

MEMO# 25741

December 23, 2011

Draft ICI Letter on "Volcker Rule" Proposal Focuses on Unintended Effects for Registered Funds, Impact on Financial Markets; Your Comments Due Jan. 6th

URGENT/ACTION REQUESTED

[25741]

December 23, 2011

TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 55-11
DERIVATIVES MARKETS ADVISORY COMMITTEE No. 51-11
ETF (EXCHANGE-TRADED FUNDS) COMMITTEE No. 50-11
ETF ADVISORY COMMITTEE No. 70-11
EQUITY MARKETS ADVISORY COMMITTEE No. 67-11
FIXED-INCOME ADVISORY COMMITTEE No. 80-11
INTERNATIONAL COMMITTEE No. 27-11
MONEY MARKET FUNDS ADVISORY COMMITTEE No. 69-11
MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 60-11
SEC RULES COMMITTEE No. 108-11
SMALL FUNDS COMMITTEE No. 57-11 RE: DRAFT ICI LETTER ON "VOLCKER RULE" PROPOSAL
FOCUSES ON UNINTENDED EFFECTS FOR REGISTERED FUNDS, IMPACT ON FINANCIAL
MARKETS; YOUR COMMENTS DUE JAN. 6TH

As we previously indicated, the Securities and Exchange Commission, Federal Reserve Board, Office of the Comptroller of the Currency, and Federal Deposit Insurance Corporation (the "Agencies") jointly issued a proposal to implement Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, commonly known as the "Volcker Rule." [\[1\]](#) The proposal is lengthy and complex, with wide-ranging implications. ICI has prepared a draft comment letter, which is attached and briefly summarized below.

Comments on the proposal are due to the Agencies by January 13, 2012. [\[2\]](#) Please provide comments on the draft letter by Friday, January 6, 2012 directly to the person(s) responsible for each section, as indicated in the outline below.

Please note (with our apologies) that this draft is somewhat rough. By necessity, different people have drafted different parts of our letter. We will be continuing to work on and polish the draft—including to achieve consistent style, formatting, terminology, etc. throughout—but we felt it was important to give members an opportunity as soon as possible to review it and provide feedback, including letting us know if there are any issues we have missed. There are also several places in the letter where we pose questions for, or request specific information from, members.

Background

The Volcker Rule generally contains two prohibitions. First, it prohibits “banking entities” from engaging in proprietary trading of any security, derivative, and certain other financial instruments for its own account, subject to certain exemptions. Second, it prohibits banking entities from acquiring or retaining an ownership interest in, or sponsoring or having certain relationships with a hedge fund, private equity fund, or “similar fund,” subject to certain exemptions. The proposal sets forth detailed rules to implement these two broad prohibitions. The proposal also contains numerous exemptions to the Rule, as well as several appendices related to recordkeeping and reporting requirements, detailed guidance regarding trading undertaken in connection with market making activities (one of the exempted “permitted activities”), and enhanced compliance requirements for banking entities with significant trading or “covered fund” activities. In addition, the proposal defines a number of key terms.

Summary of Comments

Our comments generally fall into two categories: (1) comments related to the impact of the proposal on registered investment companies as investors; and (2) comments related to the application of the proposal to the organization or operation of registered investment companies.

I. Impact of the Proposed Rule on Markets, Market Participants, and Financial Instruments

- A. Impact of the proprietary trading prohibition on market liquidity [Ari Burstein – aburstein@ici.org]
- B. Issues affecting registered funds that invest in certain foreign securities [Frances Stadler – frances@ici.org]
- C. Impact of the proposed rule on notes issued by asset-backed commercial paper (“ABCP”) programs and securities issued pursuant to municipal tender option bond (“TOB”) programs [Jane Heinrichs – jheinrichs@ici.org]

II. Application of the Proposed Rule to Registered Funds

- A. The definition of “banking entity” should specifically exclude registered funds [Frances Stadler – frances@ici.org]
- B. The definition of “covered fund” should specifically exclude registered funds [Rachel Graham – rgraham@ici.org]

C. Impact of the proposed rule on ETFs [this section of the draft letter will be circulated separately]

D. Potential issue for fund complexes with one or more banking entities – Incubator funds [Frances Stadler – frances@ici.org]

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General Counsel

[Attachment](#)

endnotes

[1] See ICI [Memorandum](#) No. 25634 (November 10, 2010). The proposal is available on the SEC's website at <http://www.sec.gov/rules/proposed/2011/34-65545.pdf>. The Dodd-Frank Act requires coordinated rulemaking by the Agencies as well as by the Commodity Futures Trading Commission. The CFTC has not yet issued its proposal, but is expected to do so in the near future.

[2] Today, ICI filed a letter seeking an extension of the comment deadline. A copy of that letter is attached. The letter notes that several organizations have requested that the Agencies extend the comment deadline to the later of 90 days after the current deadline of January 13th or 60 days after the CFTC releases its proposed rules. It indicates that such an extension would allow ICI sufficient time to fully develop our comments and vet them with members in order to provide a thorough and meaningful response to the Agencies. There is no assurance that the Agencies will grant this request.

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