

Order Approving Extension of Conformance Period Under Section 13 of the Bank Holding Company Act

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 (“BHC Act”) (codified at 12 U.S.C. § 1851) that generally prohibits banking entities from engaging in proprietary trading and from acquiring or retaining an ownership interest in, sponsoring, or having certain relationships with a hedge fund or private equity fund (together, a “covered fund”).¹ These prohibitions are subject to a number of statutory exemptions, restrictions, and definitions.

The restrictions and prohibitions of section 13 of the BHC Act became effective on July 21, 2012; however, the statute provided banking entities a grace period until July 21, 2014, to conform their activities and investments to the requirements of the statute and any implementing rules issued by the Board, OCC, FDIC, SEC, and CFTC (collectively, “the Agencies”).² Under the statute, the Board may, by rule or order, extend the two-year conformance period for one year at a time, for a total of not more than 3 years, if in the judgment of the Board, an extension is consistent with the purposes of section 13 and would not be detrimental to the public interest. This would allow extensions of the conformance period until July 21, 2017. Section 13 also permits the Board to provide banking entities an additional transition period of up to five years to conform certain illiquid funds.

¹ See 12 U.S.C. § 1851. A banking entity is defined by statute as any insured depository institution, any company affiliated with an insured depository institution, as well as any foreign bank that has a branch or agency in the U.S., with certain limited exceptions.

² 12 U.S.C. § 1851(c).

In December 2013, the Agencies approved a final regulation implementing the provisions of section 13 of the BHC Act.³ In connection with issuing the final rule, the Board also extended the conformance period until July 21, 2015.⁴ One year later, in December 2014, the Board granted a limited extension, until July 21, 2016, to permit banking entities additional time to conform investments in and relationships with covered funds and foreign funds that were in place prior to December 31, 2013 (“legacy covered funds”), and announced its intention to act again to grant banking entities an additional one-year extension of the conformance period, until July 21, 2017, to conform ownership interests in and relationships with legacy covered funds.⁵

Since approval of the final rule implementing section 13, a number of banking entities, private equity funds, trade associations, and members of Congress have requested additional extensions of the conformance period to allow banking entities additional time to conform or divest covered fund investments and relationships. Commenters requested additional time to identify funds that are covered by the statutory provisions, determine whether those funds can be conformed to the statute and final rule or must be divested, and divest or conform nonconforming investments in covered funds.

Commenters argued that, prior to adoption of the final rule, banking entities were permitted to make and did make significant investments in many thousands of covered

³ See Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Fund and Private Equity Funds, 79 Fed. Reg. 5536 (Jan. 31, 2014); 79 Fed. Reg. 5808 (Jan. 31, 2014).

⁴ See Order Approving Extension of Conformance Period (Dec. 10, 2013), [available at http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20131210b1.pdf](http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20131210b1.pdf).

⁵ See Order Approving Extension of Conformance Period (Dec. 18, 2014), [available at http://www.federalreserve.gov/newsevents/press/bcreg/20141218a.htm](http://www.federalreserve.gov/newsevents/press/bcreg/20141218a.htm).

funds that, following adoption of the final rule, must be evaluated and conformed to the requirements of section 13. Commenters asserted that an extended period of time is needed to allow for the orderly sale of covered fund interests that must be divested, including divestitures that must, by statute, be made by employees, officers, and directors of banking entities.⁶ In addition, banking entities contended that the statutory requirements to change the names of covered funds and restrict relationships with covered funds that may be retained by banking entities would require additional time to allow consultation with, and the consent of, investors in and managers of covered funds.⁷ Private funds that are sponsored by nonbanking entities have also indicated that a number of investors in their funds include foreign banks subject to section 13 and the final rule. These nonbanking entities have requested additional time to restructure, conform, redeem, or sell investments by foreign banks in these third-party funds. Moreover, commenters argued that additional time is needed for foreign funds that have some activities in the U.S., and their managers and investors, to determine whether they must take steps to modify their sales practices, governance, or ownership structure to ensure compliance with various provisions of section 13.

Providing banking entities with additional time to conform investments that were made in covered funds prior to the adoption by the Agencies of implementing rules for

⁶ The statute prohibits employees and directors of a banking entity from investing in certain types of funds sponsored by the banking entity unless the director or employee is directly engaged in providing investment advisory or other services to the covered fund. See 12 U.S.C. § 1851(d)(1)(G)(vii).

⁷ The statute prohibits a fund sponsored by a banking entity from sharing the same name or a variation of the same name with the banking entity or any affiliate for corporate, marketing, promotional, or other purposes. See 12 U.S.C. § 1851(d)(1)(G)(vi). The statute also imposes limits on lending and other transactions between a covered fund and a banking entity that sponsors, manages, or advises the fund. See 12 U.S.C. § 1851(f).

section 13 would enable banking entities to terminate existing activities and divest existing investments in an orderly manner consistent with protecting the safety and soundness of those banking entities. It would also reduce the potential for disruptive effects that significant divestitures of covered funds could have on markets and on the investments of others not subject to section 13, as well as allow banking entities additional time to work with other investors and investment managers to take steps to conform covered funds to the requirements of the statute and the final rule (such as by issuing disclosures, changing fund names, and conforming employee investments).

The legislative history of section 13 indicates that an extended conformance period was intended to give markets and firms an opportunity to adjust to the prohibitions and requirements of the statute and any implementing rules.⁸ The Board believes granting a one-year extension of the conformance period, until July 21, 2017, for banking entities to conform investments in and relationships with legacy covered funds is consistent with the purposes of section 13 of the BHC Act and would facilitate the effective implementation of the statute. A limited extension for legacy covered funds would permit banking entities the full period permitted by the Dodd-Frank Act to divest or conform investments made by banking entities prior to adoption of the final rules implementing section 13. Moreover, a one-year extension of the conformance period would not be detrimental to the public interest and would ensure that there are no unnecessary disruptions to the financial markets as banking entities restructure their covered fund activities and investments to comply with section 13 and its implementing regulations.

⁸ See 156 Cong. Reg. S5898 (daily ed. July 15, 2010) (statement of Sen. Merkley).

This extension would permit banking entities additional time to divest or conform only legacy covered fund investments and relationships made by banking entities prior to December 31, 2013. All investments in and relationships related to investments in a covered fund made after that date were required to be in conformance with section 13 of the BHC Act and the implementing rule by July 21, 2015. The extension would not apply to proprietary trading activities, which also were required to conform to the final rule by July 21, 2015.

During the extended conformance period, banking entities are expected to make plans well in advance of the end of the extended conformance period regarding how they will conform or divest legacy covered fund investments in an orderly and safe and sound manner. Banking entities are encouraged to take steps to divest covered funds or conform such funds to the statute and final rule during the extended conformance period. The Board will also continue to consider whether to take action regarding illiquid funds.

The other Agencies charged with enforcing the requirements of section 13 of the BHC Act and the final rule plan to administer their oversight of banking entities under their respective jurisdictions in accordance with the Board's conformance rule and this extension of the conformance period. Nothing in this Order restricts in any way the authority of any agency to use its supervisory or other authority to limit any activity or investment the agency determines to be unsafe or unsound or otherwise inconsistent with applicable law.

Based on the foregoing, the Board hereby extends the conformance period under section 13 of the BHC Act for all banking entities to conform investments in and relationships with legacy covered funds for one year, until July 21, 2017.⁹

By order of the Board of Governors of the Federal Reserve System, effective July 6, 2016.

Robert deV. Frierson (signed)

Robert deV. Frierson
Secretary of the Board

⁹ 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, 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).