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By Electronic Mail

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Washington, DC 20551

Commodity Futures Trading Commission
1155 21st Street, NW
Washington, DC 20551

Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20520

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

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

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

Re: Marketing-Making Issues in the Volcker Rule Proposal (FRB Docket No R-1432 and RIN 7100-AD82; FDIC RIN 3064-AD85; OCC Docket ID OCC-2011-14; SEC File Number S7-41-11)

Ladies and Gentlemen·

This letter is submitted on behalf of dealers, asset managers, pension funds, hedge funds and other clients and customers of dealers (the "Commenting Parties")[1] in response to the request for comments regarding the proposed rule (the "Proposed Rule")[2] implementing Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"),[3] commonly known as the "Volcker Rule " The Commenting Parties include dealers that act as market makers in a variety of securities markets, including the markets for various types of

1 The Commenting Parties are the firms listed at the conclusion of this letter

2 Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds, 76 Fed. Reg. 68,846 (Nov. 7, 2011) The proposed rule was issued by the Board of Governors of the Federal Reserve System (the "Federal Reserve"), the Federal Deposit Insurance Corporation (the "FDIC"), the Office of the Comptroller of the Currency (the "OCC") and the Securities and Exchange Commission (the "SEC" and, together with the Federal Reserve, the OCC and the FDIC, the "Agencies")

3 Codified as new Section 13 of the Bank Holding Company Act of 1956 (the "BHCA").

structured finance and asset-backed securities, and clients and customers of dealers that transact in those markets. The Commenting Parties appreciate the opportunity to provide these comments, and in this letter focus on the impact the Proposed Rule would have on certain market-making activities involving such securities issued by entities that the Proposed Rule would treat as covered funds.

The broad definition of "covered fund" in the Proposed Rule, which in relevant part uses Sections 3(c)(1) and 3(c)(7) of the Investment Company Act of 1940, as amended (the "Investment Company Act") to demarcate its scope, would bring within the Volcker Rule's reach securities of entities that do not possess or exhibit the characteristics of hedge funds or private equity funds at which the Volcker Rule is aimed For instance, collateralized loan obligations ("CLOs") and other privately placed asset-backed securities rely on Section 3(c)(1) or 3(c)(7), and by that fact alone would be covered funds, without any analysis of whether a banking entities' ownership of CLO securities presents risks that are in any way related to what the Volcker Rule is intended to address

Other comment letters have described a number of negative impacts stemming from the breadth of this definition. This submission discusses the negative impact on the market for privately placed structured finance securities that will result from the failure of the Proposed Rule to properly apply the market-making exemption in the Volcker Rule to the purchase of covered fund interests In particular, because the structured finance market depends heavily on dealers to provide liquidity, prohibiting banking entities from engaging in market-making in such securities will significantly impede the secondary market. Without a viable secondary market, demand for new issuances will also suffer. If not revised, this aspect of the Proposed Rule would contravene congressional intent and have significant adverse effects on important segment of the securities market.[4]

The Proposed Rule Fails to Properly Implement Congress's Market-Making Exemption

Pursuant to the Volcker Rule, Section 13(a) of the BHCA directs that a covered banking entity shall not "(A) engage in proprietary trading or (B) acquire or retain any equity, partnership, or other ownership interest in or sponsor a hedge fund or a private equity fund." BHCA Section 13(d) (the "Market-Making Exemption") provides that "[n]otwithstanding the restrictions under subsection (a) . . . the following activities are permitted: . . . (B) The purchase, sale, acquisition or disposition of securities and other instruments described in subsection (h)(4) in connection with underwriting or market-making-related activities "[5] Congress's inclusion

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4 Many of the modifications to the Proposed Rule that are suggested in other industry comment letters, in particular the definition of "covered funds," may indirectly address the issues identified in this letter While we support these modifications, the specific suggestions raised herein are aimed at the rules as proposed.

5 The "other instruments" to which Market-Making Exemption applies is defined by reference to BHCA Section 13(h)(4), which defines "proprietary trading." See BHCA § 13(d)(1)(B) This cross-reference to subsection (h)(4) refers only to the description of the instruments to which the proprietary trading

of underwriting and market-making activities within the scope of "permitted activities" under the Volcker Rule explicitly recognizes "the important liquidity and intermediation services that market makers provide to their customers and to capital markets at large."[6]

In implementing the Volcker Rule, the Agencies must give effect to legislative intent. Indeed, as Chairman Gensler stated during the recent Volcker Rule hearing before the House Financial Services Committee, "Congress actually laid out seven key permitted activities or, if you wish, exceptions And underwriting, market-making, hedging are three critical ones . And we want to fully comply with the intent of Congress."[7]

The Proposed Rule, however, fails to properly implement the Market-Making Exemption because it ignores Congress's intent to exempt market-making and underwriting activities from the full scope of the Volcker Rule's prohibitions. Section ___.4(b) of the Proposed Rule only addresses the prohibition against proprietary trading and does not exempt the acquisition or retention of ownership interests in covered funds that is prohibited by Section __.10 of the Proposed Rule.[8] This contravenes the statute's explicit provision to the contrary and threatens to have a significantly negative impact on liquidity for a large segment of privately placed securities that form an essential part of the international finance market.

Proper Implementation of the Market-Making Exemption Is Necessary to Ensure Liquidity in and Stability of the Financial Markets

The Commenting Parties depend on the market-making activity of dealers to provide liquidity to the market for a wide spectrum of privately placed securities that range from securitizations of a variety of corporate and consumer debt, synthetic structures such as credit linked notes and securities issued by simple bond repackaging vehicles. As the Agencies have previously recognized, these types of structured securities have become an essential part of U S and international capital markets [9] They are an important source of capital and liquidity and serve as key risk management tools that support a wide range of beneficial economic activity.

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prohibition applies, it does not limit the exemption itself to the activity of proprietary trading. Had Congress intended to limit the Market-Making Exemption to proprietary trading, it could have said that "proprietary trading" as defined in BHCA Section 13(h)(4) would be permitted subject to the relevant conditions See, e.g., BHCA § 13(d)(1)(H) (permitting "[p]roprietary trading conducted by a banking entity . provided that the trading occurs solely outside of the United States") It did not.

6 Proposed Rule, 76 Fed Reg. at 68869

7 Examining the Impact of the Volcker Rule on Markets, Businesses, Investors and Job Creation Before the H. Comm. on Fin. Servs., 112 Cong. (Jan. 18, 2012), Federal News Service, Inc. (statement of Chairman Gary Gensler, U S Commodity Futures Trading Comm'n)

8 "The prohibition on proprietary trading contained in § __.3(a) does not apply to the purchase and sale of a covered financial position by a covered banking entity that is made in connection with the covered banking entity's market-making related activities " Proposed Rule § __ 4(b)

9 Proposed Interagency Statement on Sound Practices Regarding Complex Structured Finance Activities, 69 Fed. Reg 28980 (May 19, 2004).

Many issuers of structured finance securities rely on Sections 3(c)(1) and 3(c)(7) of the Investment Company Act, and a broad segment of these securities take the form of a "share, equity security . . . limited partnership interest, membership interest, trust certificate or other similar instrument."[10] Without an exemption, therefore, banking entities generally will not be permitted to acquire or hold such interests, as would be necessary to continue both to act as underwriter in an initial offering of the securities and to engage in market-making activities within this segment of the securities market. And although the Proposed Rule provides limited exemptions to the prohibition against holding ownership interests in covered funds, including a limited exemption for hedging positions, these exemptions are both inadequate for underwriting and market-making activities and also do not cover many privately placed structured finance securities, including securities issued by loan securitizations that Congress specifically aimed to protect,[11] but that the Proposed Rule fails to exempt both through too narrow a definition of loan securitization and too broad an application of the prohibition on "covered transactions."

For example, Section __.13(d)'s exemption permitting the purchase of ownership interests in securitizations "solely" comprised of loans, contractual rights or assets directly arising from those loans, will not cover a wide range of structured finance securities, including in fact, CLOs. It is customary and expected for CLOs to include assets other than "loans" as defined in the Proposed Rule, such as money-market interests, cash and cash equivalents, and a limited amount of other securities, and therefore they would not qualify under Section __.13(d). Even if the Agency makes further changes to expand the loan securitization exemption, as they should, there will be a large volume of both new and existing structured finance products that will fall outside the exemption and which critically depend on dealer market-making for liquidity Moreover, even for structured finance securities that did qualify for the overly narrow loan securitization exemption, Section __.16(a)'s prohibition against "covered transactions" between a banking entity and a covered fund it sponsors, advises, or organizes and offers could potentially be interpreted to prohibit banking entities from purchasing and thus underwriting and making markets in debt securities issued by such a covered fund.

The existing Section __.12(a) exemption is also insufficient to protect necessary underwriting activity. Section __.12(a) gives banking entities a limited and temporary ability to engage in conduct "[e]stablishing the covered fund and providing the fund with sufficient initial equity for investment to permit the fund to attract unaffiliated investors." But this exemption does not address the ordinary role of an underwriter or initial purchaser structured finance securities, which is generally to purchase 100% of such securities for concurrent or subsequent resale to investors. Nor does the exemption resolve the potential prohibition on purchasing securities other than "ownership interests" presented by Section __.16(a), or address funds that a banking entity has not "organize[d]," the latter omission eliminating the availability of the exemption to members of an underwriting syndicate who may purchase fund interests for distribution but are not involved in organizing the fund.

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10 Proposed Rule, § __ 10(b)(3)

11 BHCA § 13(g)(2)

If the Proposed Rule is not modified to implement a broader market-making exemption, dealers will be quite limited in their ability to underwrite and make markets in these securities, which could ultimately have a negative impact on the availability of credit.[12] The liquidity in the secondary trading market in the private asset-backed and structured finance market is heavily dependent on dealer participation, as these securities are not exchange traded and thus rely on market makers to act in an intermediation role between customers, buying and selling securities as principal, in order to support a two-way market. If there is not a viable secondary market, the primary market for new issuances will also suffer, limiting the ways in which banks, and therefore the companies that are their clients, can access the markets to facilitate financing activity.

The ability of banking entities to purchase structured finance securities is important to new origination and placements in other ways as well. A banking entity involved in the development and initial placement of structured finance securities will often both underwrite and thereafter attempt to make a market in, and thus add to the liquidity of, those securities. While a dealer's ability to make a market in the securities is understood by investors not to be guaranteed, investors generally look to underwriters to make a market in securities they distribute, and take comfort from the presence of at least one dealer willing to attempt to act as a market maker. If the Volcker Rule were to prohibit or limit either the initial underwriting or the market-making in these securities, the impact on this market could be severe.

Customers also depend on the inter-dealer market for the price transparency that is necessary to accurately mark the structured finance securities to market. If dealers are unable to continue in this role, then the mutual funds, insurance companies, pension funds and endowments that rely on the pricing provided by dealers as part of their market-making function will face new obstacles to accurately valuing these securities, which could further damage the viability of this market.

Such a negative effect on the secondary market for these types of securities is not the result required by Congress, which has expressly sought to protect "[t]he purchase, sale, acquisition or disposition of securities . in connection with underwriting or market-making-related activities."[13] The language of the Market-Making Exemption refers to the "restrictions under subsection (a)", which covers both the ban on proprietary trading and the directive that a banking entity "shall not . . . (B) acquire or retain any equity, partnership, or other ownership interest in or sponsor a hedge fund or a private equity fund." There is no statutory authority to exclude the acquisition or retention of covered fund ownership interests from the scope of permissible underwriting or market-making activities.

Moreover, the Volcker Rule was not intended to exclude banking entities from the

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12 We are not suggesting that Section __ 16(a) prohibits covered banking entities from investing in structured finance securities of issuers that they do not advise, sponsor or organize and offer, which should not be within the scope of Super 23A.

13 BHCA § 13(d)(1)(B).

market for structured finance securities. As other comment letters have pointed out, many issuers of these securities are affected by the Volcker Rule due only to the overly broad definition of "covered fund" in the Proposed Rule. The task of reforming and regulating the asset-backed securities market in particular is accomplished by other Dodd-Frank provisions, including the risk retention provision now found in Section 15G of the Securities Exchange Act of 1934, as amended, and the conflicts of interest provisions of Section 621 of Dodd-Frank, adopted in parallel with the Volcker Rule Evidence of this balance is present in the Volcker Rule itself, as it protects the sale and securitization of loans by banking entities,[14] and recognizes a need to permit banking entities to comply with the Dodd-Frank risk retention requirements.[15] Without giving proper force to the Market-Making Exemption, however, the Volcker Rule could significantly hamper the liquidity in, and viability of, these markets.

We therefore urge the Agencies to revise the Proposed Rule to properly implement the Market-Making Exemption and avoid placing significant restrictions on legitimate underwriting and market-making activity. To properly reflect congressional intent, the Agencies should (i) expand the scope of the Section __.4(b) underwriting and market-making exemption and (ii) expand the scope of the Section __ 16(a)(2) exemption to the ban on covered transactions in each case in a manner sufficient to permit banking entities to purchase structured finance securities as part of their traditional underwriting and market-making activities. Such revisions would advance congressional policy aiming to protect underwriting and market-making as a traditional client-oriented financial services.

Suggested Modifications to Section __.4(b) of the Proposed Rule

As described above, Section 13(d) clearly applies the Market-Making Exemption to the purchase of interests in covered funds as well as to the proprietary trading prohibition. Section ___.4(b) of the Proposed Rule, however, applies the Market-Making Exemption only to the proprietary trading prohibition in Section __.3(a), and not to Section __.10(a)'s prohibition against sponsoring and investing in covered funds. The rule implementing the Market-Making Exemption should permit banking entities to purchase, acquire and hold interests in covered funds in connection with its underwriting and market-making-related activities to preserve dealers' ability to continue to participate in the initial issuance of and to support the secondary market in structured finance securities (We note that other commenters have proposed that the provisions seeking to distinguish market-making from proprietary trading be modified to better reflect market practice. We support this view, and would also suggest the Agencies consider the differences that exist between different securities markets in undertaking to revise the proposed metrics and other standards.)

Without this modification to Section __.4(b) of the Proposed Rule, banking entities will be unable to underwrite and make a market in a wide variety of securities that might be construed as "ownership interests" in covered funds Section __.13(d)'s loan securitization

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[14] BHCA § 13(g)

[15] Proposed Rule § __.14(a)(ii)(3).

exemption is far too narrow to resolve this issue (even if modified to better reflect existing CLO structures). Given the explicit interest of Congress in preserving banking entities' underwriting and market-making role and the extensive regulation of the asset-backed securities market elsewhere under Dodd-Frank, it would disserve both the express terms of Dodd-Frank and its purposes to effectively bar banking affiliates from underwriting or making a market in structured finance securities.

Suggested Modifications to Section __.16(a)(2) of the Proposed Rule

While not entirely clear, Section __.16(a) of the Proposed Rule ("Super 23A") might be interpreted to also bar banking entities from engaging in underwriting and market-making activities with respect to some structured finance securities where the banking entities' role as market maker might be most important. Super 23A prohibits a banking entity from entering into "covered transactions" with a covered fund it sponsors, advises or organizes and offers, and defines "covered transaction" to include "a purchase of or an investment in securities issued by the affiliate."[16] While a banking entities' underwriting activities alone would not invoke Super 23A, that provision could be read to prohibit banking entities from purchasing debt securities issued by a securitization it sponsors, advises or organizes and offers, including securities purchased in its capacity as underwriter or market maker

If a banking entity that structures or places securities is viewed as "sponsor[ing]" or "organiz[ing] and offer[ing]" the covered fund, the impact of these limitations could be particularly acute in the market for structured finance securities.[17] It is difficult to see how a prohibition against a banking entity underwriting an issuance it sponsors or organizes and offers is workable on any level In addition, as noted above, there is often an expectation that a banking entity involved in the initial placement of securities will attempt to act as a market-maker for those securities While investors acknowledge the existence of such a market cannot be assured, for the Volcker Rule to actually prohibit a banking entity from making a market for securities it sponsors would have substantial and adverse impact on investor expectations market liquidity, and overall market structure.

The Agencies interpreted Super 23A to permit the purchase of "ownership interests in a covered fund" that comply with the covered-fund activities described in Subpart C

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16 12 U.S C § 371c(b)(7). As other comment letters have noted, Super 23A's far-reaching scope would cause significant disruptions to typical market practices.

17 If a banking entity merely acting as underwriter were to be considered "sponsor[ing]" or "organiz[ing] and offer[ing]" a covered fund, this interpretation would have a substantial and detrimental effect on the securitization market. While we do not think such an interpretation would be correct, a proper implementation of the statutory text of the Market-Making Exemption as explained herein by expanding the scope of Section _4(b) underwriting and market-making exemption, and the scope of Section _16(a)(2) to cover the purchase of securities issued by covered funds in a banking entities' underwriting or market making capacity, would make it clear that banking entities that underwrite covered funds may purchase the debt securities of such covered funds and may fully participate in underwriting and market-making activities with respect to such covered funds

of the Proposed Rule [18] The Subpart C exemptions, however, relate only to ownership interests, not other securities such as debt securities issued by covered funds, and the exemptions themselves are either not properly defined or are not workable in a market-making context.[19] It would be an incongruous result to protect a banking entity's ability to purchase ownership interests despite Super 23A restrictions, and yet preclude banking entities from the lesser involvement with covered funds that would result from market-making in debt securities. The Agencies should therefore modify this provision to give proper effect to the Market-Making Exemption such that it applies to securities that the banking entity purchases in its role as market maker.

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[18] Proposed Rule § __ 16(a)(2)

[19] Aside from the inadequacy of the "loan securitization" exemption of Section __.13(d), neither the de minimis exemption for funds the banking entity has organized and offered, or the risk retention exemption permitting banking entities to hold ownership interests in securitization issuers to the extent that the banking entity is required to do so to comply with the minimum requirements of section 15G of the Exchange Act, is sufficiently broad to accommodate traditional market-making activity

In consideration of the foregoing, we urge the Agencies to interpret the Market-Making Exemption according to its plain statutory language and modify Section __.4(b) and Section __.16(a)(2) of the Proposed Rule to allow banking entities to purchase securities issued by covered funds in connection with the underwriting and market-making activities of a banking entity These modest revisions to facilitate underwriting and market-making activities are justified by the express congressional directive to preserve banking entities' underwriting and market-making activities for the benefit of customers.

Respectfully submitted,

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The Commenting Parties:

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