

FEDERAL RESERVE SYSTEM

Order Approving Extension of Conformance Period

Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) added a new section 13 to the Bank Holding Company Act of 1956 (codified at 12 U.S.C. § 1851) that generally prohibits banking entities from engaging in proprietary trading and from investing in, sponsoring, or having certain relationships with a hedge fund or private equity fund. These prohibitions are subject to a number of statutory exemptions, restrictions, and definitions.

Section 619 provides that a banking entity must conform its activities and investments to the prohibitions and restrictions of that section and any final implementing regulation no later than two years after the statutory effective date of section 13, which is July 21, 2012, unless extended by the Board.¹ Under the statute, the Board may, by rule or order, extend the two-year conformance period for up to three one-year periods, if in the judgment of the Board, an extension is consistent with the purposes of section 619 and would not be detrimental to the public interest.

The Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Commodity Futures Trading Commission, and the Securities and Exchange Commission (“Agencies”) have responsibilities for implementing section 619 through regulation. These Agencies issued final rules implementing section 619 on December 10, 2013, which become effective on April 1, 2014. These final rules contain critical definitions and descriptions of permissible and impermissible activities and require implementation of a comprehensive compliance program to ensure that impermissible activities do not take place. In particular, the final rules require a banking entity engaged in covered activities or investments to establish a variety of limits, written policies, internal review processes, and controls related to its marketmaking, underwriting, and hedging activities and to restructure and limit certain of its investments in and relationships with covered funds, including securitizations of nonloan assets.

¹ See 12 U.S.C. § 1851(c).

In order for a banking entity to conform its activities to the prohibitions and restrictions in section 619 and the final rules, a banking entity must first evaluate the extent to which it and all of its affiliates are engaged in covered activities as defined in the final implementing rules and then develop and implement a conformance plan to come into compliance by the end of the conformance period. Banking entities must also terminate prohibited activities and divest impermissible investments in order to be in compliance by the end of the conformance period, which in some cases will require the divestiture or restructuring of illiquid covered funds and in other cases will involve complying with investment limits that are tied to the risk-retention requirements imposed by section 941 of the Dodd-Frank Act. These requirements are the subject of an ongoing rulemaking that will be completed during the conformance period for section 619. Banking entities also must implement ongoing compliance and regulatory reporting/recordkeeping programs for permitted activities to ensure that no impermissible activities or investments occur.

To ensure effective compliance with section 619 and the final rules, banking entities need sufficient time to conform their activities in a safe and sound manner. Providing banking entities with sufficient time is consistent with protecting the safety and soundness of the entities because it allows for the termination of activities and the divestiture of prohibited investments in an orderly manner.

Section 619 itself provided banking entities with a two-year conformance period (with the possibility for extension). The legislative history of section 619 indicates this extended conformance period was intended to give markets and firms an opportunity to adjust to the prohibitions and requirements and any implementing rules.² Final implementing rules were only recently adopted by the Agencies and contain important details identifying the activities and investments that are covered by the prohibitions in section 619 and the final rules, as well as details about the manner in which activities permitted by the statute and final rules must be conducted.

For these reasons, the Board believes that granting a one-year extension of the conformance period is consistent with the purposes of section 619 of the Dodd-

² 156 Cong. Reg. S5898 (daily ed. July 15, 2010)(statement of Sen. Merkley).

Frank Act and would facilitate the effective implementation of the statute. Moreover, a one-year extension of the conformance period is not detrimental to the public interest and will ensure that there are not unnecessary disruptions to the financial markets as banking entities restructure their activities.

Each banking entity must conform all of its proprietary trading activities and investments to the prohibitions and requirements of section 619 and the final implementing rules by no later than the end of the conformance period. During the conformance period, each banking entity is expected to engage in good-faith efforts, appropriate for its activities and investments, that will result in the conformance of all of its activities and investments to the requirements of section 619 and the implementing rules by no later than the end of the conformance period.³ Good faith efforts include evaluating the extent to which the banking entity is engaged in activities and investments that are covered by section 619 and the final rules, as well as developing and implementing a conformance plan that is appropriately specific about how the banking entity will fully conform all of its covered activities and investments by the end of the conformance period. In addition, banking entities that have stand-alone proprietary trading operations are expected to promptly terminate or divest those operations. Moreover, banking entities should not expand activities and make investments during the conformance period with an expectation that additional time to conform those activities or investments will be granted.

Based on the foregoing, the Board hereby extends the conformance period under section 619 of the Dodd-Frank Act for all banking entities (subject to the reporting requirements noted above) for one year, until July 21, 2015.⁴ This extension does not apply to the data reporting and recordkeeping requirements

³ The Board issued a Statement of Policy Regarding the Conformance Period for Entities Engaged in Prohibited Proprietary Trading or Private Equity Fund or Hedge Fund Activities in which the Board clarified the activities that are permissible during the conformance period. 77 Fed. Reg. 33,949 (June 8, 2012).

⁴ Pursuant to the Board's regulation regarding the conformance period, a company that was not a banking entity or a subsidiary or an affiliate of a banking entity on July 21, 2010, must bring its activities into conformance before the later of the general conformance date, which by this order is July 21, 2015, or two years after the date on which the company becomes a banking entity or a subsidiary or an affiliate of a banking entity. 76 Fed. Reg. 8265 (February 14, 2011).

applicable under Appendix A of the final rule to certain banking entities with significant trading activities.

By order of the Board of Governors of the Federal Reserve System, effective December 31, 2013.

Robert deV. Frierson (signed)

Robert deV. Frierson
Secretary of the Board