

**Statement by Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation,
Final Rule: Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain
Interests in, and Relationships with, Hedge Funds and Private Equity Funds**

August 20, 2019

The global financial crisis a decade ago exposed many weaknesses in the supervision and regulation of the financial industry. In the years following the crisis, regulators imposed a number of new rules, including many rigorous requirements that apply to the largest banks. Some of these mandates, such as enhanced capital and liquidity standards and resolution planning obligations, have made our financial system safer and more resilient. As these rules were being implemented over the past few years, we learned that certain improvements can be made, which is why the regulators continue to review and tweak them as warranted.

Today, the largest banks are subject to many levels of oversight. On-site examiners are in these banks every day, ensuring the banks are engaged in prudent risk management and have proper internal controls in place. In addition, these banks are subject to a complex framework of regulations, including standardized and advanced risk-based capital standards, market-risk capital standards, global systemically important bank (G-SIB) capital surcharges, leverage ratios, supplementary leverage ratios, enhanced supplementary leverage ratios, liquidity coverage ratios, long-term debt requirements, stress testing, and mandatory clearing and margin requirements for derivatives. In addition, these banks are subject to the Federal Reserve Board's Comprehensive Capital Analysis and Review (CCAR) exercise.

One of the post-crisis reforms that has been most challenging to implement for regulators and industry is the Volcker Rule, which restricts banks from engaging in proprietary trading and from owning hedge funds and private equity funds. In fact, the rule has turned out to be so complex that it required 21 sets of frequently asked questions (FAQs) issued by the regulators within three years of its adoption. Distinguishing between what qualifies as proprietary trading and what does not has proven to be extremely difficult. Meanwhile, banks that do relatively little trading are required to go through substantial compliance exercises to ensure that activities that have long been considered traditional banking activities do not run afoul of the Volcker Rule.

The amendments the Board will vote on today seek to address these issues. The amendments will provide more clarity, certainty, and objectivity around the Volcker Rule, while tailoring the requirements to focus on those banks that conduct the overwhelming majority of trades.

Under the final rule, firms with a significant level of trading activity will remain subject to the most stringent compliance requirements, while those firms with lower amounts of trading activity will be subject to tiered compliance programs. The agencies estimate that banking entities classified as having significant trading activity hold approximately 93 percent of the trading assets and liabilities in the U.S. banking system, or approximately 99 percent if combined with the trading assets and liabilities of those banking entities classified as having moderate

trading activity. The final rule thus reflects the fact that the overwhelming majority of activity covered by this final rule is conducted by relatively few banks.

The final rule also simplifies and clarifies which activity is covered by the rule, including through amendments to the definition of the trading account. Banks that are subject to the market risk capital rule would not also be subject to the short-term intent prong. The market risk capital prong covers positions that introduce market risk resulting from trading activities, and, as noted by the 2013 final rule implementing the Volcker Rule, the definition of covered positions under the market risk capital rule “largely parallels” the statutory Volcker Rule definition and “mirrors the short-term trading account prong of both the proposed and final rules.”

Banks that are not subject to the market risk capital rule would have the option to elect to apply the market risk capital prong, or alternatively would be subject to a modified short-term intent prong. These modifications to the short-term intent prong are designed to better reflect the statutory prohibition on proprietary trading.

The existing short-term intent prong, which relies on a rebuttable presumption, is very difficult to apply in practice. As such, banks have found it technically difficult to rebut the presumption that positions held for less than 60 days constitute proprietary trading, which has resulted in many activities that do not constitute proprietary trading being captured by the rule. One such example is error trades – transactions to correct or undo an erroneous trade. The final rule also excludes certain common banking activities, such as the hedging of mortgage servicing rights, from the scope of covered activity.

While we are making important fixes to the proprietary trading and compliance provisions of this rule today, there is more work to be done. Additional fine tuning is necessary on the restrictions associated with covered funds, and we plan to make such changes through a future rulemaking.

I recognize that trading activities can present unique risks to insured institutions, and the FDIC will continue to work with our fellow regulators to ensure that such risks are managed prudently. At the same time, the final rule we are voting on today will ensure that banks continue to comply with the statutory requirements of the Volcker Rule.

I would like to conclude with words of appreciation to the staffs at the five agencies responsible for the Volcker Rule who worked on this final rule. In particular, I would like to thank the staff of the FDIC for all of their hard work on the improvements made to the Volcker rule since its proposal in October 2011 and finalization in December 2013, including the subsequent interim final rule amendment in January 2014 that required a lot of staff hours over the holidays, 21 sets of FAQs issued in the three years following its adoption, the changes mandated by S. 2155, and finally the changes that are before us today. Only those who have spent countless hours on these revisions and clarifications understand the amount of work and analysis that went into the final rule before the Board today. I would personally like to thank you for all the hard work and professionalism throughout this process.