SVB› Financial Group

January 10, 2011

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: *Conformance Period for Entities Engaged in Prohibited Proprietary Trading or Private Equity Fund or Hedge Fund Activities,* Docket No. R-1397, RIN No. AD 7100-58

Ladies and Gentlemen:

SVB Financial Group (*"SVB"*) is pleased to submit these comments in response to the Proposed Rule and Request for Public Comment (the *"Proposed Rules"*) on regulations to implement the conformance period under for the "*Volcker Rule*," as set forth in Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "*Act*").[1]

Generally speaking, the Proposed Rules provide a workable framework for banks to come into compliance with the Volcker Rule. In particular, we believe Sections 225.181(a)(3) and 225.181(b) of the Proposed Rules correctly provide that the initial conformance period, the three one-year extensions, and the single five-year extension for illiquid funds, if granted, apply sequentially.[2]

However, there are four substantive areas that require modification or clarification:

1. The Board should modify its proposed definitions to preserve its discretion to reach appropriate decisions – particularly its proposed definitions of "contractual obligation," "liquid asset," and "illiquid fund" – and should augment the factors it will consider in deciding whether to grant a requested extension.

2. The Board should clarify that the extension periods apply to all investing and fund management activities and, to the extent they apply to pre-existing funds, to the requirements of Section 619(d)(1)(G), 619(d)(2)-(4) and 619(f).

3. The Board should clarify that the Proposed Rules do not imply – and should not be read as implying – any views on the substance of the Volcker Rule. These issues are to be addressed by an interagency rulemaking process, with the benefit of a study authored by the Financial Stability Oversight Council, not as a part of this rulemaking.

4. The Board should establish a process to ensure banking institutions receive timely decisions granting or denying requests for extensions.

[1] Pub. Law 111-203, 124 Stat. 1376, Section 619 is codified as Section 13 of the Bank Holding Company Act of 1956, as amended. For ease of reference, we refer to Section 619 of the Act throughout.

[2] The Proposed Rules may be found at 75 Fed. Reg. 7241 *et seq.* (to be codified at 12 C.F.R. pt 225) (proposed Nov. 26, 2010). For ease of reference, we cite to Proposed Rules section numbers throughout.

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In addition, as a procedural matter, we urge the Federal Reserve to take an appropriate amount of time to finalize its conformance period rules. While it is important to issue rules promptly to promote certainty and allow for an orderly transition, it would be counter-productive for the Board to issue rules before it has had a reasonable opportunity to consider the comments filed in this proceeding and ensure its final rules are clearly written and well thought through. Additionally, we believe the Board should issue the rules on an interim basis and review and revise them as appropriate once final substantive regulations implementing the Volcker Rule have been issued.

BACKGROUND ON SVB FINANCIAL GROUP

SVB is a bank holding company and a financial holding company. Our principal subsidiary, Silicon Valley Bank, is a California chartered bank and a member of the Federal Reserve System. As of September 30, 2010, SVB had total assets of $14.75 billion.

SVB is the premier provider of financial services for high growth, innovative companies. Through Silicon Valley Bank and our other subsidiaries, we provide a comprehensive array of banking services to clients in the technology, life science, venture capital and premium wine industries. Over nearly three decades, we have become the most respected bank serving the innovation sector, and today serve more than 13,000 clients through 26 U.S. offices and international offices located in China, India, Israel and the United Kingdom. We have deep expertise and extensive knowledge of the people and business issues driving the technology sector, which we believe allows us to measurably impact our clients' success.

We earn the vast majority of our income by providing traditional banking and financial services. In addition, we have sponsored a number of venture capital funds and made investments in several third-party venture funds. Through our SVB Capital division, we currently manage nine "funds-of-funds" (which invest in venture capital funds managed by third parties) and four "direct investment funds" (which invest directly in high growth technology start-ups). Our sponsored funds are predominantly made up of third-party capital, which we manage for limited partner investors in the funds.

DISCUSSION

I. THE PROPOSED RULES PROPERLY PROVIDE FOR SEQUENTIAL CONFORMANCE PERIODS.

The Proposed Rules appropriately reflect the letter of the law and Congress' intent by providing that the initial conformance period, the three one-year extensions, and the single five-year extension for illiquid funds, if granted, will apply sequentially.[3] This approach provides clear, long term guidance for investors, permits the kind of long term planning required for a

[3] *See*, Sections 225.181(a)(3) and 225.181(b).

smooth transition, and appropriately reflects the long-term life cycle of some investments that may be covered by the Volcker Rule.

II. The Federal Reserve Board Should Modify its Proposed Definitions to Preserve Its Discretion – Particularly its Proposed Definitions of "Contractual Obligation," "Liquid Asset," and "Illiquid Fund" – and Should Augment the Factors It Will Consider In Deciding Whether to Grant a Requested Extension.

In passing the Volcker Rule, Congress recognized that the Rule constituted a dramatic shift from current law that could best be implemented over time. In particular, Congress recognized the extraordinary challenge banks would face if they were forced to reduce pre-existing investments and commitments to invest in illiquid assets over a time frame that was inconsistent with the long term nature of those investments.

As a result, Congress provided an extended wind-down period for illiquid investments. In the words of Senator Merkley, one of the provision's primary sponsors, "[t]he purpose of this extended wind-down period is to minimize market disruption while still steadily moving firms away from the risk of the restricted activities."[4] Senator Merkley urged the Federal Reserve Board to "adopt rules to define the contours of an illiquid fund as appropriate to capture the intent of the provision."[5]

In several cases, the proposed rules are too rigid or too narrow to achieve Congress' intent. This is both counter-productive and unnecessary. The definitions only determine the class of assets for which the Federal Reserve *may* grant an extension: even for assets that fall within the definitions, the Federal Reserve retains the discretion to approve or deny each request. As a result, it is much more important for the Board to preserve an appropriate level of discretion than to risk unintended and counter-productive results by adopting overly rigid definitions.

In this vein, SVB offers four specific recommendations.

A. The Proposed Definition of "Contractual Obligation" Contradicts the Meaning and Intent of the Act and Should Be Modified.

In order to keep banks from making an end-run around the Volcker Rule, Congress made clear that the extended transition period could *only* be used to satisfy pre-existing commitments – or, in the words of the statute, "to fulfill a contractual obligation that was in effect on May 1, 2010."

The plain meaning of the term "contractual obligation" is quite straightforward. A "contractual obligation" is an "obligation which arises from a contract or agreement," and a

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4 156 CONG. REC. S5,899 (July 15, 2010).

5 Id. at S5,899.

"contract" is "an agreement between two or more persons which creates an obligation to do or not to do a particular thing. Its essentials are competent parties, subject matter, a legal consideration, mutuality of agreement, and mutuality of obligation."[6]

Rather than relying on the plain meaning of "contractual obligation," the Proposed Rules state that a banking entity would be considered to have a contractual obligation only if:

- The contractual obligation could not be terminated under the terms of the agreement with the fund; and
- In the case of an obligation that can be terminated with the consent of other persons, the entity has used "reasonable best efforts" to obtain such consent and such consent has been denied.

This definition is unnecessarily narrow. Any contract can be modified or terminated with the consent of the parties. In some contracts, the parties explicitly address conditions under which they may amend, waive, or terminate the agreement. In others, they do not. But in both cases, a valid, binding contractual obligation exists.

More importantly, this definition would totally gut the "illiquid asset" provision and result in precisely the outcome Congress sought to avoid. The Board should modify this proposed definition to eliminate any requirement to seek consent to terminate a contractual obligation.

By definition, the assets at issue in the extended transition provision are *illiquid assets* – *i.e.*, assets for which there is no ready market. It is axiomatic that forced sales in illiquid markets do not yield fair prices. Buyers who know that a seller *must* sell and face no meaningful competition have leverage to extract substantial price discounts. Sellers, facing a legal deadline, have no choice but to sell at whatever prices buyers are willing to offer.

If the Board adopts the Proposed Rule in its current form, the fate of banking entities and their funds will rest in the hands of individual fund managers. If a fund manager refuses to consent to a sale, the banking entity will be able (with the Federal Reserve's approval) to wind the fund down in an orderly manner, over an extended period. But if a fund manager consents, the banking entity will be forced to sell an illiquid asset, prematurely, at whatever price it is able to get.

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6 Black's Law Dictionary; *see also* the Securities and Exchange Commission's Final Rule, "*Disclosure in Management's Discussion and Analysis about Off-Balance Sheet Arrangements and Aggregate Contractual Obligations*," Release Nos. 33-8182; 34-47264; FR-67 International Series Release No. 1266, File No. S7-42-02 (Apr. 7, 2003). In this rulemaking, the Commission adopted rules governing disclosures for certain types of contractual obligations. The Commission uses the term "contractual obligations" throughout its discussion and final rules, in a manner consistent with the basic definition set forward in Black's Law Dictionary. It appears the Commission considered the term to be sufficiently clear and self-defining that no further definition was required.

Recent data on secondary sales in the venture capital, private equity/buyout and funds of funds markets paints a picture of what banks might face if they are forced to sell illiquid assets under these conditions. As recently as December of 2007, sellers of alternative assets were, on average, able to sell investments at or relatively near to the investment's net asset value.[7] During the downturn, however, as many institutional investors considered selling investments to address liquidity needs or rebalance their portfolios, a buyers' market emerged and prices dropped by about 50%.[8] By the spring of 2009, those selling venture investments were getting only about fifty cents on the dollar (down from 100 cents on the dollar a year and a half earlier), those selling private equity/buyout investments were getting only about fifty five cents on the dollar (down from about 88 cents on the dollar), and those selling funds of funds were getting only about twenty five cents on the dollar (down from about 83 cents on the dollar).[9]

Of course, these investors were free to adjust their plans. Seeing the steep discounts buyers were demanding, many declined to sell. As a result, prices rose, hitting discounts of "only" twenty to fifty percent of net asset value by the spring of 2010.[10]

If the Federal Reserve adopts its Proposed Rules in their current form, it risks creating the kind of dynamic described above – or worse. Sellers would face a ticking clock. Buyers would know the sellers' predicament. The market could not re-calibrate, since sellers would have no choice but to sell at whatever price they could get. Furthermore, the entire process would begin when the market is still recovering from the downturn and secondary sales continue to be made, on average, at prices that are well below net asset values.

Forcing sales of illiquid assets merely because a banking entity has the legal right to ask for consent to sell, and a fund general partner is willing to grant that consent, could thus result in a very significant transfer of wealth from banks to non-bank investors and in precisely the kind of disruption and losses Congress sought to avoid. It would be truly perverse if the Volcker Rule was implemented in a way that weakened banks and gave non-bank hedge funds, private equity funds and other buyers a free pass to purchase bank assets at huge discounts.

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7 According to the research firm Preqin, sellers of venture capital investments in December 2007 received 100 cents on each dollar of net asset value ("*NAV*"), while sellers of private equity/buyout and funds of funds received between 80 and 90 cents on each dollar of NAV. *See* Preqin Research Report, *Private Equity Secondaries: The Market in 2010*, at page 2, Figure 3 (available at www.preqin.com). These data reflect aggregates across the sectors. Individual sales – and the prices at which individual assets can be sold – can vary meaningfully, due to the variation in assets and the illiquid nature of the secondary market for these assets.

8 Id. at page 2, Figure 3.

9 Id. at page 2, Figure 3.

10 Id. at page 2, Figure 3; *see also Preqin Launches Free Indicative Secondaries Portfolio Valuation Service as 11% of Private Equity LPs Currently Look to Sell*, May 13, 2009 (available at http://www.preqin.com/docs/press/14.May.09%20-%20Preqin%20Launches%20Free%20Indicative%20Secondaries%20Portfolio%20Valuation% 20Service.pdf).

In addition, the Proposed Rules would open a Pandora's Box of other issues. Regulators will have to resolve potentially complicated questions of fact about whether a banking entity used "reasonable best efforts" to get consent, whether a banking entity was justified in refusing if the consent depended on the bank agreeing to onerous conditions, and the like. Outcomes would depend on the actions of individual fund general partners, and could vary dramatically across otherwise similarly situated assets or banking entities, for reasons totally unrelated to – or even directly contrary to – the statute's purpose. For example, it is entirely possible that general partners of strong, successful funds – which present no risk to the banking entity's safety or soundness – could use this as an opportunity to consent to transfers, at "fire sale" prices, solely to the fund itself or to favored investors, forcing losses on the bank and its investors and weakening the institution.

The consent requirement is particularly unworkable for bank-sponsored funds (as opposed to bank investments in third-party funds). Consider a bank-sponsored fund, created before the May 1 deadline and invested principally in assets that meet the other requirements to be considered "illiquid." The Proposed Rules could be read as requiring the bank (as general partner) to seek consent from the funds' limited partner investors to sell off the banks' share in the fund. This would destroy the alignment of interest the limited partners thought they had obtained when the fund was formed. Alternatively (or additionally), for funds that invest in other funds, the Proposed Rules could be read as requiring the bank (as general partner) to seek consent from underlying fund managers to liquidate each investment within the fund, in order to reduce the total size of the fund and, as a result, the bank's total commitment to the fund. This could damage the fund and harm its investors – reducing, perhaps meaningfully, the total dollars invested, destroying diversification across time or investment type, and creating losses. At the extreme, it could even force banking entities to unwind funds in their entirety: as illiquid investments were sold, the overall mix of the fund would shift in the direction of any liquid investments, and at the extreme sales could turn a fund that had legitimately been invested primarily in illiquid assets into a fund whose residual investments failed to meet this test.

For all of these reasons, SVB urges the Board to strike paragraph (iii) of its proposed definition of "contractual obligation" and replace it with a definition that more closely tracks the plain meaning of the term and Congress' objectives, as follows:

> (iii) A banking entity shall be considered to have a contractual obligation for purposes of paragraph (b)(3)(i) or (ii) only if the banking entity, on or before May 1, 2010, entered into a written agreement, enforceable in accordance with its terms, pursuant to which the banking entity agreed to take or retain an equity, partnership, or other ownership interest in a fund.

B. The Federal Reserve Board Should Clarify its Definition of "Liquid Asset."

The definitions of "liquid asset" and "illiquid asset" attempt to distinguish liquid from illiquid assets, based on the attributes of markets typically used to buy and sell such assets.

These include, for example, bona fide bid/offer mechanisms, transparency and the ability to access trading partners and determine pricing on a near-instantaneous basis.[11]

All of these attributes, however, are means to an end ... not an end in and of themselves. In the end, the essence of a liquid asset is that it can quickly, easily and reliably be turned into cash without significant loss.

The Proposed Rules should explicitly incorporate this requirement, by adding the phrase "and the asset can consistently be bought and sold at reasonable expense and at a price that reflects the asset's fair value" to the end of paragraphs (2), (3) and (4) of the definition of "liquid asset."[12]

C. The Federal Reserve Board Should Clarify its Definition of "Illiquid Fund."

Section 225.180(f) of the Proposed Rules largely tracks the statute in defining the term "illiquid fund." However, it changes the wording of the second statutory test in one slight but potentially important way, by adding a comma after the phrase "was invested in" in paragraph (f)(2).

Under the statute, a fund qualifies as an illiquid fund if, as of May 1, 2010, it "[w]as invested in and contractually committed to principally invest in, illiquid assets." This definition appears to be designed to cover funds at different stages in their life cycle. For funds that are fully invested, it focuses on the actual investments held by the fund. For funds at an earlier stage of their investing cycle, it focuses on the combination of actual investments and contractual investment strategy.

The Proposed Rules, in contrast, state that a fund qualifies as an illiquid fund only if, as of May 1, 2010, it "[w]as invested in, and contractually committed to principally invest in, illiquid assets."

By inserting a comma after the phrase "was invested in," the Proposed Rules could be read as splitting the statutory requirements into two elements – one, that the fund made at least one investment in an illiquid asset before May 1, 2010, and two, that the fund is contractually committed to principally invest in illiquid assets.

There are probably a very small number of funds that were legally formed before May 1 but did not make their first investment until after this date. Where they exist, however, they should be treated as "illiquid funds" and eligible for the extended conformance period as long as they are contractually committed to principally invest in illiquid assets and, in fact, invest in these assets over time. Any other outcome would ignore the fact that the primary consideration

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11 *See* Proposed Rules, Section 225.180(h) (proposed definition of liquid asset).

12 For illiquid assets, the concept of "fair value" should incorporate both fair market value and book value.

under the statute is – and should be – the date on which the contractual commitment was entered into by the banking entity.

In addition, it is possible that specific facts and circumstances not specifically set forth in the definitions of "liquid fund" and "illiquid fund" may affect a banking entity's ability to dispose of the asset, at a fair value. To preserve its discretion to deal with such situations, the Federal Reserve Board should add a third element to its definition of "illiquid asset," as follows:

> "(3) Is an asset as to which other facts and circumstances exist, as determined by the relevant banking authorities, that materially and adversely affect the hedge fund or private equity fund's ability to dispose of the asset within a reasonable period and at the asset's fair value."

D. The Federal Reserve Board Should Augment the Factors It Will Consider in Deciding Whether to Grant a Requested Extension.

The Proposed Rules discuss various factors the Federal Reserve will consider in deciding whether to grant a requested extension. SVB believes that the Board should expressly state in its final rules that these factors will include whether granting or denying the extension will promote the purposes of the Volcker Rule and the financial stability of the United States; the effect granting or denying the extension will have on the safety and soundness of the banking entity; whether granting or denying the request will adversely affect investors in any affected funds, the bank's shareholders, or any other affected party; and whether granting or denying the extension will adversely affect the banking entity's ability to perform its contractual, fiduciary and other obligations to the affected fund and to third parties.

III. THE FEDERAL RESERVE BOARD SHOULD CLARIFY THAT THE EXTENSION PERIODS GOVERN ALL INVESTING AND FUND MANAGEMENT ACTIVITIES AND ANY OTHER REQUIREMENTS IMPOSED BY THE VOLCKER RULE.

The Proposed Rules do not clearly address whether the five-year "illiquid fund" extended transition period applies solely to investment activities, or more broadly to all activities under the Volcker Rule. For the reasons discussed below, the Board should clarify this issue and ensure that banks, bank-sponsored funds and bank-affiliated investors have a reasonable period and a workable approach to come into compliance.

Under the statute, the regular two-year conformance period, as well as the three one-year extensions, applies to all "activities and investments" that must be modified in order to comply with the Volcker Rule's requirements.[13] In contrast, the language governing the extended transition period for illiquid funds refers apply only to investments (specifically, to taking or

[13] Section 619 (c)(2).

retaining an equity, partnership, or other ownership interest in, or providing additional capital to, an illiquid fund).[14]

At first blush, this might seem to imply that the extended transition period applies solely to investment activities. By inference under this reading, a banking entity might be compelled to modify pre-existing illiquid funds to bring them into compliance with all the other provisions of the statute by the end of the regular two-plus-three year conformance period.

A careful reading of the statute, however, leads to a different conclusion. By its terms, the Volcker Rule creates two regulatory regimes: one that applies to funds formed before the Act's effective date, and the other that applies to funds formed after that date. The former – funds formed before the effective date – would be required to wind down in accordance with the conformance period requirements of Section 619(c). The latter – new funds formed after the effective date – could be formed only if they fell within one of the Volcker Rule's exceptions, including principally the "permitted funds" exception, as set forth in Section 619(d)(1)(G) and, in this case, only if they comply with the limits on investment and the branding, affiliate transactions, and other restrictions set forth in Sections 619(d(1)(G), 619(d)(2)-(4) and 619(f).

The Proposed Rules fail to clarify which of these two readings will be used to regulate banking entities. The resulting uncertainty has substantial practical consequences and leads to several problems.

First, banking entities with pre-existing investments that exceed the 3% Tier 1 cap do not know whether they may form new permitted funds and invest up to 3% in those funds, or whether they must put fund formation activities on hold – potentially for years – while their existing illiquid investments wind down in the natural course and fall below the aggregate 3% Tier 1 limit. This kind of near-term uncertainty and instability is something Congress attempted to avoid.

Second, the Proposed Rules could be read as allowing a banking entity to continue to hold investments in a bank-sponsored illiquid fund during the extended transition period, *but not to continue to carry out its responsibilities to manage the fund.* This outcome would harm banking institutions and investors and create instability in long term funds, without promoting the safety and soundness of the banking sector.

And third, the ambiguity leaves bank directors and employees in a potential bind. Under the Proposed Rules, the *banking entity* will be allowed to rely on the extended transition period for illiquid investments, but bank directors and employees – whose investments are captured

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[14] Section 619(c)(3).

solely due to their affiliation with the banking entity – will not have the same ability to wind down illiquid investments over time.[15]

In order to cure these problems and promote an orderly transition to the new rules, the Federal Reserve should state that the requirements of Sections 619(d)(2)-(4) and 619(f) only apply to funds formed by a banking entity under Section 619(d)(1)(G), after the effective date of the Volcker Rule.

Alternatively, and at an absolute minimum, the Federal Reserve Board should:

- Preserve its ability to allow banks to form new sponsored funds and invest in those funds up to the 3% per-fund limit, where they conclude that the bank can do so in a safe and sound manner.
- Explicitly confirm that banking entities may continue to manage pre-existing funds through any approved extension period and need to comply with the new requirements of Sections 619(d)(1)(G), 619(d)(2)-(4) and 619(f) for such funds only to the extent reasonably practicable.
- Explicitly state that bank directors and employees in pre-existing funds are not required to divest their interests or, at a minimum, are covered by the same extended transition period for illiquid investments provided to banking entities.

IV. The Federal Reserve Should Clarify that the Proposed Rules Do Not Imply – And Should Not Be Read As Implying – Any Views on the Substance of the Volcker Rule.

In the Overview to the Proposed Rules, the Board properly states its goals in addressing the conformance period provisions of the Volcker Rule:

> The proposed rule does not address other aspects of the Volcker rule which, as noted above, are subject to separate rulemaking requirements under section 13(b)(2) of the BHC Act. Because the proposed rule is not intended to address the definitional and other issues that are appropriately the subject of that coordinated, interagency rulemaking process, the proposed rule incorporates without modification the definitions of "banking entity," "hedge fund," and "private equity fund" contained in the Dodd-Frank Act. In addition, the Board

[15] The Volcker Rule restricts the ability of directors and employees of a banking entity to take or retain equity, partnership and other ownership interests in funds covered by the Volcker Rule. Section (d)(G)(vii). Under this provision, only directors and employees directly engaged in providing investment advisory or other services to the hedge fund or private equity fund may take or retain such interests. Some banks, including SVB, sponsor long-term illiquid funds in which bank employees may invest their own capital.

> has structured the proposed rule to address only those matters that are essential to implementation of the conformance period provisions of the Volcker Rule.[16]

Yet in several instances, the Proposed Rules could be read as implying a view on substantive aspects of the Volcker Rule. In particular, they could be read as implying that venture capital funds are "private equity funds" within the meaning of the Volcker Rule.

The ambiguity arises because Congress correctly noted that venture capital *investments* are illiquid investments.[17] This provision ensures that, to the extent a private equity or hedge fund has made investments in venture capital as part of its overall portfolio of investments, the venture investments will be protected by the extended wind down period.

While venture capital *investments* are clearly illiquid investments, it is an entirely different question whether venture capital *funds* are "private equity funds" within the meaning of the Volcker Rule. As discussed extensively by parties who filed comments before the Financial Stability Oversight Council,[18] and as recognized by Congress during consideration of the Act,[19] there are strong statutory and policy reasons to distinguish venture capital funds from private equity funds and to allow banking entities to continue to invest in and sponsor venture funds.

The issue of whether venture capital funds are within the ambit of the Volcker Rule's prohibitions is squarely before the FSOC. We urge the Federal Reserve Board to make clear in its final order that its conformance period rules do not pre-judge this important question.

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16 Proposed Rules at 5 (internal citations omitted; emphasis in original).

17 Section 619(h)(7)(A)(i).

18 *See*, Letter of SVB Financial Group to the Financial Stability Oversight Council, Docket ID: FSOC-2010-0002-1327 (November 5, 2010); Letter of Senator Mark Warner to the Secretary Timothy Geithner and Members of the Financial Stability Oversight Council (January 5, 2011) (stating that "Congress provided discretion to the regulators to treat venture capital as a separate class of activity" under the Volcker Rule because "venture capital presents none of the risks that the Volcker Rule seeks to mitigate and provides unique and essential benefits"); Letter of the AFL-CIO to the Financial Stability Oversight Council, Docket ID: FSOC-2010-0002-1327 (November 4, 2010) at page 5 (noting that "the Volcker Rule does not appear to be aimed at limiting banking entities' investment in venture capital funds" and urging the FSOC to adopt a definition of "private equity funds" that excludes venture capital funds); Letters of the Westly Group, Canaan Partners, Venrock, Bessemer Venture Partners, Benhamou Global Ventures, Trinity Ventures, Flybridge Capital Partners, Charles River Ventures, New Enterprise Associates, Gold Hill Capital, Scale Venture Partners, the National Venture Capital Association, and the Silicon Valley Leadership Group to the Financial Stability Oversight Council, Docket ID: FSOC-2010-0002-1327 (same); *see also* Letter from Rep. Spencer Bachus to Members of the Financial Services Oversight Council (Nov. 3, 2010) at 8 (urging the FSOC and implementing Regulatory Agencies to avoid interpreting the Volcker Rule in an expansive, rigid way that would damage U.S. competitiveness and job creation).

19 *See, e.g.*, Statement of Senator Dodd, 156 Cong. Rec. S5,904 (July 15, 2010); Colloquy between Senators Dodd and Boxer, 156 Cong. Rec. S5,904-5,905 (July 15, 2010); Statement of Rep. Eshoo, 156 Cong. Rec. E1,295 (July 13, 2010); Statement of Senator Brown, 156 Cong. Rec.S6,242 (July 26, 2010).

V. THE FEDERAL RESERVE BOARD SHOULD ESTABLISH A PROCESS TO ENSURE BANKING ENTITIES RECEIVE TIMELY DECISIONS GRANTING OR DENYING REQUESTS FOR EXTENSIONS.

If banking entities are to divest illiquid assets without creating market disruption or suffering unreasonable losses, they will need as much time as possible to plan for and execute these sales. The Proposed Rules should set forth a cohesive, end-to-end process that achieves this objective.

Yet currently, the Proposed Rules contain only the last step – a deadline after which banking entities may no longer seek an extension.[20] They do not explicitly provide for an earlier application process, allow the Federal Reserve to consider multiple conformance period requests on a consolidated basis, or set forth deadlines for regulators to respond to requests. We recommend that the Board make the following enhancements to its procedural rules.

First, we urge the Board to confirm that banking entities may file applications at any time. This will empower banking entities to be proactive in addressing their obligations to comply with the Volcker Rule and help avoid a last-minute inflow of extension requests.

Second, we urge the Board to adopt rules that permit it to consider multiple conformance periods on a consolidated or partially consolidated basis. Upon a sufficient demonstration of cause, the Federal Reserve should be able to approve all three one-year conformance period extensions at one time. Similarly, the Proposed Rules should empower the Federal Reserve to consider a banking entity's request for the final five year extended transition period for illiquid assets at any time after the initial one year extension (or consolidated one-year extensions) has been granted.

Finally, we urge the Board to ensure that any delay by the Federal Reserve in acting upon a timely request for an extension will not reduce the time available to the banking entity to achieve compliance. Specifically, the Board should set a time limit within which it generally will act upon applications for extension of time – we would suggest 90 days. This would enable banking entities to plan their transition process, with clear notice about the time the Federal Reserve may take to act on their request. To preserve the Federal Reserve's flexibility, we suggests that the Board allow itself to take longer than the specified 90-day period to issue a decision – but to provide that, in such cases, the banking entity would automatically be granted an equal extended period within which to come into compliance.

To illustrate, assume that a bank submitted a completed application on January 1 seeking a one-year extension of time for a conformance period ending on December 31. Under normal circumstances, the Federal Reserve's would issue its decision by April 1, and the applicant would have nine months to dispose of any investments for which the extension was denied. If

[20] *See* Section 225.181(c) (requiring a banking entity to submit a request for extension of time at least 90 days before the expiration of a relevant time period).

the Federal Reserve took an additional 90 days to issue a decision (*i.e.*, until July 1), the applicant would automatically receive a 90-day extension, until April 1 of the following year, to come into compliance. Through such an approach, the Board will preserve its flexibility to issue decisions at an appropriate time, but banking entities will be able to plan ahead and, by filing applications early, ensure they will have sufficient time to dispose of any assets for which an extension is denied.

Together, the above changes would provide for a smoother transition process, encourage banks to seek extensions in a timely manner, and better meet the intent of Section 13(c) of the Volcker Rule – "to minimize market disruption while still steadily moving firms away from the risk of the restricted activities."[21]

VI. THE BOARD SHOULD TAKE AN APPROPRIATE AMOUNT OF TIME TO CONSIDER FULLY ALL PUBLIC COMMENTS AND CAREFULLY CRAFT ITS FINAL RULES.

SVB recognizes the strict statutory deadlines facing the Board and applauds the Board's desire to act quickly to provide clarity on the transition process. At the same time, we urge the Board to take an appropriate amount of time to finalize its transition rules. While it is important to issue rules promptly to promote certainty and allow for an orderly transition, it would be counter-productive for the Board to issue rules before it has had a reasonable opportunity to consider the comments filed in this proceeding and ensure its final rules are clearly written and well thought through.

We believe that the Board has flexibility under the Act to issue final rules within a reasonable time. Any other reading of the Act would force the Board to issue final rules a mere nine working days after the deadline for submitting comments – which clearly would not provide sufficient time to consider fully all the comments, revise the rules, vet the revised rules thoroughly, approve the rules and make them public. Recognizing the importance and complexity of these rules, we urge the Board not to feel bound to issue final rules by January 21.

In addition, because the substantive regulations implementing the Volcker Rule will be issued after the Board finalizes its conformance period regulations, it is quite possible that some changes may be required to conform the conformance period rules to the final substantive rules. In order to avoid unanticipated or unintended consequences, we encourage the Board to issue its conformance rules on an interim basis and provide for an additional public notice and comment period shortly after the issuance of the final substantive regulations, in order to identify and address any inconsistencies or other issues.

CONCLUSION

For the reasons discussed above, SVB:

[21] Statement of Sen. Merkely, 156 CONG. REC. S5,899 (July 15, 2010).

- Supports the approach adopted in Sections 225.181(a)(3) and 225.181(b), providing that the initial conformance period, the three one-year extensions, and the single five-year extension for illiquid funds, if granted, apply sequentially;

- Urges the Board to provide greater flexibility in its proposed definitions – specifically, to modify its proposed definitions of "contractual obligation," "liquid asset," and "illiquid fund" and to augment the factors it will consider in deciding whether to grant a requested extension;

- Urges the Board to clarify that the five year extended conformance period for illiquid funds applies to all investing and sponsorship activities and governs all pre-existing funds;

- Urges the Board to expressly confirm that the Proposed Rules do not imply – and should not be read as implying – any views on the substance of the Volcker Rule;

- Urges the Board to establish a process to ensure banking institutions receive timely decisions granting or denying requests for extensions; and

- Urges the Board to take an appropriate amount of time to finalize its conformance period rules.

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We thank you for the opportunity to comment on the Proposed Rules. If you have any questions, please do not hesitate to contact me at any of the below points of contact.

Sincerely,

Mary Dent

Mary Dent
General Counsel
SVB Financial Group