

# United States Senate

WASHINGTON, DC 20510

February 16, 2012

The Honorable Ben S. Bernanke  
Chairman  
Board of Governors of Federal  
Reserve System  
20<sup>th</sup> Street and Constitution Avenue, NW  
Washington, D.C. 20551

The Honorable Mary L. Schapiro  
Chairman  
Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549

The Honorable Martin J. Gruenberg  
Acting Chairman  
Federal Deposit Insurance Corporation  
550 17<sup>th</sup> Street, NW  
Washington, D.C. 20429

Mr. John G. Walsh  
Acting Comptroller of the Currency  
Office of the Comptroller of the Currency  
250 E Street, SW  
Washington, D.C. 20219

The Honorable Gary Gensler  
Chairman  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, NW  
Washington, D.C. 20581

Dear Chairman Bernanke, Chairman Schapiro, Acting Chairman Gruenberg, Acting Comptroller Walsh, and Chairman Gensler:

We are writing to you regarding your proposed rule on the *Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds*, more commonly known as the “Volcker Rule.” While reducing systemic risk and taxpayer exposure are important objectives, we are concerned with the proposed rule. The current 300-page proposal takes a complex transaction-based approach, which has generated numerous outstanding questions and resulted in a great deal of uncertainty. We hope these issues can be resolved and would like to highlight a few examples that demonstrate the broader concerns surrounding the economic impact of the rule as proposed.

As you know, businesses of all sizes – including asset managers, venture capital funds, pension funds and, individual investors – depend on efficient and liquid capital markets. Much of the discussion surrounding the Volcker Rule during Congressional consideration of Dodd-Frank focused on large institutions, but the proposed rule could have a broader impact beyond what the statute intended. Specifically, we are concerned that the proposed rule, as drafted, could adversely affect Main Street businesses by reducing market liquidity and increasing the cost of capital. In fact, there is evidence that this is already beginning to occur.

Importantly, the Dodd-Frank statute prevents proprietary trading while preserving “permitted activities” that are essential to the efficient functioning of vibrant capital markets. These permitted activities include market-making, underwriting, hedging, and trading in an insurance company’s general account. However, as drafted, the proposed Volcker Rule could restrict a firm’s market-making activity as part of client-oriented trading operations. As market-makers reduce or eliminate inventory, liquidity is reduced and trading spreads widen. This will increase trading costs paid by investors, thereby reducing returns for investors large and small alike, including individuals saving for retirement through an IRA, 401(k), or similar programs. Additionally, the proposed Volcker Rule applies to banks, regardless of size or activity. Thus, the Volcker Rule could force small and regional banks to build out compliance programs even though they do not have proprietary trading desks. The associated compliance costs could cause some banks to exit certain types of activities that provide liquidity to their customers and are permitted by the Volcker Rule, such as market-making, hedging and other asset-liability management activities, thereby leading to further concentration in the industry.

We are also concerned that the covered funds definition is so broad that it would inadvertently sweep in many commonly held corporate structures that are used for capital formation and risk mitigation, such as wholly owned subsidiaries and joint ventures – entities that the Financial Stability Oversight Council acknowledged in its study on the Volcker rule “would not be thought of as a ‘hedge fund’ or ‘private equity fund.’” The covered fund definition may also sweep in venture capital investing, which is contrary to Congressional intent. In fact, former Senate Banking Committee Chairman Christopher Dodd specifically stated on the Senate floor on July 15, 2010 that “properly conducted venture capital investment will not cause the harms at which the Volcker rule is directed.” As you move forward, we urge you to address the definition of covered funds in order to prevent disrupting commonly held corporate structures, used mainly for ordinary course lending and investing, and to conclude that venture capital funds are not covered by the Volcker rule.

Furthermore, the proposed rule does not clarify whether the exemption for proprietary trading activity in an insurance company’s general account extends to investing in covered funds. We encourage you to apply the exemption for insurance company general accounts to covered funds investments. The law is clear and is further supported by statements on the Senate floor that the Volcker Rule should accommodate for the business of insurance. This includes permitting insurers to continue their investment activities in covered funds subject to the relevant insurance company investment laws at the state level. To allow an insurance company to invest in covered funds for its general account is an appropriate statutory interpretation of the Dodd-Frank Act and would preserve protections against any safety and soundness concerns, as state laws already sufficiently restrict insurance companies’ investments.

We also encourage greater clarity on the Volcker Rule’s application to offshore activities of U.S.-based firms and foreign firms. It is essential that the Volcker Rule allow both U.S. banks and foreign banks with U.S. operations to maintain their ability to compete globally with local firms where the Volcker Rule does not apply.

Finally, we respectfully request that the proposal ensure that legitimate trading activity is preserved, while focusing on banning proprietary trading desks as well as investment in liquid

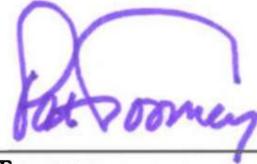
hedge funds that may be used to evade the proprietary trading ban. In addition, market participants and stakeholders should be provided with an ample opportunity to review and provide feedback going forward. Likewise, it will be important to ensure that implementation is properly coordinated among agencies and provides an adequate compliance regime that will prevent market disruptions.

We look forward to working with you to ensure that the rule provides the flexibility needed to preserve core market functions, while maintaining the intent of the Dodd-Frank statute.

Sincerely,



Thomas R. Carper  
United States Senator



Pat Toomey  
United States Senator



Mark Warner  
United States Senator



Mike Crapo  
United States Senator



Christopher A. Coons  
United States Senator



Scott Brown  
United States Senator