September 21, 2017

*Via Electronic Filing (regs.comments@occ.treas.gov)*

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street SW, Suite 3E-218
Washington, DC 20219

**Re: Volcker Rule; Request for Information**

Ladies and Gentlemen:

The Investment Adviser Association[1] (**IAA**) appreciates the opportunity to comment on the Office of the Comptroller of the Currency's (**OCC's**) request for public comment[2] on how the regulations implementing the Volcker Rule statute[3] should be revised to better accomplish the purposes of the Statute and on improvements to the administration of these regulations by the five Volcker Agencies.[4] The OCC anticipates that the comments it receives will also inform the other Volcker Agencies' consideration of the Volcker Regulations.

The IAA believes that the Volcker Regulations go far beyond the purpose and intent of the Statute, unnecessarily constraining the activities of banks and their affiliates, including many of our investment adviser members. In this regard, we support the comments of the Securities Industry and Financial Markets Association (**SIFMA**) as they relate to asset management, including their comments on the breadth, complexity, and prescriptive nature of the Volcker Regulations generally, and on the definitions of "trading account" and "covered funds" more

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[1] The IAA is a not-for-profit association that represents the interests of investment adviser firms registered with the Securities and Exchange Commission (**SEC**). The IAA has more than 600 member firms that collectively manage approximately $20 trillion for a wide variety of individual and institutional investors, including pension plans, trusts, investment companies, private funds, endowments, foundations, and corporations. For more information, please visit www.investmentadviser.org.

[2] Proprietary Trading and Certain Interests in and Relationships With Covered Funds; Request for Public Input, 82 Fed. Reg. 36,692 (Aug. 7, 2017). Docket ID OCC-2017-0014.

[3] Section 13 of the Bank Holding Company Act of 1956 (12 U.S.C. 1851) (**Statute**); Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds, 79 Fed. Reg. 5,536 (Jan. 31, 2014); and Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds, 79 Fed. Reg. 5,808 (Jan. 31, 2014) (**Volcker Regulations**).

[4] The Volcker Agencies are the Board of Governors of the Federal Reserve System (**Board**), the Commodity Futures Trading Commission (**CFTC**), the Federal Deposit Insurance Corporation (**FDIC**), the OCC, and the SEC.

specifically. Our comments, however, focus on and make recommendations with respect to four specific issues that directly affect investment advisers. Specifically, we recommend:

1. Excluding from prohibited proprietary trading transactions entered into for the purpose of developing products or services for asset management clients;

2. Excluding registered investment companies (**RICs**) from the definition of "banking entity" regardless of the percentage of ownership interest in the RIC by a banking entity;

3. Excluding all foreign funds from both the "covered fund" and "banking entity" definitions; and

4. Eliminating the prohibition on name-sharing in the asset-management exemption from covered fund restrictions, or, at a minimum, modifying the prohibition to allow name-sharing with a separately-branded adviser.

We discuss each of these below.

**Discussion**

***1. Transactions in financial instruments entered into by a banking entity for purposes of developing new products or services for asset management clients should be excluded from the definition of "proprietary trading" or alternatively be permitted as trading on behalf of customers.***

The Statute defines "proprietary trading" as engaging as principal for the "trading account" of the banking entity. "Trading account" is defined as acquiring or taking positions in financial instruments principally for purposes of short-term resale.[5] Recognizing that they do not raise short-term speculative trading risks, the Volcker Regulations exclude certain types of transactions from the definition of "proprietary trading." All other transactions that fall within the Volcker Regulations' extremely broad definition of "trading account," however, are presumptively prohibited proprietary trading. For a banking entity to continue to engage in these transactions, it must rely on one of the narrow permitted activity exemptions under the Volcker Regulations.

Registered investment advisers routinely invest their own money in a seed account to develop and test new strategies. The seed account is not used to generate short-term profits. Instead, it is generally used to work through a strategy, test its viability, develop a performance track record, and ascertain the strategy's suitability for different types of investors under

[5] 12 U.S.C. §§ 1851(h)(4) and (6).

different market conditions. Yet, while the Volcker Regulations permit a banking entity to seed a RIC or a private fund, they do not permit the seeding of a strategy and thus prohibit a bank-affiliated adviser from using its own funds this way. And because these investments do not qualify as permitted market making, risk-mitigating hedging, or trading on behalf of customers, an exemption from prohibited proprietary trading is not available. Bank-affiliated advisers must therefore use client funds to develop and test new strategies, or not develop and test them at all. Investors and the markets are both better served by encouraging this strategy development activity and allowing advisers to undertake this activity with their own, rather than with client, funds, and without having to set up separate legal entities to do so.

Because this type of activity is not principally for the purpose of short-term trading, we recommend that it be excluded from the definition of "proprietary trading."

Alternatively, we recommend that the exemption in the Volcker Regulations for trading on behalf of customers,[6] which is currently drawn unworkably narrowly, be revised to include transactions in financial instruments that a banking entity or its affiliates may enter into with a registered investment adviser affiliate for purposes of developing, testing, or delivering products or services to asset management clients.

2. ***Registered investment companies should be excluded from the definition of "banking entity" regardless of the percentage of seed ownership by a banking entity.***

Although Congress clearly never intended that RICs should be covered by the Statute – and there has been no suggestion that RICs raise any of the concerns the Statute was intended to address – RICs may nonetheless be captured under the Volcker Regulations. A RIC will be considered a banking entity, and therefore itself subject to the Volcker Rule's prohibitions and restrictions, if a banking entity owns, controls, or has the power to vote 25 percent or more of the RIC's voting shares, or if the banking entity provides investment advisory, commodity trading advisory, administrative, and other services to the company or fund other than in compliance with other limitations under applicable regulation, order, or other authority.[7]

The preamble to the Volcker Regulations makes clear that a seeding vehicle that will become a RIC would be permissible during the seeding period as long as the banking entity that establishes the seeding vehicle operates it under a written plan that reflects a determination that the vehicle will become a RIC by the end of the seeding period.[8] However, the seeding period

[6] 12 C.F.R. § 44.6(c).

[7] 12 CFR § 44.12(b)(1)(ii).

[8] *See* 79 Fed. Reg. at 5,676-77. Volcker FAQ No. 16, Seeding Period Treatment for Registered Investment Companies and Foreign Public Funds, *available at* https://www.occ.treas.gov/topics/capital-markets/financial-

permitted under the Volcker Regulations is exceedingly short. Moreover, a banking entity may end up owning more than 25 percent of a RIC after the end of the seeding period even if it is below that threshold at the end of that period. For example, a bank affiliate may own less than 25 percent of a fund that liquidates after the seeding period. As part of the liquidation, it may be necessary for the bank to wait to liquidate its shares until other investors have liquidated theirs, resulting in the bank holding more than 25 percent.

The Volcker Agencies have noted that the Statute reflects "an intention not to disrupt registered investment companies, such as U.S. mutual funds."[9] Consistent with this intent, we recommend that the Volcker Regulations be revised to make clear that RICs will not be considered to be banking entities at any time, regardless of the percentage of ownership by a banking entity or if the banking entity provides investment advisory, commodity trading advisory, administrative, and other services to the RIC in accordance with applicable regulations.

***3. Foreign funds, whether public or private, should not be considered either covered funds or banking entities.***

The Volcker Regulations' treatment of foreign public funds is extraordinarily complex, imposing a significant compliance burden on banking entities to determine whether a fund is covered.[10] In addition, many of the conditions of the foreign public fund exclusion from the definition of "covered fund" are simply not practical. For example, banking entities may not be able to confirm that a foreign public fund meets the condition that shares be sold predominantly through public offerings outside of the United States. We recommend that the Volcker Regulations be revised to provide a clear exclusion from the "covered fund" definition for non-U.S. public funds.

For the reasons discussed above in connection with RICs, we also recommend that the Volcker Regulations make clear that foreign public funds are not banking entities, regardless of the percentage of banking entity ownership.

The Volcker Regulations should also codify the recent no-action relief provided to foreign private funds that are not covered funds from the definition of "banking entity" based on

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markets/trading-volcker-rule/volcker-rule-implementation-faqs.html, provides additional relief to RICs during the seeding period.

[9] *See* Volcker FAQ No. 14, How does the final rule apply to a foreign public fund sponsored by a banking entity?, *available at* https://www.occ.treas.gov/topics/capital-markets/financial-markets/trading-volcker-rule/volcker-rule-implementation-faqs.html.

[10] 12 CFR § 44.10(c)(1). *See also* Volcker FAQ No. 2, Foreign Public Fund Seeding Vehicles, *available at* https://www.occ.treas.gov/topics/capital-markets/financial-markets/trading-volcker-rule/volcker-rule-implementation-faqs.html; Volcker FAQ No. 16, *supra,* note 8.

a foreign bank's control of such funds through ownership or other relevant control factors.[11] Forcing a foreign private fund to be subject to the Volcker Rule's trading and investment prohibitions and restrictions would substantially harm the fund's ability to invest on behalf of its shareholders. The Volcker Agencies recognized this illogical result when they excluded covered funds from the definition of "banking entity." They should similarly permanently exclude foreign private funds.

4. ***The name-sharing prohibition under the asset management exemption from the covered fund restrictions should be eliminated, or at a minimum should be permitted for separately-branded asset managers.***

The "asset management exemption" in the Volcker Regulations provides that a banking entity may sponsor a covered fund subject to a number of conditions, including that the covered fund "does not share the same name or a variation of the same name with the banking entity (or an affiliate thereof)."[12] According to the Volcker Agencies, the prohibition on name-sharing is intended to prevent "customer confusion regarding the relationship between the banking entity and the covered fund," and also not "mislead an investor into thinking that the banking entity or any of its affiliates, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of the covered fund or any covered fund in which such covered fund invests."[13] The overly restrictive and costly name-sharing prohibition does not achieve either of these goals.

To comply with the prohibition, many of our members that are investment adviser affiliates of banking entities have changed the names of funds they sponsor to remove not only the name of their banking entity parent organization, but also their own name (since the prohibition extends to names of affiliates), even when that name has no similarity to the banking entity's name. This change has not only been extremely costly, but has confused investors, who are no longer easily able to associate the fund name with the sponsoring asset manager. The change has been confusing in other respects as well. For example, we understand that certain tax authorities have been puzzled by filings by existing funds with new names.

In addition, to the extent that the name-sharing prohibition is intended to address "bailout" risk, it is entirely unnecessary. First, the exemption expressly prohibits a banking entity and its affiliates from directly or indirectly guaranteeing, assuming, or otherwise insuring the obligations or performance of the fund, thus prohibiting the banking entity from bailing out a covered fund.[14] Second, the asset management exemption is designed to ensure that investors

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[11] Board, FDIC, OCC, Statement regarding Treatment of Certain Foreign Funds under the Rules Implementing Section 13 of the Bank Holding Company Act (Jul. 21, 2017), *available at* https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20170721a1.pdf.

[12] 12 C.F.R. § 44.11(a)(6)(i).

[13] Volcker FAQ No. 5, Namesharing Prohibition, *available at* https://www.occ.treas.gov/topics/capital-markets/financial-markets/trading-volcker-rule/volcker-rule-implementation-faqs.html.

[14] 12 C.F.R. § 44.11(a)(8)(i).

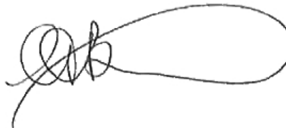
understand that there will be no bailout. It requires clear and conspicuous written disclosure to actual and prospective investors: (i) that all losses in the fund will be borne solely by investors and not by the banking entity; (ii) that ownership interests in the fund are not FDIC-insured and are not deposits, obligations of, or endorsed or guaranteed in any way by any banking entity; and (iii) of the role and services of the banking entity and its affiliates with respect to the fund.[15] Prohibiting an asset manager-sponsored fund from sharing a name with a banking entity or a banking entity affiliate does not meaningfully further reduce the bailout risk but it does add enormous additional costs to the sponsoring asset manager.

We therefore recommend that the name-sharing prohibition in the asset management exemption be eliminated.[16] Alternatively, we ask that the name-sharing prohibition be modified to allow name sharing with a separately-branded asset manager whose name has no similarity to the name of the insured depository institution or its holding company.

## Conclusion

We appreciate the opportunity to provide comments on this important issue. Please do not hesitate to contact the undersigned at (202) 293-4222 if we can be of further assistance during your review of the Volcker Regulations.

Respectfully,



Gail C. Bernstein
General Counsel
Investment Adviser Association

cc: Honorable Jay Clayton, Kara M. Stein and Michael S. Piwowar, Chairman and Commissioners, Securities and Exchange Commission
Dalia Blass, Director, Division of Investment Management, Securities and Exchange Commission

[15] 12 C.F.R. § 44.11(a)(5).

[16] The Volcker Agencies could use the authority granted to them in subsection (d)(1)(J) of the Statute to effect this change.