entity to bring its investments in covered funds into compliance with the proposed rule within a reasonable period of time if, for example, the banking entity's aggregate permitted investments in covered funds exceeds 3 percent of its tier 1 capital for reasons unrelated to additional investments (e.g., a banking entity's tier 1 capital decreases)? Why or why not?

Question 269. Does the proposed rule effectively and appropriately implement the deduction from capital for an investment in a covered fund contained in section 13(d)(4)(B)(iii) of the BHC Act? If not, what alternative approach would be more effective or appropriate, given the statutory language of the BHC Act and overall structure of section 13(d)(4), and why? What effect, if any, should the Agencies give to the cross-reference in section 13(d)(4) to section 13(d)(3) of the BHC Act, which provides Agencies with discretion to require additional capital, if appropriate, to protect the safety and soundness of banking entities engaged in activities permitted under section 13 of the BHC Act? How, if

at all, should a banking entity's deduction of its investment in a covered fund be increased commensurate with the leverage of the covered fund? Should the amount of the deduction be proportionate to the leverage of the covered fund? For example, instead of a dollar-for-dollar deduction, should the deduction be set equal to the banking entity's investment in the covered fund times the difference between 1 and the covered fund's equity-to-assets ratio?

Question 270. Does the proposed rule effectively implement the Board's statutory authority to grant an extension of the period of time a banking entity may retain in excess of 3 percent of the ownership interests in a single covered fund? Are the enumerated factors that the Board may consider in connection with reviewing such an extension appropriate (including factors related to the effect of an extension of the covered fund), and if not, why not? Are there additional factors that the Board should consider in reviewing such a request? Are there specific additional conditions or limitations that the Board should, by rule, impose in connection with granting such an extension? If so, what conditions or limitations would be more effective?

Question 271. Given that the statute does not provide for an extension of time for a banking entity to comply with the aggregate funds limitation, within what period of time should a banking entity be required to bring its investments into conformance with the aggregate funds limit? Should the proposed rule expressly contain a grace period for complying with these limits? Why or why not? If yes, what grace period would be most effective and why?

Question 272. Does the proposed rule effectively implement the prohibition on a banking entity guaranteeing or insuring the obligations or performance of certain covered funds? If not, what alternative approach would be more effective and why?

Question 273. In the context of securitization transactions, control and ownership are often completely separated. Is additional guidance necessary with respect to how control should be determined with respect to issuers of asset-backed securities for purposes of determining the calculation of the per-fund and aggregate ownership limitations?

Question 274. In many securitization transactions, the voting rights of investors are extremely limited and management may be contractually delegated to a third party (because issuers of asset-backed securities rarely have a board with any authority or any employees). The servicer or manager has the "ability to control the decision-making and operational functions of the fund." When calculating the per-fund and aggregate ownership limitations, to whom should the proposed rule allocate "control" in this type of situation? Which participants in a securitization transaction would need to include the activities of an issuer of asset-backed securities in their calculations of per-fund and aggregate ownership, and what is the potential impact of such inclusion?

Question 275. For purposes of calculating the per-fund and aggregate ownership limitations, how should the proposed rule address those instances in which equity is issued, but the equity holder does not receive economic benefits or have any control rights? For instance, in order to enhance or achieve bankruptcy remoteness, a single purpose trust without an owner (i.e, an orphan trust) may hold all of the equity interests in a securitization vehicle. Such interests often do not have any meaningful economic or control rights.

The Agencies request comment on the following regarding the proposed rule's approach to implementing the exemption for permitted investments in and relationships with SBICs and certain related funds:

Question 276. Is the proposed rule's approach to implementing the SBIC, public welfare and qualified rehabilitation investment exemption for acquiring or retaining an ownership interest in a covered fund effective? If not, what alternative approach would be more effective?

Question 277. Should the approach include other elements? If so, what elements and why? Should any of the proposed elements be revised or eliminated? If so, why and how?

Question 278. Should the proposed rule permit a banking entity to sponsor an SBIC and other identified public interest investments? Why or why not? Does the Agencies' determination under section 13(d)(1)(J) of the BHC Act regarding sponsoring of an SBIC, public welfare or qualified rehabilitation investment effectively promote and protect the safety and soundness of banking entities and the financial stability of the United States? If not, why not?

Question 279. What would the effect of the proposed rule be on a banking entity's ability to sponsor and syndicate funds supported by public welfare investments or low income housing tax credits which are utilized to assist banks and other insured depository institutions with meeting their Community Reinvestment Act ("CRA") obligations?

Question 280. Does the proposed rule unduly constrain a banking entity's ability to meet the convenience and needs of the community through CRA or other public welfare investments or services? If so, why and how could the proposed rule be revised to address this concern?

The Agencies request comment on the following with respect to the proposed implementation of the risk-mitigating hedging exemption for covered fund activities:

Question 281. Is the proposed rule's approach to implementing the hedging exemption for acquiring or retaining an ownership interest in a covered fund effective? If not, what alternative approach would be more effective?

Question 282. Should the approach include other elements? If so, what elements and why? Should any of the proposed elements be revised or eliminated? If so, why and how?

Question 283. What burden will the proposed approach to implementing the hedging exemption have on banking entities? How can any burden be minimized or eliminated in a manner consistent with the language and purpose of the statute?

Question 284. Are the criteria included in § __.13(b)'s hedging exemption effective? Is the application of each criterion to potential transactions sufficiently clear? Should any of the criteria be changed or eliminated? Should other requirements be added?

Question 285. Is the requirement that an ownership interest in a covered fund may only be used as a hedge (i) by the banking entity when acting as intermediary on behalf of a customer that is not itself a banking entity to facilitate the exposure by the customer to the profits and losses of the covered fund, or (ii) to cover compensation arrangements with an employee of the banking entity that directly provides investment advisory or other services to that fund effective? If not, what other requirements would be more effective?

Question 286. Does the proposed rule sufficiently articulate the types of risks and positions that a banking entity typically would utilize an ownership interest in a covered fund to hedge? If not, how should the proposal be changed?

Question 287. Is the requirement that that the hedging transaction involve a substantially similar offsetting exposure to the same covered fund and in the same amount of ownership interest to the risk or risks the transaction is intended to hedge or otherwise mitigate effective? If not, how should the requirement be changed? Should some other level of correlation be required? Should the proposal specify in greater detail how correlation should be measured? If not, how could it better do so?

Question 288. Is the requirement that the transaction not give rise, at the inception of the hedge, to material risks that are not themselves hedged in a contemporaneous transaction effective? Is the proposed materiality qualifier appropriate and sufficiently clear? If not, what alternative would be effective and/or clearer?

Question 289. Is the requirement that any transaction conducted in reliance on the hedging exemption be subject to continuing review, monitoring and management after the transaction is established effective? If not, what alternative would be more effective?

Question 290. Is the proposed documentation requirement effective? If not, what alternative would be more effective? What burden would the proposed documentation requirement place on covered banking entities? How might such burden be reduced or eliminated in a manner consistent with the language and purpose of the statute?

With respect to the proposed rule's approach to implementing the foreign covered funds activity and investment exemption, the Agencies request comment on the following:

Question 291. Is the proposed rule's implementation of the "foreign funds" exemption effective? If not, what alternative would be more effective and/or clearer?

Question 292. Are the proposed rule's provisions regarding when an activity will be considered to be conducted pursuant to section 4(c)(9) of the BHC Act effective and sufficiently clear? If not, what alternative would be more effective and/or clearer? Does it effectively address application of the foreign funds exemption to foreign banking entities not subject to the BHC Act generally? If not, how could it better address application of the exemption?

Question 293. Are the proposed rule's provisions regarding when a transaction or activity will be considered to have occurred solely outside the United States effective and sufficiently clear? If not, what alternative would be more effective and/or clearer? Should additional requirements be added? If so, what requirements and why? Should additional requirements be modified or removed? If so, what requirements and why or how?

Question 294. Is the proposed exemption consistent with the purpose of the statute? Is the proposed exemption consistent with respect to national treatment for foreign banking organizations? Is the proposed exemption consistent with the concept of competitive equity?

Question 295. Does the proposed rule effectively define a resident of the United States for these purposes? If not, how should the definition be altered? What definitions of resident of the United States are currently used by banking entities? Would using any one of these definitions reduce the burden of complying with section 13 of the BHC Act? Why or why not?

The Agencies request comment on the following with respect to the proposed rule's approach to implementing the rule of construction related to the sale and securitization of loans:

Question 296. Is the proposed rule's implementation of the statute's "sale and securitization of loans" rule of construction effective? If not, what alternative would be more effective and/or clearer?

Question 297. Are there other entities or activities that should be included in the proposed rule's implementation of the rule of construction related to the sale and securitization of loans? If so, what entity or activity and why?

Question 298. Is the proposed rule's application of the rule of construction contained in section 13(g)(2) of the BHC Act appropriate?

Question 299. Are the proposed rule and this Supplementary Information sufficiently clear regarding which derivatives would be allowed in a "securitization of loans" under § __.13(d)(3) of the proposed rule? Is additional guidance necessary with respect to the types of derivatives that would be included in or excluded from a securitization of loans for purposes of interpreting the rule of construction contained in section 13(g)(2) of the BHC Act? If so, what topics should the additional guidance discuss and why?

Question 300. Should derivatives other than interest rate or foreign exchange derivatives be allowed in a "securitization of loans" for purposes of interpreting the rule of construction contained in section 13(g)(2) of the BHC Act? Why or why not? What would be the legal and economic impact of not allowing the use of derivatives other than interest rate or foreign exchange derivatives in a "securitization of loans" under § __.13(d)(3) of the proposed rule for existing issuers of asset-backed securities and for future issuers of asset-backed securities?

Question 301. Should the Agencies consider providing additional guidance for when a transaction with intermediate steps constitutes one or more securitization transactions that each would be subject to the rule? For example, both auto lease securitizations and asset-backed commercial paper conduits typically involve intermediate securitizations. The asset-backed securities issued to investors in such covered funds are technically supported by the intermediate asset-backed securities. Should these kinds of securitizations be viewed as a single transaction and included within a securitization of loans for purposes of the proposed rule? Should each step be viewed as a separate securitization?

The Agencies request comment on the proposed rule's approach to implementing the exemption related to activities specifically determined to be permissible under section 13(d)(1)(J) of the BHC Act, including the following:

Question 302. Is the proposed rule's implementation of exemptions for covered fund activities and investments pursuant to section 13(d)(1)(J) of the BHC Act effective? If not, what alternative would be more effective and/or clearer?

Question 303. Is the proposed rule's approach to utilizing section 13(d)(1)(J) of the BHC Act to permit a banking entity to acquire or retain an ownership interest in, or act as sponsor to, certain entities that would fall into the definition of covered fund effective? Why or why not? If not, what alternative would be more effective and why? What legal authority under the statute would permit such an alternative?

Question 304. Are the proposed rule's provisions regarding when a covered fund activity will be deemed to be permitted under authority of section 13(d)(1)(J) of the BHC Act effective and sufficiently clear? If not, what alternative would be more effective and/or clearer?

Question 305. Do the exemptions provided for in § __.14 of the proposed rule effectively promote and protect the safety and soundness of banking entities and the financial stability of the United States? If not, why not?

Question 306. Are the proposed rule's provisions regarding what qualifications must be satisfied in order to qualify for an exemption under § __.14 of the proposed rule effective and sufficiently clear? If not, what alternative would be more effective and/or clearer? Should additional requirements be added? If so, what requirements and why? Should additional requirements be modified or removed? If so, what requirements and why or how?

Question 307. Does the proposed rule effectively cover the scope of covered funds activities which the Agencies should specifically determine to be permissible under section 13(d)(1)(J) of the BHC Act? If not, what activity or activities should be permitted? For additional activities that should be permitted, on what grounds would these activities promote and protect the safety and soundness of banking entities and the financial stability of the United States?

Question 308. Does the proposed rule effectively address the interplay between the restrictions on covered fund activities and investments in section 13 of the BHC Act and the requirements imposed on certain banking entities under section 15G of the Exchange Act? Why or why not?

Question 309. Rather than permitting the acquisition or retentions of an ownership interest in, or acting as sponsor to, specific covered funds under section 13(d)(1)(J) of the BHC Act, should the Agencies use the authority provided under section 13(d)(1)(J) to permit investments in a covered fund that display certain characteristics? If so, what characteristics should the Agencies consider? How would investments with such characteristics promote and protect the safety and soundness of the banking entity and promote the financial stability of the United States?

Question 310. Should venture capital funds be excluded from the definition of "covered fund"? Why or why not? If so, should the definition contained in rule 203(l)-1 under the Advisers Act be used? Should any modification to that definition of venture capital fund be made? How would permitting a banking entity to invest in such a fund meet the standards contained in section 13(d)(1)(J) of the BHC Act?

Question 311. Should non-U.S. funds or entities be included in the definition of "covered fund"? Should any non-U.S. funds or entities be excluded from this definition? Why or why not? How would permitting a banking entity to invest in such a fund meet the standards contained in section 13(d)(1)(J) of the BHC Act?

Question 312. Should so-called "loan funds" that invest principally in loans and not equity be excluded from the definition of "covered fund"? Why or why not? What characteristics would be most effective in determining whether a fund invests principally in loans and not equity? How would permitting a banking entity to invest in such a fund meet the standards contained in section 13(d)(1)(J) of the BHC Act?

Question 313. Are the proposed rule's proposed determinations that the specified covered funds activities or investments promote and protect the safety and soundness of banking entities and the financial stability of the United States appropriate? If not, how should the determinations be amended or altered?

The Agencies request comment on the proposed rule's approach to implementing the limitations on certain relationships with covered funds and a banking entity's ability to make explicitly permitted investments for these purposes, including the following:

Question 314. Is the proposed rule's approach to implementing the limitations on certain transactions with a covered fund effective? If not, what alternative approach would be more effective and why?

Question 315. Should the approach include other elements? If so, what elements and why? Should any of the proposed elements be revised or eliminated? If so, why and how?

Question 316. What types of transactions or relationships that currently exist between banking entities and a covered fund (or another covered fund in which such covered fund makes a controlling investment) would be prohibited under the proposed rule? What would be the effect of the proposed rule on banking entities' ability to continue to meet the needs and demands of their clients? Are there other transactions between a banking entity and such covered funds that are not already covered but that should be prohibited or limited under the proposed rule?

Question 317. Should the Agencies provide a different definition of "prime brokerage transaction" under the proposed rule? If so, what definition would be appropriate? Are there any transactions that should be included in the definition of "prime brokerage transaction"? Are there transactions or practices provided by banking entities that should be excluded in order to mitigate the burdens of complying with section 13 of the BHC Act?

Question 318. With respect to the CEO (or equivalent officer) certification required under section 13(f)(3)(A) (ii) of the BHC Act and § __.16(a)(2)(ii)(B) of the proposed rule, what would be the most useful, efficient method of certification (e.g., a new stand-alone certification, a certification incorporated into an existing form or filing, website certification, or certification filed directly with the relevant Agency)?

Subpart D (Compliance Program Requirement) and Appendix C (Minimum Standards for Programmatic Compliance)

The Agencies request comment on the following with respect to the compliance program requirement contained in the proposed rule and the minimum standards specified in proposed Appendix C:

Question 319. Is the proposed rule's inclusion of a compliance program requirement effective in light of the purpose and language of the statute? If not, what alternative would be more effective?

Question 320. Is the proposed application of § __.20's compliance program requirement to all banking entities engaged in covered trading activity or covered trading investments and activities and the minimum standards of proposed Appendix C to only banking entities with significant covered trading or covered fund activities, effective? If not, what alternative would be more effective? Should proposed Appendix C apply to all banking entities? If so, why? Are the thresholds proposed for determining whether a banking entity must comply with proposed Appendix C appropriate? If not, what alternative would be more effective?

Question 321. What implementation, operational, or other burdens or expenses might be associated with the compliance program requirement? How could those burdens or expenses be reduced or eliminated in a manner consistent with the purpose and language of the statute?

Question 322. Do the proposed compliance program requirement and minimum standards provide sufficient guidance and clarity regarding how compliance programs should be structured? If not, what additional guidance or clarity is needed? Do the proposed compliance program requirement and minimum standards provide sufficient discretion to banking entities to structure a compliance program that appropriately reflects the unique nature of their businesses? If not, how could additional discretion be provided in a manner consistent with the purpose and language of the statute?

Question 323. Are the six proposed elements of a required compliance program effective? If not, what alternative would be more effective? Should elements be added or removed? If so, which ones and why?

Question 324. For each of the six proposed elements of a required compliance program for which minimum standards are provided in proposed Appendix C, are the proposed minimum standards effective? If not, what alternative would be more effective? Should minimum standards be added or removed? If so, which ones and why?

Question 325. Does the requirement that a banking entity provide timely notification to the relevant Agency provide sufficient guidance as to what activities must be reported and how and when such reporting should be made? Should more specific standards be provided (e.g., regarding the timing of reporting and the types of activities that must be reported)? If so, what additional criteria should be implemented? Should the notification requirement be applied explicitly to banking entities that are not required to comply with the minimum standards specified in Appendix C because they are below the thresholds specified in §__.20(c)(2)? Why or why not?

Question 326. Are there specific records that banking entities should be required to make and keep to document compliance with section 13 of the BHC Act and the proposed rule? Please explain.

Question 327. What process should the Agencies use in determining whether to require a banking entity that, based on its size, would not be subject to Appendix C to comply with all or portions of the appendix under section I.E of the proposed appendix? What considerations should the Agencies take into account in making such a determination? Should this requirement be implemented by an Agency order, by authority delegated to Agency staff, or a different method? Please explain.

Question 328. Should the proposed rule permit banking entities to comply with Appendix C of the proposed rule on an enterprise-wide basis? If so, why? What are the advantages and disadvantages of an enterprise-wide compliance program? Should the proposed appendix provide additional clarity or discretion regarding how such an enterprise-wide program should be structured? If so, how? Please include a discussion relating to the infrastructure of an enterprise-wide compliance program and its management. If enterprise-wide compliance or similar programs are used in other contexts, please describe your experience with such programs and how those experiences influence your judgment concerning whether or not you would choose an enterprise-wide compliance program in this context.

Question 329. Should the proposed rule permit banking entities to comply with § __.20(b) of the proposed rule on an enterprise-wide basis? If so, why? What are the advantages and disadvantages of an enterprise-wide compliance program for smaller banking entities that are not subject to Appendix C? Please include a discussion relating to the infrastructure of an enterprise-wide compliance program and its management in the context of smaller banking entities. If enterprise-wide compliance or similar programs are used in other contexts, please describe your experience with such programs and how those experiences influence your judgment concerning whether or not you would choose an

enterprise-wide compliance program in this context. Are there particular reasons why a enterprise-wide compliance program should be permitted for larger banking entities subject to the requirements of Appendix C, but not those that are subject to § __.20(b) of the proposed rule?

Question 330. What are the particular challenges that should be considered in connection with establishing a compliance program on an enterprise-wide basis? How will such challenges be addressed? Can an enterprise-wide compliance program be appropriately tailored to each of the subsidiaries and affiliates of a banking entity?

Question 331. Are there efficiencies that can be gained through an enterprise-wide compliance program? If so, how and what efficiencies?

Question 332. Would the complexities of various types of covered trading activity be adequately reflected in an enterprise-wide compliance program?

Question 333. Should only outside parties be permitted to conduct independent testing for the effectiveness of the proposed compliance program to satisfy certain minimum standards? If so, why? Under the proposal, the independent testing requirement may be satisfied by testing conducted by an internal audit department or a third party. Should the rule specify the minimum standards for "independence" as applied to internal and/or external parties testing the effectiveness of the compliance program? For example, would an internal audit be deemed to be independent if none of the persons involved in the testing are involved with, or report to persons that are involved with, activities implicated by section 13 of the BHC Act? Why or why not?

Question 334. Do you anticipate that banking entities that do not meet the thresholds specified in §_.20(c) would voluntarily comply with the proposed minimum standards in Appendix C in order to effectively implement the six elements specified in §_.20(b)? Are there specific minimum standards that would not be practical or would be unattainable for a banking entity that does not meet the §__.20(c) thresholds? Please identify the minimum standard(s) and explain.

Question 335. In light of the size, scope, complexity, and risk of covered trading activities, do commenters anticipate the need to hire new staff with particular expertise in order to establish, maintain, and enforce the proposed compliance program requirement concerning covered trading activities or any subset of covered trading activities?

Question 336. With respect to the proposed requirement that training should occur with a frequency appropriate to the size and risk profile of the banking entity's covered trading activities and covered fund activities, should there be a minimum requirement that such training shall be conducted no less than once every twelve (12) months? If so, why?

Question 337. Should proposed rule's Appendix C be revised to require a banking entity's CEO to annually certify that the banking entity has in place processes to establish, maintain, enforce, review, test and modify the compliance program established pursuant to Appendix C in a manner that is reasonably designed to achieve compliance with section 13 of the BHC Act and this proposal? If so, why? If so, what would be the most useful, efficient method of certification (e.g., a new stand-alone certification, a certification incorporated into an existing form or filing, website certification, or certification filed directly with the relevant Agency)? Would a central data repository with a CEO attestation to the Agencies be a preferable approach?

Question 338. Do the proposed rule requirements relating to establishment and implementation of a compliance program pose unique concerns or challenges to issuers of asset-backed securities that are banking entities, and if so, why? Are certain asset classes particularly impacted by the proposed rule requirements, and if so, how?

Question 339. How would existing issuers of asset-backed securities that are banking entities pay for establishing and implementing a compliance program? Should existing issuers of asset-backed securities that cannot comply with the compliance program requirements be excluded from the proposed definition of "banking entity"? Should such exclusion be limited, and if so, based on what factors? Are the proposed thresholds specified in § __.20(c) of the proposed rule and/or the allowance of an enterprise-wide compliance program as set forth in Appendix C of the proposed rule sufficient to minimize these concerns for issuers of asset-backed securities?

Question 340. With respect to future securitizations, what would be the impact of the establishment and implementation of the compliance program related to the provisions of the proposed rule as required by § __.20 of the proposed rule (including Appendix C, where applicable)? Are the proposed thresholds specified in § __.20(c) of the proposed rule and/or the allowance of an enterprise-wide compliance program as set forth in Appendix C of the proposed rule sufficient to minimize these concerns for issuers of asset-backed securities?

Question 341. Would existing issuers of asset-backed securities that are banking entities be able to establish and implement a compliance program related to the provisions of the proposed rule as required by § __.20 of the proposed rule (including Appendix C, where applicable)? If amendments to transactional documents are necessary, are there any obstacles that would make such amendments difficult to execute? If existing issuers of asset-backed securities cannot establish and implement a compliance program, what would be the impact on such existing issuers of asset-backed securities and the holders of securities issued by a noncompliant issuer of asset-backed securities? Is the allowance of an enterprise-wide compliance program as set forth in Appendix C of the proposed rule sufficient to minimize these concerns for issuers of asset-backed securities?

Question 342. To rely on the exemptions for permitted underwriting, market making-related, and risk-mitigating hedging activities, the proposed rule requires banking entities to establish the internal compliance program under § __.20 and, where applicable, Appendix C, designed to ensure compliance with the requirements of the applicable exemption (e.g., policies and procedures, internal controls and monitoring procedures, etc.). Do these requirements in the proposed rule impose undue cumulative burdens, such that the marginal benefit of a given requirement is not justified by the cost that the requirement imposes? If so, why does the proposed rule impose cumulative burdens and what are the costs of those burdens? Please explain the circumstances under which these burdens may arise. Is there a way to reduce or eliminate such burdens or requirements in a manner consistent with the language and purpose of the statute? For any requirements that impose undue burdens, are there other requirements that could be substituted that would more efficiently ensure compliance with the statute? Are there any requirements that the proposed rule imposes that are particularly effective, and if so, how can the Agencies make better use of these requirements?

Question 343. Are the six elements of the proposed compliance program requirement mutually reinforcing and cost effective, or are there redundancies in the six elements? Please explain any redundant requirements in the policies and procedures, internal controls, management framework, independent testing, training, and recordkeeping requirements in § __.20(b) of the proposed rule or

proposed Appendix C. Why are such requirements redundant, and how should the redundancy be addressed and remedied in the rule?

Question 344. A banking entity that meets the $1 billion or greater trading assets and liabilities threshold would be required under the proposed rule to comply with both the reporting and recordkeeping requirements in Appendix A with respect to quantitative measurements and the compliance program requirement in Appendix C. Are the requirements in these appendices mutually reinforcing and cost effective, or do the appendices impose redundant requirements on banking entities that meet the $1 billion threshold? Please explain any redundant requirements in the appendices and how such redundancy should be addressed and remedied in the rule.

Question 345. Proposed Appendix C incorporates the quantitative measurements provided in proposed Appendix A in the internal controls requirement for banking entities that are engaged in covered trading activity and meet the $1 billion or greater trading assets and liabilities threshold. Do the requirements in proposed Appendix A and Appendix C impose undue cumulative burdens with respect to any elements (e.g., quantitative measurements), such that the marginal benefit of a given requirement is not justified by the cost that the requirement imposes? Please explain why the proposed appendices impose cumulative burdens, the costs of those burdens, and the circumstances under which these burdens may arise. Is there a way to reduce or eliminate such burdens or requirements in a manner consistent with the language and purpose of the statute? For any requirements in the appendices that impose undue burdens, are there other requirements that could be substituted that would more efficiently ensure compliance with the statute? Are there any requirements that the proposed appendices impose that are particularly effective, and if so, how can the Agencies make better use of these requirements?

Question 346. Should the relevant Agency prescribe any specific method by which the board of directors or similar corporate body reviews and approves the compliance program? For example, should the relevant Agency require that: (i) a chief compliance officer or similar officer present an annual compliance report including, as appropriate, recommended actions to be taken by the banking entity to improve compliance or correct any compliance deficiencies; (ii) the board review any such recommendations and determine whether to approve them; and (iii) the banking entity notify the relevant Agency if the board declines to approve such recommendations, or approves different actions than those recommended in the compliance report? What are the advantages and disadvantages of such an approach?

The Federal Reserve Board requests comment on the following regarding the interplay between its previously issued Conformance Rule for implementation of the Volcker Rule and the current proposed rule:

Question 347. Should any portion of the Board's Conformance Rule be revised in light of other elements of the current proposed rule? If so, why and how?

Economic Impact Assessment

The Agencies also seek comment on the following additional questions related to the potential economic impacts of the proposed framework for implementing section 13 of the BHC Act (i.e., the Volcker Rule):

Question 348. What are the expected costs and benefits of complying with the requirements of the proposed rule? We seek commenters' estimates of the aggregate cost or benefit that would be incurred or received by banking entities subject to section 13 of the BHC Act to comply. We also ask commenters to break out the costs or benefits of compliance to banking entities with each individual aspect of the proposed rule. Please provide an explanation of how cost or benefit estimates were derived. Please also identify any costs or benefits that would occur on a one time basis and costs that would recur. Would particular costs or benefits decrease or increase over time? If certain costs or benefits cannot be estimated, please discuss why such costs or benefits cannot be estimated.

Question 349. Please identify any costs or benefits that would occur on a one-time basis and costs or benefits that would recur (e.g., training and compliance monitoring). Please identify any costs or benefits that you believe would decrease over time. Please identify any costs or benefits that you believe may increase over time or remain static.

Question 350. Are there circumstances in which registered dealers, security-based swap dealers, and/or swap dealers (i) hold accounts other than trading accounts or (ii) hold investment positions for activities for which they are required to be registered? If so, would including all such dealer positions within the trading account definition create competitive burdens as well as additional burdens on the operations of such dealers that may not be consistent with the language and purpose of the statute? Please describe how this may occur, and to what extent it may occur.

Question 351. Please identify the ways, if any, that banking entities might alter the ways they currently conduct business as a result of the costs that could be incurred to comply with the requirements of the proposed rule. Do you anticipate that banking entities will terminate any services or products currently offered to clients, customers, or counterparties due to the proposed rule, if adopted? Please explain.

Question 352. How would trading systems and practices used in today's marketplace be impacted by the proposed rule? What would be the costs and/or benefits of such changes in trading practices and systems?

Question 353. Would the proposed rule create any additional implementation or operational costs or benefits associated with systems (including computer hardware and software), surveillance, procedural, recordkeeping, or personnel modifications, beyond those discussed in the above analysis? Would smaller banking entities be disproportionately impacted by any of these additional implementation or operational costs?

Question 354. We seek specific comments on the costs and benefits associated with systems changes on banking entities with respect to the proposed rule, including the type of systems changes necessary and quantification of costs associated with changing the systems, including both start-up and maintenance costs. We request comments on the types of jobs and staff that would be affected by systems modifications and training with respect to the proposed rule, the number of labor hours that would be required to accomplish these matters, and the compensation rates of these staff members.

Question 355. Please discuss any human resources costs associated with the proposed rule, along with any associated overhead costs.

Question 356. What are the benefits and costs associated with the requirements for relying on the underwriting exemption? What impact will these requirements have on capital formation, efficiency,

competition, liquidity, price efficiency, if any? Please estimate any resulting benefits and costs or discuss why such benefits and costs cannot be estimated. What alternatives, if any, may be more cost-effective while still being consistent with the purpose and language of the statute?

Question 357. What are the benefits and costs associated with the requirements for relying on the exemption for market making-related activity, including the requirement that such activity be consistent with the commentary in Appendix B? What impact will these requirements have on liquidity, price efficiency, capital formation, efficiency, and competition, if any? Please estimate any resulting benefits and costs or discuss why such benefits and costs cannot be estimated. What alternatives, if any, may be more cost-effective while still being consistent with the purpose and language of the statute?

Question 358. What are the benefits and costs associated with the requirements for relying on the exemption for risk-mitigating hedging activity, including the requirement that certain hedge transactions be documented? What impact will these requirements have on liquidity, price efficiency, capital formation, efficiency, and competition, if any? Please estimate any resulting benefits and costs or discuss why such benefits and costs cannot be estimated. What alternatives, if any, may be more cost-effective while still being consistent with the purpose and language of the statute?

Question 359. Are there traditional risk management activities of banking entities that are not covered by the liquidity management and risk-mitigating hedging exemptions as currently proposed? What risks do banking entities face that go beyond market, counterparty/credit, currency/foreign exchange, interest rate, and basis risk? Could the proposed construction of the liquidity management and risk-mitigating hedging exemptions increase the costs of management or impede the ability of banking entities to effectively manage risk?

Question 360. To rely on the exemptions from the proposed rule for permitted underwriting, market making-related activity, and risk-mitigating hedging, banking entities must establish, maintain, and enforce a compliance program, including written policies and procedures and internal controls. Please discuss how the costs incurred, or benefits received, by banking entities related to initial implementation and ongoing maintenance of the compliance program would impact their customers and their businesses with respect to underwriting, market making, and hedging activity.

Question 361. Please discuss benefits and costs related to the limitations on permitted activities for material conflicts of interest, high-risk assets and trading strategies, and threats to the safety and soundness of banking entities or to the financial stability of the U.S in the proposed rule. Are there particular benefits and costs related to the proposed definitions of material conflict of interest, high-risk asset, and high-risk trading strategy in the proposed rule? Would these definitions have any unintended costs, such as creating undue burdens and limitations on permitted underwriting, market making-related, or hedging activity? Please explain. What alternatives, if any, may be more cost-effective while still being consistent with the purpose and language of the statute?

Question 362. Please discuss the benefits and costs related to the definition of derivative in the proposed rule and the application of the restrictions on proprietary trading to transactions in the different types of derivatives covered by the definition. What alternatives, if any, may be more cost-effective while still being consistent with the purpose and language of the statute?

Question 363. What costs and benefits would be associated with calculating, reviewing, and analyzing the proposed quantitative measurements? What costs and benefits would be associated with reporting

the proposed quantitative measurements to an Agency? Please identify any of the proposed quantitative measurements that are already reported to an Agency and discuss whether the current reporting regime would mitigate costs associated with the proposed rule. With respect to any quantitative measurement that is not already reported to an Agency, what are the costs and benefits of beginning to report the measurement? Would banking entities have to create or purchase new systems or implement changes to existing systems in order to report these quantitative measurements? Please discuss the costs and benefits associated with such systems changes.

Question 364. How much of the data necessary to calculate the quantitative measurements in Appendix A is currently captured, retained, and utilized by banking entities? If the applicable data is not currently used by banking entities, is it readily available? Is it possible to collect all of the data that is necessary for calculating the required measurements? Please identify any data that banking entities do not currently utilize that would need to be captured and retained for purposes of proposed Appendix A and discuss the costs and benefits of capturing and retaining such data.

Question 365. Do the costs and benefits of calculating, analyzing, and reporting certain or all quantitative measurements differ between trading units and their trading activities, including trading strategies, asset classes, market structure, experience and market share, and market competitiveness? Are any quantitative measurements particularly costly to calculate or analyze for specific trading activities or, alternatively, particularly beneficial? If so, which quantitative measurement, what type of trading activity, and what factor(s) of that trading activity makes the quantitative measurement particularly costly or beneficial? Please discuss how these costs, if any, could be mitigated or benefits, if any, could be enhanced.

Question 366. The proposed definition of trading unit would require a tiered approach to calculating and reporting quantitative measurements, such that the measurements would be calculated and reported for different levels within the banking entity, with higher levels encompassing smaller units (e.g., trading desks, business lines, and all trading operations). What are the costs and benefits of calculating the quantitative measurements for each level within the definition of trading unit? Can the higher level calculations incorporate the lower level calculations such that the higher level calculations result in small, incremental costs? Why or why not? Are there particular costs or benefits associated with calculating, analyzing, and reporting a quantitative measurement at one of the levels within the definition of trading unit that would not be experienced at the other levels? Please explain. What are the costs, if any, of “noise,” “false positives,” or “false negatives” with respect to the quantitative measurements and calculations at different levels? Can these costs be mitigated and, if so, how? What alternatives, if any, may be more cost-effective while still being consistent with the purpose and language of the statute?

Question 367. We seek comment on whether the requirement that banking entities employ a suite of quantitative measurements may lead to redundancies and/or inefficiencies in the application of the measurements for some types of trading units within some banking entities. Despite the flexibility of Appendix A via recognition that quantitative measurements will be applied with respect to differences within a banking entity’s structure, business lines, and trading desks, we seek comment on whether the requirement of a mandatory suite of quantitative measurements may prove burdensome. For instance, is the application of certain quantitative measurements not efficient, appropriate, or calculable for certain asset classes or trading units or would the benefits of applying such quantitative measurements be negligible in relation to the costs of applying such measurements? In addition, would the overlay divert a banking entity from allocating resources toward quantitative – or other –

measurements that might prove more useful and better tailored to its specific and unique trading practices?

Question 368. What are the benefits and costs of the recordkeeping requirement in proposed Appendix A? Please explain and quantify, to the extent possible. To what extent would the proposed recordkeeping requirement impose new or additional costs and benefits beyond the current recordkeeping obligations of different types of banking entities (e.g., affiliated broker-dealers, affiliated investment advisers, insured depository institutions, etc.)? What alternatives, if any, may be more cost-effective while still being consistent with the purpose and language of the statute?

Question 369. Please identify any cost savings that would be achieved through the use of an enterprise-wide compliance program. Alternatively, would you expect certain costs to increase when using an enterprise-wide compliance program? Please explain. Please identify any benefits that might be amplified or reduced when using an enterprise-wide compliance program.

Question 370. Are there tools or elements in the contents of the compliance program set forth in § __.20(b) for which the costs may be negligible because banking entities use the same or similar elements for other purposes (e.g., satisfying other regulatory requirements, risk management, etc.) and could utilize existing infrastructure for purposes of the proposed rule? For example, could existing trader mandates or an existing training program be expanded to meet the requirements of the proposed rule, rather than developing an entirely new infrastructure? Alternatively, would the proposed rule require redundancies or duplications within a banking entity's infrastructure (e.g., the trader mandates currently used for one purpose do not conform to the requirements of the proposed rule, so a banking entity would have to utilize both in different circumstances)? Please identify and explain any such redundancies and how the rule could be modified to reduce or eliminate such redundancies, if possible.

Question 371. How would the proposed rule affect compliance costs (e.g., personnel or system changes) or benefits for each category of banking entity: small, medium, and large? Please discuss any differences between the costs and benefits of the compliance program required under § __.20(b) for smaller banking entities and the compliance program requirements of Appendix C for larger banking entities. Are the differences between these benefits and costs justified due to the differences in size and complexity of smaller and larger banking entities?

Question 372. The definition of trading unit in proposed Appendix C covers different levels of a banking entity and, as a result, requires a tiered approach to establishing, maintaining, and enforcing the compliance program requirements with respect to covered trading activities. What are the costs and benefits of applying the compliance program requirements at several levels within the banking entity? To what extent does the ability to incorporate written policies and procedures of lower-level units by reference, rather than establishing separate written policies and procedures, mitigate the costs of the proposed requirements? Are there other ways that the proposed requirements could be made more cost-effective for the different levels within the banking entity?

Question 373. How will the proposed definition of "covered fund" affect a banking entity's investment advisory activities, in particular activities and relationships with investment funds that would be treated as "covered funds"? Please estimate any resulting costs or benefits or discuss why such costs or benefits cannot be estimated.

Question 374. How have banking entities traditionally organized and offered covered funds? What are the benefits and costs associated with the proposed requirements for relying on the exception for organizing and offering covered funds? Please estimate any resulting costs or benefits or discuss why such costs or benefits cannot be estimated.

Question 375. What are the costs and benefits associated with the way the proposed rule implements the "customers of such services" requirement in the exception for organizing and offering covered funds? What alternative, if any, may be more cost-effective while still being consistent with the language and purpose of the statute?

Question 376. Is it common for a banking entity to share a name with the covered funds that it invests in or sponsors? If yes, what entity in the banking structure typically shares a name with such covered funds? What costs and benefits will result from the proposed rule's implementation of the name sharing requirement in exception for organizing and offering a covered fund? What alternatives, if any, may be more cost-effective while still being consistent with the purpose of the statute?

Question 377. Under what circumstances do directors and employees of a banking entity invest in covered funds? What are the benefits and costs associated with the proposed provisions regarding director and employee investments in covered funds? What alternatives, if any, may be more cost-effective while still being consistent with the purpose of the statute?

Question 378. Do banking entities currently invest in or sponsor SBICs and public welfare and qualified rehabilitation investments? If yes, to what extent? What are the benefits and costs associated with the proposed rule's implementation of the exception for investment in SBICs and public welfare and qualified rehabilitation investments?

Question 379. Do banking entities currently invest in or sponsor each of the vehicles that the proposed rule permits banking entities to continue to invest in and sponsor under section 12(d)(1)(J) of the BHC Act? If yes, to what extent? What are the benefits and costs associated with the proposed rule's implementation of these exceptions?

Question 380. For banking entities that are affiliated investment advisers, are there additional costs or benefits to complying with section 13 of the BHC Act and the proposed rule? For example, do affiliated investment advisers typically maintain records that would enable them to demonstrate compliance with the 3% ownership limits or restrictions on transactions that would be subject to sections 23A and 23B of the FR Act?

Question 381. Would complying with section 13 of the BHC Act and the proposed rule affect an affiliated investment adviser's other business activities (benefit or burden) that are not subject to restrictions on proprietary trading or other covered fund activities? For example, would advisers incur additional burdens to distinguish covered fund activities from non-covered fund activities?

Question 382. For banking entities that are affiliated investment advisers, are there particular costs or benefits to complying with the portions of Appendix C that are applicable to each asset management unit of the adviser? Do these costs and benefits differ depending on whether the adviser complies with Appendix C individually or on an enterprise basis? Does the rule provide sufficient clarify for how Appendix C applies to unregistered affiliates of an affiliated investment adviser?

Question 383. To the extent applicable, please address each of the questions above with respect to securitization vehicles that would be included in the proposed definition of covered fund.

Paperwork Reduction Act Analysis/Request for Comment on Proposed Information Collection

This is a relatively obscure area included in all federal rules and is generally overlooked by commenters during the comment process. However, given the compliance provisions set forth in the proposed rule, it is worthwhile highlighting the following questions on which the Agencies invite comment:

(a) Whether the collections of information are necessary for the proper performance of the Agencies' functions, including whether the information has practical utility;

(b) The accuracy of the estimates of the burden of the information collections, including the validity of the methodology and assumptions used;

(c) Ways to enhance the quality, utility, and clarity of the information to be collected;

(d) Ways to minimize the burden of the information collections on respondents, including through the use of automated collection techniques or other forms of information technology; and

(e) Estimates of capital or start up costs and costs of operation, maintenance, and purchase of services to provide information.

SEC Additional Matters – Statutory Authority and "Covered Banking Entity" Definition

The SEC requests comment on the proposed definition of "covered banking entity," and particularly on the following:

Question SEC-1. Is the SEC's proposed definition of the term "covered banking entity" sufficiently clear? If not, why not? Please suggest an alternative definition.

Question SEC-2. Is the SEC's proposed definition of the term covered banking entity appropriate, or is it over- or under-inclusive? Please explain.

Question SEC-3. Should any of the covered banking entities included in the SEC's proposed definition of "covered banking entity" be excluded? If so, which entities, why, and on what basis? Should the SEC's proposed rule provide specific guidance or exemptions for any such entities?

Question SEC-4. Would particular types of entities incur costs or burdens that are greater than other types of entities that are included in the SEC's proposed definition of "covered banking entity"? If so, should any such difference be addressed or mitigated? How?

Question SEC-4.[1] Are all of the provisions in the proposed rule relevant to the business conducted by SEC covered banking entities? If not, which provisions are not relevant and how should this be addressed in the rule? Are there differences between the SEC's covered banking entities and other types of banking entities subject to the rules of the Federal banking agencies or the CFTC that have not been sufficiently accounted for in the proposed rule? If so, what are these differences and how

[1] The proposed rule includes two items referenced as "Question SEC-4."

should the SEC's rule account for such differences in a manner that is consistent with the statutory requirement that the Agencies' rules be consistent and comparable, to the extent possible?

The SEC requests comment on the applicability of the proposed rule to registered advisers with respect to the covered fund restrictions set forth in the proposal, and particularly requests comment on the following:

Question SEC-5. Should the SEC instead require registered advisers to comply with the covered fund restrictions proposed by the SEC, instead of those issued the appropriate Federal banking agency? If so, could this create incentives to move the advisory business between the registered adviser and its affiliated bank? Are there benefits to this alternate approach? If so, please explain.

Question SEC-6. Are there other alternative approaches to the proposed rule that would be more effective? If yes, what alternatives and why?

Question SEC-7. Would registered advisers affiliated with insured depository institutions benefit from the proposed approach? Why or why not?

Question SEC-8. Would a registered adviser that is affiliated with insured depository institutions that are regulated by multiple Federal banking agencies encounter additional burdens in implementing the proposed approach? With respect to these registered advisers, which Federal banking agency's rules should be applicable to the registered adviser? For example, should the registered adviser be subject to the rules applicable to the registered adviser's immediate parent that is an insured depository institution?

Question SEC-9. Is the proposed requirement that registered advisers comply with the covered fund restrictions in § __.20 issued by the Federal banking agency that regulates the banking entity specified in § __.2(e)(1), (2) and (3) of the proposed rule with which the registered adviser is affiliated sufficiently clear? Are there particular compliance program requirements in § __.20 with respect to the covered fund restrictions that overlap with the proprietary trading restrictions, such that it would be difficult to identify which requirements are related to the covered fund restrictions and which requirements are related to the proprietary trading restrictions? If so, which requirements and how should this overlap be addressed? Should registered advisers be required to comply with § __.20 of the SEC's rule in its entirety? Why or why not?

Question SEC-10. Will the SEC's proposed approach limit the potential for inconsistent application of the proposed rules with respect to affiliates of entities specified in §__.2(e)(1), (2) and (3)? Why or why not?

Question SEC-11. Will the SEC's proposed approach be effective in avoiding the creation of incentives for covered fund activities to move from a registered adviser to a bank? Why or why not?