October 17, 2018

Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
1155 21st Street NW
Washington, DC 20581

Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

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

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549–1090

Re: Proposed Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds

OCC: 12 C.F.R. Part 44, Docket No. OCC-2018-0010, RIN: 1557-AE27; Federal Reserve: 12 C.F.R. Part 248, Docket No. R-1608, RIN: 7100-AF 06; FDIC: 12 C.F.R. Part 351, RIN 3064-AE67; SEC: 17 C.F.R. Part 255 Release No. BHCA-3, File No. S7-14-18 RIN: 3235-AMIO; CFTC: 17 C.F.R. Part 75 RJN: 3038-AE72

Ladies and Gentlemen:

The Center for American Entrepreneurship (CAE) appreciates this opportunity to submit a comment letter in response to the request for public comments[1] on the joint rulemaking of the Board of Governors of the Federal Reserve System, Commodity Futures Trading Commission, Federal Deposit Insurance Corporation ("FDIC"), Office of the Comptroller of the Currency, and Securities

[1] *Proposed Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds*, 83 Fed. Reg. 33432 (July 17, 2018) (the "Release").

and Exchange Commission (together, the "Agencies") to revise the rules that implement section 13 of the Bank Holding Company Act of 1956 (such statute, the "BHCA",[2] and section 13 thereof, the "Volcker Rule", or "Rule"). The Rule establishes restrictions on proprietary trading by "banking entities" and certain relationships between banking entities and hedge funds and private equity funds. The implementing regulations for the Rule are codified at 12 C.F.R. §§ 44, 248, 351 and 17 C.F.R. §§ 75, 255.

CAE is a nonpartisan, Washington, DC area-based 501(c)(3) research, policy, and advocacy organization. CAE's mission is to engage policymakers in Washington and across the nation regarding the critical importance of entrepreneurs and startups to innovation, economic growth, and job creation – and to pursue a comprehensive policy agenda intended to significantly enhance the circumstances for new business formation, survival, and growth.

Background

Prior to the passage of the Dodd-Frank Act in July of 2010, many banks across the country – including many community and regional banks – participated in venture capital funds as limited partners. Banks' participation in such funds was beneficial to both banks and new businesses – banks served as an important source of early-stage capital for promising young companies in their towns and regions, while earning healthy returns and helping to develop the next generation of business customers.

Following enactment of Dodd-Frank, however – and, in particular, following the promulgation by regulators of rules to enforce the prohibition on proprietary trading – bank participation in such funds was prohibited.[3] In drafting rules to implement Volcker prohibitions, regulators cast a wide net – banning any trading or covered fund investment activities that might possibly be considered proprietary, regardless of their value to banks, their customers, or the broader economy – rather than specifically targeting those trading and fund activities that were clearly the object and intent of the Volcker Rule's systemic risk concerns.

As a result, rather than reducing systemic risk, Volcker Rule regulations have in many ways impeded the efficient operation of the financial system, driving banks away from providing services valued by their customers, reducing competition in affected markets, and undermining economic growth. A vivid example of the negative impact on banks of all sizes – including the nation's community and mid-size banks to which the Volcker Rule was not intended to apply – is the prohibition of banks' participation in covered funds, including venture capital funds. The unfortunate effect has been to stifle investment in emerging growth companies, which, research shows, contribute disproportionately to innovation, productivity gains, economic growth, and job creation.

Recommended Changes

Because the damage caused by the Volcker Rule stems principally from its implementing regulations and not the underlying statute, CAE is strongly of the view – along with other organizations like the

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[2] 12 U.S.C. § 1841 *et. seq.*

[3] The five federal financial agencies charged with implementing and administering the Volcker Rule are the Federal Reserve, Office of the Comptroller of the Currency (OCC), Federal Deposit Insurance Corporation (FDIC), Securities and Exchange Commission (SEC), and Commodity Futures Trading Commission (CFTC).

National Venture Capital Association and the American Bankers Association[4] – that financial regulators have the authority and latitude to revise covered fund restrictions in ways that would remove unwarranted obstacles to economic growth and focus more sharply on the specific activity that the statute seeks to prohibit – namely, engaging primarily in stand-alone, short-term proprietary trading.

This can be accomplished through three changes to the implementing regulation:

- First, limit the definition of "covered fund" expressly to those Section 3(c)(1) and Section 3(c)(7) funds[5] that are engaged primarily in short-term proprietary trading. This would align the definition with the statute's intent, while excluding those funds that rely on those Investment Company Act exemptions, but do not engage in activity that the Volcker rule targets.

- Second, the exclusions from "covered fund" currently found in the regulation can be preserved and revised in order to identify further those funds, such as venture capital funds and public welfare investment entities, that should not be treated as covered funds simply for relying on a federal securities law exemption (*i.e.*, sections 3(c)(1) or 3(c)(7)) that is unrelated to the purposes of the Volcker rule.

- Third, the regulation's definition of the term "ownership interest" can be narrowed substantially in order to reduce the regulatory uncertainty caused by its unintentionally broad scope, since the statute does not contemplate any expansion of the term beyond its ordinary meaning. In particular, the definition should apply only to equity or equity-like interests that are commonly understood to indicate a *bona fide* ownership interest in a covered fund.

CAE is grateful for the opportunity to submit this comment letter. Should you have any questions about this letter or any of the information or arguments contained herein, please contact me at (202) 821-9448 or at john@startupsUSA.org.

Sincerely,
S/
John R. Dearie
Founder and President

[4] See ABA Letter to the OCC (Sept. 21, 2017) (responding to OCC RFI on Volcker Rule reform proposals) (available at https://www.aba.com/Advocacy/commentletters/Documents/cl-Revising-Volcker2017.pdf); Department of the Treasury, Office of the Comptroller of the Currency, Proprietary Trading and Certain Interests in and Relationships with Covered Funds (Volcker Rule); Request for Input, 82 Fed. Reg. 36,692 (2017).

[5] Investment funds that rely on the exemptive provisions of section 3(c)(1) or section 3(c)(7) of the Investment Company Act of 1940, as amended (Investment Company Act). *See* 15 U.S.C. § 80a-1 *et seq.*