Statement of Jeremiah O. Norton on Interim Final Rule Regarding Treatment of Certain Collateralized Debt Obligations Backed Primarily by Trust Preferred Securities with Regard to Prohibitions and Restrictions on Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds

I am not able to support the promulgation of the Interim Final Rule (IFR). The rationale offered by the agencies promulgating the IFR is that a separate provision in the Dodd-Frank Act, Section 171, grandfathers the treatment of certain trust preferred securities or subordinated debt securities (TruPS) as regulatory capital for certain issuer community banking organizations.[1] The agencies believe that certain TruPS CDOs should be a permitted investment for all banking entities to avoid undercutting the grandfathering provisions of Section 171, notwithstanding the fact that nothing in the Volcker Rule impairs or frustrates the capital position of TruPS issuers subject to the grandfathering provision.

The legal authority under which the IFR is being promulgated, however, is not clear. Section 619 of the Dodd-Frank Act prohibits a banking entity from "acquir[ing] or retain[ing] any equity, partnership, or other ownership interest in or sponsor a hedge fund or a private equity fund" unless otherwise provided in the Section.[2] Section 619 contains a definition of "hedge fund and private equity fund" which includes "an issuer that would be an investment company, as defined in the Investment Company Act of 1940,[3] but for section 3(c)(1) or 3(c)(7) of that Act…"[4] The agencies acknowledge in the IFR that the

[1] *See* 12 U.S.C. § 5371(b)(4)(C).
[2] 12 U.S.C. § 1851(a)(1)(B).
[3] 15 U.S.C. 80a-1 *et seq.*
[4] 12 U.S.C. § 1851(h)(2).

formulation of this definition in the agencies' December 10, 2013 Final Rule "generally includes pooled investment vehicles, such as many TruPS CDOs, that use 3(c)(1) or 3(c)(7) but do not qualify for another exclusion under the Investment Company Act or the Final Rule."[5] Section 619(d) contains a specific list of activities in which banking entities are permitted to engage notwithstanding the general prohibition in the Section. In addition to the specifically-included permitted activities in the statute, the agencies may permit such other activity as they jointly determine by rule "would promote the safety and soundness of the banking entity and the financial stability of the United States."[6] The agencies have not demonstrated that these criteria have been satisfied.

In my view, it is more appropriate to address this matter through the legislative process.

[5] Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Securities and Exchange Commission, Commodity Futures Trading Commission, *Treatment of Certain Collateralized Debt Obligations Backed Primarily by Trust Preferred Securities with Regard to Prohibitions and Restrictions on Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds*, Interim Final Rule (http://fdic.gov/news/news/press/2014/pr14003a.pdf).

[6] 12 U.S.C. § 1851(d)(1)(J).