ALLIANCEBERNSTEIN

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By electronic submission

Federal Deposit Insurance Corporation
550 17th Street, NW.
Washington, DC 20429

Securities and Exchange Commission
100 F Street, NE.
Washington DC 20549

Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, NW.
Washington, DC 20551

Department of the Treasury
Office of the Comptroller of the Currency
250 E Street, SW.
Washington, DC 20219

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

Dear Madames/Sirs:

AllianceBernstein L.P. ("AllianceBernstein") is a global asset management firm with approximately $424 billion in assets under management as of October 31, 2011. AllianceBernstein provides investment management services to both institutional and individual investors through a broad line of investment products. AllianceBernstein is a major mutual fund and institutional money manager and our clients include, among others, state and local government pension funds, universities, 401(k) plans, and similar types of retirement funds and private funds. The investors we serve include savers, pension beneficiaries, mutual fund investors and other "main street" stakeholders.

AllianceBernstein recognizes and supports the effort of the Office of the Comptroller of the Currency, Treasury ("OCC"); Board of Governors of the Federal Reserve System ("Board"); Federal Deposit Insurance Corporation ("FDIC"); and Securities and Exchange Commission ("SEC") (collectively the "Agencies") to

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promulgate appropriate rules (the "Proposal") to implement Section 619 of the Dodd–Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). We appreciate having the opportunity to comment on the Proposal and, as described in more detail below, believe that significant changes to the approach taken by the Agencies are necessary, particularly with respect to the provisions effectuating the market making exemption contained in the Dodd-Frank Act.

Market making is a core function of banking entities and provides liquidity needed by all market participants, including the pension funds, endowments and individual investors that are our investment management clients. We believe it is crucial that the steps mandated by the Dodd-Frank Act be implemented in a manner that does not disrupt the liquidity necessary for functioning securities markets and impose potentially prohibitive costs and burdens on market participants.

Market Making: Necessary and Vital for Functioning Markets

Market makers transact with investors at a price that reflects the general risk of the security, including (i) the perceived demand from buyer's of the security, (ii) the cost to carry the security if it had to be held until a buyer is found, (iii) the general credit risk and price volatility of the security, and (iv) the incremental impact that the market makers position would have on its liquidity, overall risk positions, and expected return on the capital required to hold the security. In short, the market maker is required to evaluate all risks in purchasing the security which would inure to an owner of the risk.

The simplest of market making activities involve exchange traded securities. Over time and with the help of improved regulation, liquidity in this market has vastly improved and transaction costs have declined significantly, largely because the buyers and sellers of an issuer's equity always transact in a fungible unit representing ownership of an issuer (the issuer's common stock). The homogeneity of the equity structure helps to ensure there is a steady stream of liquidity for the majority of issues being traded[1]. Accordingly market makers can reasonably expect in most cases to be able to quickly dispose of securities purchased in these markets.

Other markets, however, are more complex and less liquid. In the fixed income market, for example, each issuer typically has multiple securities trading in the market and each individual issue is vastly smaller than the related equity capitalization of the issuer. In other words, unlike equities there is no single, homogenous, tradable unit of credit risk for an issuer and as a result there is fragmentation and intermittent liquidity for any single issue. By definition it is much harder for these transactions to find liquidity, and it is the responsibility of market makers to bridge the gap between buyers and sellers and provide the immediate liquidity necessary for these markets to function.

If banking entity market makers are essentially prohibited from holding inventory due to the Proposal, this will be reflected in both the ability of the market makers to

[1] This does not necessarily apply to block-sized trades, where there may be liquidity constraints and the corresponding need for market makers to take principal positions.

provide liquidity and transactions costs. The uncertainty created will also increase volatility since in markets when uncertainty rises, the search and demand for liquidity at the lowest possible transaction price still occurs but at the expense of price volatility.

The Impact of the Proposal on Market Making Activities

While Section 619 of the Dodd-Frank Act generally prohibits any "covered banking entity" from engaging in "proprietary trading," there are certain statutory exceptions. The legislation specifically provides an exemption for *"The purchase, sale, acquisition, or disposition of securities and other instruments . . . . . in connection with underwriting or market-making-related activities . . . . . ".*

Rather than acknowledge this tenet and setting forth broadly applicable standards to govern permitted market making activities, the Proposal creates a presumption that any covered financial position[2] that a covered banking entity holds for a period of sixty days or less is a prohibited proprietary transaction. While the presumption is "rebuttable" we respectfully submit that the framework for rebutting the presumption contained in the Proposal and accompanying documentation is unworkable for a number of reasons, including: (i) an inability to predict the financial impact of market making activities (a) for purposes of complying with the metrics set forth in the Proposal and (b) due to the acceleration of market instability caused by limitations on price discovery in periods of rising market volatility, where banking entity market makers could otherwise have provided liquidity; (ii) the general erosion of investor confidence by limiting price discovery in periods of rising market volatility, again where market makers could otherwise provide liquidity; (iii) the failure of the Proposal to identify and account for different types of market making environments, particularly those related to the fixed income markets and other OTC markets; (iv) the creation of perverse incentives through mandates on how compensation is calculated; and (v) the onerous and potentially contentious compliance mandates that could encourage covered banking entities to abandon less liquid and more volatile segments of various markets.

With respect to (ii) above, we believe that the Proposal was drafted solely from the perspective of regulated market making activities in organized markets where intermediaries generally act as agents, such as those for listed securities, with the exception of block trades, which also require market makers to commit capital and hold positions. The description of market making activities set forth in the Proposal clearly do not take into account unregulated over-the-counter market making activities that covered banking entities provide to these markets, which require intermediaries to regularly trade as principal due to the high degree of fragmentation and intermittent liquidity of said markets[3] or where market makers provide capital as a principal for listed securities.

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[2] A "covered financial position" is any of the list of securities listed in Subpart B, Section __.3, which includes a security, derivative, commodity futures contract, or an option on any of the preceding, but does not include any loan, or direct purchase or sale of a commodity or foreign currency.

[3] The release specifically states at page 56 that "*The language used in § __.4(b)(2)(ii) of the proposed rule to describe bona fide market making-related activity is similar to the definition of "market maker" under section 3(a)(38) of the Exchange Act. The Agencies have proposed to use similar language because the Exchange Act definition is*

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While our comments reflect our view as to the application of the Proposal to all markets, one of our greatest concerns is the devastating effect that the Proposal would have on the fixed income markets that exhibit intermittent liquidity and thus require market makers to act as principal in order to ensure liquidity or for that matter any market where rising and spiking uncertainty requires market makers taking principal positions to provide capital to insure normal liquidity. We respectfully submit that the failure to take into account over-the-counter market making activities reflects a major oversight and must be addressed in the final analysis and rulemaking. The final rules must take into account other scenarios when committing capital is essential to ensuring normal markets prevail.

The ability of corporate issuers to place their debt securities in the US capital markets is fundamentally dependent on the availability of adequate secondary market liquidity for these securities. Purchasers of these securities, including large pension funds, mutual funds, insurance companies and college and other endowments, and their investment managers, are willing to purchase these securities only because of adequate secondary market liquidity (so that they can meet their ongoing cash needs) which depends in large part on the market making activities of banking entities. We believe that any significant reduction in liquidity provided by market makers will, until another source of liquidity develops, have a dramatic adverse effect on the ability of corporate issuers to access needed funds in the US capital markets. We are convinced that the Proposal will in fact significantly reduce the liquidity of the secondary market for debt securities and is likely to have a profound and unintended adverse effect on our capital markets.

In summary, we believe that the inability to confidently engage in market making activities on a principal basis under the Proposal, along with the onerous recordkeeping and compliance burdens required will have a material and detrimental impact on the ability of covered banking entities to engage in market making activity. The Proposal, as drafted, will likely dramatically reduce market liquidity, increase costs and in some cases impact the ability of market participants to meet their legally required obligations to investors and other stakeholders. The net effect of this will be to reduce returns to savers, increase transaction costs, and increase the risk of investments by reducing liquidity to savers.

A more detailed explanation of some of our concerns is set forth below.

Holding Period

The Proposal generally prohibits a covered banking entity from acting as principal in the purchase or sale of a covered financial position for its own trading account. As noted above, the Proposal creates a presumption that any account that holds a covered financial position for a period of sixty days or less is a trading account

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generally well-understood by market participants and is consistent with the scope of bona fide market making-related activities in which banking entities typically engage"

and thus such transaction is presumptively prohibited. The Proposal allows this presumption to be rebutted if the covered banking entity can demonstrate that the position was not acquired principally for any of the purposes list in Subpart B, Section __.3(b)(2)(i)(A). We submit that the combination of this negative presumption combined with rebuttals that may be difficult (if not impossible) to demonstrate, will provide a strong incentive to covered banking entities to dispose of each and every position as quickly as possible in order to avoid any taint that could result in the transaction being considered a prohibited proprietary transaction.

As a result, banking entity market makers are going to be reluctant to make a market in any securities they are not reasonably confident they can dispose of immediately. Since the market maker is disincentivized from holding a security, it must charge a fee that is commensurate with the inherent risk of the position, particularly the risk associated with having to quickly dispose of it. The fee will be of necessity greater than current levels, as banking entity market makers' can no longer rely on mitigating the risk and cost associated with committing capital on behalf of clients by holding positions. Additionally, since the possibility of holding the security until natural buyer demand is located is not viable, the market maker must charge an additional amount compensate for the pricing risk involved with finding immediate buyer interest.

On top of this, the market maker employee is incentivized under the Proposal to maximize the fee charged on individual transactions without concern for the underlying profitability of the trade as their personal compensation depends solely on the amount of the spread and fees earned. From a market making and client facing perspective, this is a perverse arrangement that will further inflate spreads and in some cases dissuade the market maker from providing liquidity at all.

Competition among market makers will certainly provide some respite for the sellers, but all banking entity marker makers will share the same constraints, competitive aspirations and compensation objectives. The banking entity market makers possessing strong distribution systems will be able to charge more to sellers, since they have distribution strength and can only commercialize that strength by increasing the spread or fees charged, which are to be the sole economic drivers for these market makers.

The final rules must take into account the fact that market making often involves the need to take short-term positions that will result in profit and loss. This activity is distinguishable from proprietary trading activity and is the natural economic result flowing from the willingness of the market maker to commit capital to facilitate orderly trading. Moreover, this is a necessary requirement for functioning markets.

Hedging

The market making exemption in the Proposal appears to be predicated on the incorrect assumption that there is a perfect hedge for all securities and that all risks can be hedged for any given holding period for any position. The Proposal relies heavily on

the use of hedging as a means of enabling market makers to offset the risks associated with taking short term positions, and perhaps more importantly in the context of compliance with the Proposal, avoiding realized profits or losses in connection with positions held by a banking entity market maker. The Proposal ignores the fact that there are not perfect hedges for all securities. Certainly there are segments of fixed income markets and OTC markets where such hedges do not exist or markets where even the best structured hedges fail to protect the hedging party fully. It is impossible to predict what the behavior of even the most highly correlated hedge will be versus the underlying asset being hedged. In general, the realization of some profit and loss is unavoidable even when a market maker commits capital to facilitate orderly trading of liquid securities with properly structured hedges. Also, as is the case with all of the requirements of the Proposal, each trade is looked at individually, which multiplies the probability that a covered banking entity is deemed to have engaged in a prohibited activity. Also, hedging transactions involve a cost which the market makers will pass on to their customers. This will only add to the additional expense borne by investors as a result of the Proposal.

Given these facts, and the emphasis the Proposal places on avoiding profit or loss on positions taken by market makers, intermediaries are not going to be able to place great confidence in the use of hedging as a means of staying within the exemption.

Compliance Costs and Burdens

As noted previously, the Proposal starts with the presumption that taking a position for a period of sixty days or less is a prohibited proprietary transaction. While the market-making exemption provides a mechanism for rebutting this presumption, this involves analyzing the market making activity of a covered banking entity on almost a transaction by transaction basis. Not only would the compliance program, tasked with preventing prohibited proprietary trading, be extremely complex, onerous, and require a significant build-out of resources, manpower and systems, but the process would be vulnerable to hindsight interpretations that fail to capture or downplay important facts and color that justified the trade at time of execution.

The operational burdens and costs associated with this process are going to be magnified by the costs involved in providing the new reports and tracking the information that the covered banking entities are required to provide. The compliance process will also require numerous performance and profit/loss calculations in order to track the many metrics enumerated in the Proposal. Additionally, given the presumption created by the Proposal, there is a risk, given the dynamics of a particular firm, that the compliance process could become a contentious and adversarial process with compliance focused on generating reasons why a transaction should be classified as prohibited activity.

Impact on Open End Mutual Funds

As of year-end 2010, mutual funds accounted for approximately 22 percent of household financial assets in the US. The liquidity needs of open end mutual funds are largely driven by the need to respond to both redemptions and subscriptions. Section 22(e) of Investment Company Act of 1940 requires open end funds to meet redemptions requests within seven days and limit the ability of open end funds to borrow money to fund redemptions. Effectively, during a period of material redemptions a fund is a forced seller of securities and during a period of heavy inflows a fund is more or less a forced buyer.

Currently mutual funds can rely on intermediaries to commit capital and facilitate an orderly market. This not only benefits funds and their managers, but it ultimately benefits the millions of small investors that are served by the mutual fund industry. Implementation of the Proposal will immediately convert a significant number of these intermediaries from market makers, in the sense we see them now, to themselves being forced sellers or buyers of securities they are still willing to make markets in. Not only will this immediately impact funds in terms of higher trading costs and reduced liquidity, but in fixed income and other markets the value of the securities traded will be reduced due to long term uncertainty about the availability of liquidity. Also, in periods of significant financial system stress, liquidity could be so limited that many fixed income mutual funds could be forced to suspend redemptions, which would have a severe adverse effect on mutual fund shareholders and contribute greatly to systemic financial system risk.

"High Risk" Assets

The Proposal prohibits any transaction that results in material exposure to "high-risk assets." Section __.8(c)(1) defines a "high-risk asset" as an asset or group of assets that would, if held by the covered banking entity, significantly increase the likelihood that the covered banking entity would incur a substantial financial loss or would fail. We respectfully submit that this is unacceptably vague and open ended. To put the danger of moving forward with such an open-ended definition into perspective, we submit that during 2008, many of the securities traded in the mortgage market and other financial markets would likely have been characterized as "high risk assets" under the relevant language of the Proposal. It is vital for our markets that regulation not force market makers to exit their markets in times of stress and yet this is exactly what would happen if the Proposal is adopted as written. When considering a definition for "high risk assets," we encourage the Agencies to consider whether their definition would have forced covered banking entities to exit markets during the recent financial crisis. It is very clear that the intent of the Dodd-Frank Act is not to constrain liquidity during times of crisis since this would exacerbate the impact upon the economy.

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Exception for Government Securities

Section __.6(a) of the Proposal describes the government obligations in which a covered banking entity may trade notwithstanding the prohibition on proprietary trading, which include US government and agency obligations, obligations and other instruments of certain government sponsored entities, and state and municipal obligations. We respectfully submit that to continue to permit covered banking entities to accumulate significant risk in these markets in a manner that is not readily distinguishable from the risk associated with other asset classes, such as corporate bonds, is not reconcilable. On the one hand, the Proposal recognizes the importance of maintaining liquidity and access to capital for the US and state and local governments, while on the other hand ignoring the obvious danger of limiting liquidity and access to private capital for private businesses across the country. In short, we do not see the basis for permitting bank-owned broker dealers to assume the risks of providing unrestricted liquidity for US Government Obligations and other government related obligations, while prohibiting them from assuming the same risks for non-Government debt. The importance of insuring liquidity for US and state and local government obligations is obvious. We believe that the importance of providing the same liquidity for obligations of corporate issues, the principal drivers of US employment, is just as obvious.

Costs Versus Benefits

Assuming the Proposal is adopted in its current form, we believe that liquidity and trading costs will be significantly and adversely impacted. Implementation of the Proposal would, in our opinion, cause significant market dislocation and permanent changes in market liquidity available to transactions with no assurance that the outcomes they are designed to prevent will be avoided. What we can be certain of is that the US economy will be forced to bear both short-term and long-term costs associated with the reduction in market liquidity. While it is impossible to accurately predict what these costs would be, a simple example can give some indication of their magnitude.

Taking just the US corporate bond market and assuming: (i) the outstanding value of publicly traded debt securities is $16.4 billion; (ii) the average annual turnover of the outstanding float is 1X and (iii) the increased average cost per-trade resulting from the Proposal would be .01% would give us an annual cost of $41 billion. Not only would anything approximating this be a huge amount to pay for protection that is dubious at best, but it does not consider the indirect costs and adverse economic impact (e.g., from more limited access to debt financing) the Proposal would have on the financial markets and the US economy.

Economic and Competitive Risks

Based on the concerns and examples we have set forth, we believe implementation of the Proposal will have serious negative implications for the cost of

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capital to US businesses, liquidity in the US financial markets and the US economy. Implementation should also be examined within the context of the global financial markets, recognizing the risk that financial activity may migrate to the unregulated shadow banking system or to foreign financial centers such as Hong Kong, Singapore, London, Frankfurt, Paris or Zurich, or future foreign locations where investors can access reliable and properly-priced liquidity. The resulting negative effects on the strength and competitiveness of the United States as a global financial center and on employment for many thousands of individuals would be serious and irreversible. Investors will transact at the most economically viable point, physical locations will ebb and flow around that point.

Conclusion

If the Proposal is adopted in its current form, it can reasonably be expected that covered banking entities will be forced to severely curtail their traditional market making activities for all but the most liquid of securities. While this may be the intended effect of the Proposal, it ignores the fact that much of the current market making activities in this country are provided by covered banking entities. The short time frame provided for the covered banking entities to implement the Act almost insures a dramatic reduction in liquidity in the marketplace, as there does not now exist enough capacity among non-bank market makers to provide the necessary liquidity to the markets abandoned by the covered banking entities. The economic impact at a time when the economy is struggling is worrisome. Long term, we are concerned that a potential unintended consequence of the Proposal is that much of the market making activities currently provided by the covered banking entities may over time relocate offshore, along with much needed jobs.

Making a wholesale change of this magnitude to an activity so essential to the efficient functioning of our capital markets without the support of any empirical or academic studies analyzing the likely consequences is just not prudent or responsible.

We strongly urge the Agencies to re-think the approach taken in the Proposal by addressing the points raised in this letter in order to create a regulatory framework that accomplishes the narrow mandate of Section 619 of the Dodd-Frank Act, to prohibit speculative "proprietary trading" by covered banking entities, without adversely affecting the efficient functioning of US markets.

Very truly yours,

Peter S. Kraus
Chairman and CEO