efama
European Fund and Asset Management Association

October 17, 2018

VIA ELECTRONIC DELIVERY

Office of the Comptroller of the Currency
250 E Street, S.W.
Washington, DC 20219

Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, N.W.
Washington, D.C. 20551

Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Securities and Exchange Commission
100 F Street, N.E.
Washington DC 20549

Commodities Futures Trading Commission
1155 21st Street, N.W.
Washington DC 20581

Re: ***Proposed Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds (the "Proposal):*** Comments on OCC Docket No. OCC-2018-0010 and RIN 1557–AE27; FRB Docket No. R-1608 and RIN 7100–AF 06; FDIC RIN 3064–AE67; SEC Release No. BHCA-3; File No. S7–14–18 and RIN 3235–AM10; and CFTC RIN 3038–AE72

Questions Addressed: 12 -21 (Banking Entity Status); 140 – 154 (Foreign Public Fund Exclusion from Covered Fund Status); and 123 – 130 (TOTUS Exemption Requirements)

Dear Ladies and Gentlemen:

This letter is respectfully submitted by the European Fund and Asset Management Association ("EFAMA") [1] in response to a request by the Office of the Comptroller of the Currency ("OCC"),

[1] EFAMA is the representative trade association for the European investment management industry at large. EFAMA was founded in 1974 under the name "European Federation of Investment Funds and Companies" ("FEFSI" was its French acronym) and changed its name to EFAMA in 2004 to reflect a focus on representing the interests of European investment funds and asset management firms, as well as those of national industry trade associations.

Today, EFAMA represents 28 member associations, 62 corporate members and 25 associate members who collectively manage over EUR 25 trillion in assets, of which EUR 15.6 trillion is managed by 60,174 investments funds as of the end of December 2017. The contributing national associations are located in Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Liechtenstein, Luxembourg, Malta, Netherlands, Norway, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, Switzerland, Turkey and the United Kingdom. EFAMA's corporate members include large and mid-sized asset managers located in Europe, including European affiliates of a number of major U.S. asset management groups.

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Board of Governors of the Federal Reserve System ("Board"), Federal Deposit Insurance Corporation ("FDIC"), U.S. Securities and Exchange Commission ("SEC"), and Commodity Futures Trading Commission ("CFTC") (individually, an "Agency," and collectively, the "Agencies") for comments regarding the Proposal, which seeks to amend the regulations (the "Regulations") implementing Section 13 of the Bank Holding Company Act ("BHC Act"), commonly known as the Volcker Rule.[2]

Reflecting the Agencies' belief that supervision and implementation of the Regulations can be substantially improved and concerns that parts of the Regulations may be unclear and potentially difficult to implement in practice, the Proposal seeks to amend the Regulations in order to provide, among other things, greater clarity and certainty about what activities are prohibited. Based on almost 4 years of experience with the Regulations, the Agencies seek to simplify and tailor the Regulations to increase efficiency, reduce excess demands on available compliance capacities and to allow banking entities more efficiently to provide services to their clients consistent with the requirements of the Volcker Rule.

EFAMA applauds the Agencies' initiative and welcomes the opportunity to comment on the Proposal. Although broadly supportive of the Proposal's objective to improve and streamline the Regulations, EFAMA will limit its comments to those aspects of the Proposal that touch most directly on the asset management activities of, and therefore are of greatest interest to, EFAMA's membership. More specifically, set forth below are EFAMA's views on issues relating to (i) the potential banking entity status of investment funds, and particularly non-U.S. investment funds, (ii) the scope of the foreign public fund exclusion from covered fund status, and (iii) the proposed amendments to the requirements for compliance with the TOTUS exemption.

Banking Entity Status of Investment Funds (Questions 12 – 21)

EFAMA believes that it is appropriate to revisit the circumstances under which an investment fund sponsored, advised, managed or owned by a banking entity should itself be treated as a banking entity.

Recommendations.

EFAMA recommends that the Agencies amend the Regulations to provide a general exemption for investment funds from banking entity status, except in circumstances where the investment fund is determined to have been organized in order to permit the banking entity sponsor to engage indirectly in impermissible proprietary trading. Such an exemption would simplify greatly the ability of banking entities to engage competitively in the full range of investment management activities without the burden of a compliance program the benefits of which are far outweighed by the costs.

If the Agencies are unwilling to grant a broad exemption for bank affiliated investment funds in general, EFAMA recommends that the Agencies:

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[2] *See* Proposed Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Covered Funds 83 Fed. Reg. 33,432 (July 17, 2018).

(1) expand (and ideally codify) the current FAQ guidance with respect to seed capital investments in investment companies that are registered ("RICs") with the U.S. Securities and Exchange Commission under the Investment Company Act of 1940 ("1940 Act") and in foreign public funds to also encompass other routine circumstances where a banking entity sponsor may own or control 25% or more of an investment fund's outstanding voting securities; and

(2) exempt from banking entity status foreign excluded funds that are controlled by non-U.S. banking entities as part of their bona fide asset management activities, liquidity management, regulatory requirements (such as LCR in the EU) or in connection with bona fide customer-facing derivatives activities or other similar hedging purposes.

Rationale for EFAMA Recommendations.

The key term underlying the Volcker Rule and the Regulations is that of a "banking entity" to which the prohibitions and restrictions on proprietary trading and sponsoring or investing in hedge funds and private equity funds will apply absent an exemption or exclusion. The term banking entity is defined broadly to include not only FDIC-insured depository institutions, their holding companies and foreign banks that are treated as bank holding companies for purposes of Section 8 of the International Banking Act, but also any affiliate or subsidiary of such an entity. Affiliate and subsidiary are similarly defined broadly with the result that any company that controls, is controlled by or is under common control with, a banking entity will be deemed to be a banking entity absent an exemption or exclusion.

For this purpose, control is determined under the BHC Act, which provides that a company has control over another company if: (A) the company directly or indirectly or through one or more other persons owns, controls, or has the power to vote 25% or more of any class of voting securities of the other company; (B) the company controls in any manner the election of a majority of the directors or trustees of the other company; or (C) the Board determines, after notice and opportunity for hearing, that the company directly or indirectly exercises a controlling influence over the management or policies of the other company. The Board has also consistently ruled that the general partner of a limited partnership controls the partnership and the managing member of a limited liability company controls the limited liability company.

The net result of these broad definitions is that many, if not most, investment funds, both in the United States and in Europe, are at risk of being deemed to be controlled by their banking entity sponsor, investment adviser or investment manager due to their organizational and governance structure, and, thus, deemed banking entities subject to the Volcker Rule's restrictions on proprietary trading. Since investment funds are organized for the express purpose of investing in securities, deeming an investment fund that is controlled by a banking entity to itself be a banking entity would effectively prevent that investment fund from achieving its purpose and deny investors in the investment fund the opportunity to benefit from the banking entity sponsor, investment adviser or investment manager's investment advisory services and expertise. EFAMA respectfully submits that such a result was neither intended nor required by the Volcker Rule.

In this respect, we note that the Agencies recognized the negative and unintended consequences that banking entity status would have on covered funds and, in order to avoid those consequences, provided in the Regulations an express exclusion for covered funds from the definition of banking entity. Unfortunately, although EFAMA and other commenters had at that time requested a broader, more general exclusion for investment funds, the Agencies limited the exclusions from banking entity status to covered funds, merchant banking and SBIC portfolio company investments and the FDIC in its corporate capacity as conservator or receiver.

The Agencies' decision to not include a broader exclusion for investment funds appears to have been based in part on the Board's prior experience and interpretive guidance relating to the mutual fund activities of bank holding companies, including those circumstances where an investment adviser subsidiary of a bank holding company might be deemed to have control over the mutual funds it advises. Although that prior experience did indicate that an investment adviser to a RIC registered under the 1940 Act would ordinarily not be deemed to control the fund and that the fund would not be considered a banking entity, there remained substantial uncertainty about the status of non-U.S. investment funds that were not subject to the 1940 Act and also about the impact of seed capital investments on the control analysis. These uncertainties eventually led the Agencies to release FAQ 14 (with respect to the banking entity status of foreign public funds) and FAQ 16 (with respect to the impact of seed capital investments on the banking entity analysis for RICs and foreign public funds), which provide some, but not complete, relief on the banking entity issues for those types of investment funds. The primary class of investment funds for which no relief from the banking entity status concerns has yet been provided is that of foreign excluded funds, i.e., investment funds organized outside the United States by non-U.S. banking entities that are offered and sold only to non-U.S. investors.

A general exclusion for investment funds is appropriate for many reasons. Perhaps most importantly, such an exclusion would be consistent with the distinction made throughout the Volcker Rule between a banking entity's activities as principal, i.e., for its own account, and a banking entity's activities as fiduciary or agent for its customers. As a general principle, only when a banking entity is acting as principal do the proprietary trading and covered fund restrictions of the Volcker Rule apply. Extending that general principle to investment funds, a clear distinction can be drawn between traditional operating company affiliates or subsidiaries through which a banking entity indirectly conducts the banking entity's own activities, and investment funds where the banking entity investment manager exercises control over the investment fund for the benefit of the investors in the investment fund and not for the benefit of the investment manager. In the former situation, the banking entity is acting in a principal capacity, and the activities of the affiliate or subsidiary reasonably should be attributed to, and subject to the same limitations as the activities of, the controlling banking entity. By contrast, in the latter situation where the banking entity is acting in a fiduciary capacity, subjecting the fiduciary client (i.e., the investment fund) to the limitations on the banking entity's activities is unnecessary and inappropriate.

A general exclusion for investment funds also would restore the presumption that banking entities' asset management activities are, with the exception of those activities relating to the sponsorship or investment in covered funds, not restricted by the Volcker Rule. An important additional

justification for implementing such an exclusion is that it would eliminate the need to develop costly compliance structures to assure that an investment fund does not inadvertently become a banking entity.

As evidenced by the exclusions provided in the Regulations for covered funds and merchant banking investments, the Agencies have ample authority to provide an exclusion for investment funds from banking entity status. Although the need for such an exclusion was especially compelling for covered funds, the policy justification for excluding investment funds is substantially similar to that for excluding merchant banking portfolio company investments – namely, that the Volcker Rule did not intend to limit the activities of such affiliates of a banking entity.

If the Agencies are nevertheless unwilling to grant a broad exemption for bank affiliated investment funds in general, more tailored relief for foreign excluded funds is needed. At a minimum, EFAMA recommends that the Agencies exempt from banking entity status those foreign excluded funds that are controlled by non-U.S. banking entities as part of their bona fide asset management activities, liquidity management, regulatory requirements (such as LCR in the EU) or in connection with bona fide customer-facing derivatives activities or other similar hedging purposes. This could easily be accomplished by making permanent the temporary relief provided to foreign excluded funds by the FRB, FDIC, and OCC in a statement released on July 21, 2017. This relief provides that foreign excluded funds would not be treated as banking entities under the Volcker Rule and the Regulations, and that the Agencies would not attribute those funds' activities to their controlling banking entity during the one-year period ending July 21, 2018, which period was extended until July 21, 2019 in connection with the Proposal.

EFAMA believes that the justification for excluding foreign excluded funds from banking entity status is especially compelling because Congress expressly sought to limit the extraterritorial impact of the Volcker Rule. Moreover, since none of the Agencies otherwise has a bona fide interest in regulating the offshore fund activities of the asset management affiliates of non-U.S. banking entities, EFAMA strongly recommends that, regardless of the outcome with respect to the general exclusion for investment funds, the Agencies exclude foreign excluded funds from the definition of a banking entity.

Theoretical concerns that a non-U.S. banking entity might rely on such a general exclusion to indirectly engage in impermissible proprietary trading or covered fund activities are, in EFAMA's view, largely misplaced. As an initial matter, non-U.S. banking entities have engaged in these same types of asset management activities for years and should not be presumed suddenly to be engaging in them in an effort to avoid the Volcker Rule. In any event, the Regulations' general anti-evasion restrictions would permit the Agencies to limit any such activity were it to occur.

In the absence of a broad exemption for bank affiliated investment funds, EFAMA also recommends that the Agencies expand the existing guidance in FAQs 14 and 16 to also encompass routine circumstances outside the initial seeding period where a banking entity sponsor may own or control 25% or more of an investment fund's outstanding voting securities. Such circumstances would include scenarios where the investment manager owns all of an investment fund's voting securities, and investors own only non-voting securities, as well as situations where an investment

adviser's percentage ownership of an investment fund's voting securities increases due to the redemption activities of investors.

Foreign Public Fund Exclusion from Covered Fund Status (Questions 140 – 154)

Recommendations.

EFAMA recommends that the Agencies amend the "foreign public fund" exclusion from the definition of covered fund to more closely align the treatment of UCITS and other regulated, non-U.S. funds for purposes of the Volcker Rule with the treatment of U.S. investment companies registered under the 1940 Act. Although the existing exclusion for foreign public funds seeks to achieve that result, the very specific and detailed requirements for a foreign fund to qualify for the exclusion, which do not apply to U.S. registered investment companies, significantly undermine this intent, are unnecessarily limiting and effectively place non-U.S. funds at a competitive disadvantage to U.S. registered investment companies.

Conditions that should be eliminated include the requirement that the foreign public fund be sold primarily (i.e., at least 85%) to non-U.S. investors as well as the requirement that the fund must be available to retail investors in the jurisdiction where the fund is organized. Not only is the 85% requirement difficult if not impossible to assure given the heavily intermediated nature of most fund sales, there are no comparable restrictions on sales of U.S. investment companies registered under the 1940 Act. Similarly, although the regulatory regime established by the 1940 Act is designed to and does provide significant protections to U.S. retail investors, there is no requirement that U.S. registered investment companies actually be made available to retail investors. Moreover, it is very common for UCITS funds to be organized in one jurisdiction, but offered primarily for public sale in other jurisdictions and not in the home jurisdiction for tax, marketing and other reasons.

TOTUS Exemption (Questions 123 – 130)

EFAMA strongly supports the Agencies' proposed amendments to the exemption from the Volcker Rule's proprietary trading restrictions for activities that take place solely outside the United States. The experience of EFAMA's members has been that the current requirements with respect to trading by a non-U.S. banking entity with a U.S. counterparty are impractical and have limited the ability and willingness of non-U.S banking entities to rely on the TOTUS exemption. EFAMA would emphasize, however, that adoption of the proposed improvements to the functioning of the TOTUS exemption would not eliminate the need for an exemption for foreign excluded funds from the definition of banking entity.

On a related point, EFAMA notes that one of the conditions for reliance on the TOTUS exemption with respect to proprietary trading activities (as well as the SOTUS exemption for covered fund activities) of non-U.S. banking entities, is that the "banking entity (including relevant personnel) that makes the decision to" engage in the proprietary trading or covered fund activities "is not located in the United States or organized under the laws of the United States or of any State." Confirmation that this requirement does not limit the ability of a non-U.S. banking entity relying

on these exemptions to delegate investment authority to non-affiliated U.S. investment advisers would further clarify and render more useful the TOTUS and SOTUS exemptions.

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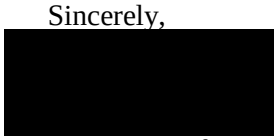
In closing, EFAMA appreciates very much the opportunity to comment on the Proposal and Agencies' willingness to consider improvements to the Regulations relating to the banking entity status of investment funds and the scope of the covered fund exclusion for foreign public funds. These issues are of great importance to EFAMA's membership and EFAMA would be happy to answer any questions and provide further information in support of its recommendations.

Sincerely,



Peter De Proft
Director General