AFG COMMENTS

Dear Ladies and Gentlemen:

AFG is very grateful to the Office of the Comptroller of the Currency, Treasury, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation and the Securities and Exchange Commission (the Agencies) for their public consultation on Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds. Indeed, many non-US investment management industries are deeply concerned by the unintended very harmful impact the implementing rules of the Dodd Frank Act (DFA) may have on them.

The Association Française de la Gestion financière (AFG) represents the France-based investment management industry, both for collective and discretionary individual portfolio management. Our members include 419 management companies, which are entrepreneurial or belong to French or foreign banking or insurance groups, as well as 554 SICAVs.

AFG members currently manage more than 2,600 billion euros (funds and/or discretionary mandates), making the French industry the leader in Europe in terms of financial management for collective investment (with 1,300 billion euros managed, i.e. 20% of all EU investment funds assets under management) and second at worldwide level after the US. In the field of collective investment, our industry includes – beside UCITS – employee savings schemes and products such as regulated hedge funds, funds of hedge funds as well as private equity funds and real estate funds.
AFG is of course an active member of the European Fund and Asset Management Association (EFAMA) and of the European Federation for Retirement Provision (EFRP). AFG also is a member of the International Investment Funds Association (IIFA).

In particular, before we develop our own comments below, we wish to stress that we actively contributed to the EFAMA response to the present consultation, that we fully support and share.

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The purpose of the present letter is to bring to the attention of the Agencies the main concerns of our members relating to the potentially very harmful impacts of the Volcker Rule on them.

Generally speaking, our members are most concerned about the unintended consequences and uncertainties of the Rule.

We understand that the Agencies cannot deviate from the requirements of the Dodd Frank Act that was adopted by the Congress and promulgated by President Obama. However, we respectfully request the Agencies to implement this Act in a proportionate way, in order not to exacerbate its negative impacts on non-US players.

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1. The scope of “covered funds” should be narrowed

We understand that the Volcker Rule covers all funds but US mutual funds. However, in our view, it would make sense that non-US funds similar to US mutual funds and which are strictly regulated are also exempted. Indeed, we believe that, in order to ensure a fair level playing field vis-à-vis US investors, both European ‘UCITS’ - which are regulated by the UCITS European Directive - and nationally regulated funds that are ‘UCITS like’ and similar to US mutual funds (according to their structure, third-party investors, distribution characteristics, underlying investments and other relevant characteristics) should be taken out of the scope of “covered funds”.

The definition of “covered fund” already reaches beyond the suggestions set out in section 619 of the Dodd Frank Act. Indeed, the Agencies added the following provision at section _-.10(b)(1) of the Proposed Rule:

> Any issuer, as defined in section 2(a)(22) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(22)), that is organized or offered outside of the United States that would be a covered fund as defined in paragraphs (b)(1)(i), (ii), or (iv) of this section, were it organized or offered under the laws, or offered to one or more residents, of the United States or of one or more States.

**AFG response to question 224:**

The Agencies ask in question 224 of their consultation whether the Proposed Rule's “language on non-U.S. entities correctly describe[s] those non-U.S. entities … that should be included in the definition of ‘covered fund’”.

To this question, AFG answer is ‘no’.

**AFG response to question 294:**

The Agencies ask whether the foreign funds exemption is “consistent with respect to national treatment for foreign banking organizations”.

For the reasons given below, AFG answer here also is ‘no’. The Agencies commented that:

> These entities have been included in the proposed rule as “similar funds” given that they are generally managed and structured similar to a covered fund, except that they are not generally subject to the Federal securities laws due to the … fact that they are not organized in the United States or one or more States.
As a result of the Proposed Rule, we would have a world where banking entities may sponsor and invest in U.S. mutual funds but may not generally sponsor or invest in UCITS or other strictly regulated foreign investment funds that are structured in accordance with local requirements for retail investors and are in their principles similar to US mutual funds. A European bank that is a “covered banking entity” would be left with no option other than organizing and offering UCITS either in accordance with the foreign funds exemption or generally in compliance with the Proposed Rule’s conditions for sponsoring and investing in covered funds. Application of the Proposed Rule could therefore, contrary to its stated aim, prevent asset management subsidiaries of some non-US banking groups from engaging fund investment and sponsorship activities that would otherwise be allowed under local law. Conversely, the Proposed Rule allows sponsorship of US mutual funds, which makes the current proposal unfair and outreaching compared to what is intended.

This result, which could attain in any non-U.S. jurisdiction with a regulated funds regime, highlights the extent to which the Proposed Rule encroaches on (and creates potential layers of redundancy in relation to) foreign regulated funds regimes and illustrates the type of extraterritorial reach that Congress sought to avoid when enacting DFA section 619. Such effects would be completely paradoxical, when the initial intention was to avoid any unnecessary extraterritorial reach.

It would therefore be appropriate for the Agencies to discuss with foreign regulators to find a clear and objective definition of the funds covered by the Rule.

2. The “foreign funds exception”: the requirement that the activity occurs "solely outside of the United States" should be clarified

2.1 Funds neither offered nor sold to US Residents – request for a “reasonable belief” exemption

AFG response to Question 293: “Should additional requirements be added [to the “solely outside of the United States” requirement]?

AFG answer to the question is yes: the Agencies should add a “reasonable belief” exemption.

We think that a “reasonable belief” exemption (see point on “resident of the US” below) should be introduced. Such an exemption would allow to consider that, provided a fund is not actively targeting or marketed to residents of the US – i.e. through a disclaimer in the fund prospectus and a prohibition of marketing in the written marketing agreements between distributors (including banks) and fund managers, stating that the relevant fund is not intended to be marketed to residents of the US – the relevant entities are not considered as marketing that fund to residents of the US.

In the context of its Rules on the registration of non-US advisers, the Securities and Exchange Commission (SEC) stated in its final rules that “if an adviser reasonably believes that an investor is not in the United States, the adviser may treat the investor as not being in the United States.” (p. 115 of the SEC final rule http://www.sec.gov/rules/final/2011/ia-3222.pdf) and rightly quoted AFG in a footnote, as follows:
“Comment Letter of Association Française de la Gestion financière (Jun. 14, 2011) recommended that investment funds that already are strictly regulated and supervised by European Union regulators should be excluded from the scope of Title IV of the Dodd Frank Act and should not be considered as private funds’ because, among other reasons, the commenter’s management company members very often do not know the identities of their funds’ investors, and therefore should not [] be held responsible if, unbeknownst to them, US persons decide to invest in their funds.”

The Agencies should indeed take into account the fact that European management companies very often:

- either have investors which spontaneously, at their own initiative, invest in the funds they manage: many investors are not solicited at all by management companies. In such case, management companies should not be subject to the Rule as they are not able to control the spontaneous investment by investors in the funds they manage;

- and/or do not even know their ultimate investors, as in many cases funds are sold through chains of intermediaries.

In other words, only active marketing towards a resident of the US should be in the scope of the Rule. Consequently, non-US banking entities which do not intend to market their funds to residents of the US and use official disclaimers in the funds’ prospectus and their distribution agreements should be left out of the scope of the Rule.

Such an exemption would allow non-US covered banking entities to establish procedures to ensure compliance with the Foreign Funds Exemption. Specifically, the Agencies should clarify that a non-US covered banking entity will not be considered to be marketing or selling to residents of the United States if: (1) the non-US covered banking entity is conducting no efforts to market or sell to residents of the Unites States; (2) the fund's selling documentation makes clear that the fund is not offered for sale or sold to U.S. residents and no U.S. resident can subscribe for fund interests; and (3) any agreement between a placement agent and a relevant fund will establish that the placement agent is not authorised to, and will not, contact U.S. residents.

2.2 Further thought should be given to the case of investments by banking entities in funds that become sold or open to residents of the US

A practical solution should be considered for cases whereby a banking entity has made an investment into a fund that is “solely outside of the US” at the time of investment in the fund, which met the exception requirements, and the banking entity received a confirmation or relied on statements in the prospectus or other legal documentation that the fund has not or will not be offered to residents of the US, and the fund later becomes a “covered fund” due to it being marketed to residents of the US, or an interest is transferred to a resident of the US, after the banking entity made its investment. Indeed, the banking entity should not find itself under the obligation to divest from the fund for the sole reason that the latter has become a “covered fund”. The marketing or transfer to residents of the US is out of the control of the investor, that made its investment in good faith and after proper due diligence. A divestment could be significantly detrimental to the banking entity that is forced to sell the illiquid
interest as it may have to sell at a discount and it will have incurred costs on the original due diligence process and also on the transfer.

2.3 Clarification is required on the requirement for a compliance programme for entities relying on the “solely outside of the US” exemption

As currently drafted, it is unclear for us if section 20 the Proposed Common Rules would apply to any exempted activity that is conducted outside of the US by a non-US banking entity. If it were not the case, this would be an unprecedented extension of US regulators’ powers outside the US. This extension would be easily challenged by non US regulators and it is difficult to see what would be the benefit of this extension of powers in terms of safety and soundness of the US markets. We therefore seek clarification on the fact that only US banking entities having activities in the US are subject to section 20 of the Proposed Common Rule.

2.4 Definition of “Resident of the US”

AFG response to Questions 295 and 139

It would make sense if the notion of “resident of the US” used in the Volcker Rule were strictly in line with that of “US person” used in the SEC framework of registration of non-US management companies (Regulation S). Indeed, such an alignment would avoid inconsistencies from one rule to another and facilitate the work of non-US professionals when applying several but complementary parts of US legislation.

Indeed, the different treatment of discretionary accounts under Regulation S and the Proposed Rules could result in significant structural changes to the markets for certain non-U.S. covered funds. In this respect, under Regulation S, a discretionary account with a U.S. adviser held on behalf of a non-U.S. person is considered to be a non-U.S. person, while the Proposed Rule would treat the discretionary account as a U.S. resident, thus prohibiting reliance on the “solely outside of the United States” exception. Accordingly, any non-U.S. covered fund, even a UCITS or other non-U.S. regulated fund, that is managed by a U.S. investment adviser or sub-adviser, will be treated as a U.S. resident under the Proposed Rule, regardless of whether the non-U.S. fund has any U.S. investors, and thus not eligible to invest in a non-U.S. covered fund that is relying on the solely outside of the United States exception. As a practical matter, this means that U.S. investment advisers will be operating at a competitive disadvantage in offering non-U.S. funds of hedge funds that are offered exclusively to non-U.S. investors because they will be denied the opportunity to invest in many of the available non-U.S. hedge funds which are managed by non-U.S. banking entities. In addition, non-U.S. banking entities that offer non-U.S. covered funds will be denied access to the investment capital of such funds of hedge funds solely because they are managed by a U.S. investment adviser.

3. Restrictions relating to fund sponsoring should be clarified

3.1 Prohibitions on the use of banks’ names by funds should be clarified

It does not seem clear to which extent the use of the name of the banking group, or the one of an affiliate or subsidiary of that banking group, in the name of a fund managed by an entity of that group would be prohibited. Such a prohibition would be unfair to non-US funds similar to
US mutual funds (e.g. European UCITS and nationally regulated “UCITS-like” funds – see para.1 above), as the former – i.e. non-US funds similar to US mutual funds – would not be allowed to use the name of the bank in the group of their management company, while the latter – i.e. US mutual funds – would be (as US mutual funds are not in the scope of the Volcker Rule). Of course, this issue would be solved if UCITS and nationally regulated “UCITS like” funds were taken out of the scope of “covered funds”.

3.2 Fund seeding should be allowed over longer periods of time and for higher amounts

The Proposed Rule allows a banking entity to own more than 3% of a fund when setting up a covered fund. We believe that this 3% ceiling should be raised as in practice fund seeding by a banking entity may be above that level.

Moreover, such an ownership interest has to be sold down prior to the 1-year anniversary of the covered fund. This requirement might be difficult to fulfill especially when the assets in the portfolio of the funds are illiquid, for example in the case of private equity funds. We therefore believe that a banking entity should not be penalized if it is unable to sell down to the 3% level within one year. Otherwise, if the banking entity had to sell its ownership interest, it might then become detrimental to the existing investors of the fund by destabilizing the management of the fund. In other words, the Rule should provide for a longer period of time for the banking entity to sell down its ownership in the fund.

AFG response to question 258

A covered fund should not be considered "established" until (a) a private equity fund has reached final close or (b) a hedge fund has reached its target Assets under Management from investors, in each case on the basis that not until this point will a fund's investment restrictions and investment strategy will operate in their intended manner.

Furthermore, a Sponsor should not be penalised if unable to sell down due to illiquidity or market disruption.

Last, we believe that exceptions to the 3% limit to fund seeding should be introduced, in order to allow for larger such investments. Indeed, very often when launching a new fund, it is necessary to ensure a minimum level of liquidity and a critical mass of portfolio to be managed, here again to the ultimate benefit of investors.

3.3 Custody or administration activities of banking entities for affiliated funds should not be considered as sponsorships

Although the proposed rules define “Sponsor”, and custodial services seem not to fall within the scope of this definition, there are some concerns that some custodial arrangements, specifically arrangements where a banking entity acts as a custodian or administrator for an affiliated fund, could be deemed sponsorships of funds. The exception applicable to custody banks that are trustees for “covered funds” but have no investment discretion seems appropriate for US arrangements. However, this exception as currently worded does not seem to apply adequately to custodians outside the US that may act as depositary banks and provide additional fiduciary or administrative services in compliance for instance with the UCITS or AIFM directives: indeed, in such capacity the EU banking entities do not exercise any investment authority or discretion over affiliated fund assets.
As a consequence, the Rule should clarify that custody/depository services should not be considered as sponsoring a fund in cases where custodians/depositaries serve in a directed, fiduciary, or administrative role for any covered fund regardless of whether the covered fund is affiliated or not (notwithstanding the enforcement of Super 23A provision when other circumstances for sponsorship are identified).

More widely, we think that this criterion that the banking entity does not exercise any investment authority or discretion over affiliated fund assets should be applied to all relationships between banking entities and affiliated funds, such as for loans.

Furthermore, we urge the Agencies to exclude custody and settlement arrangements from the definition of “covered transactions”. Indeed, we believe that normal custody and settlement services for covered funds, to the extent that they may be deemed to be provisional credit or liquidity for securities settlement, contractual settlement, pre-determined income or other banking custody-related transactions, should not be qualified as “covered transactions” for the purposes of the so-called Super 23A as these specific kinds of transactions, by their very nature, do not raise a risk of undue credit support for sponsored and advised funds.

### 3.4 The exemption applying to insurance companies regarding proprietary trading should be extended to investment in covered funds

As part of the Proposed Rule, the insurance company exemption - that has been extended to foreign insurance companies - is only applicable to the proprietary trading prohibition and not to the covered fund prohibition.

The prohibition on proprietary trading is designed to avoid banking entities making transactions for speculation purposes and includes a refutable presumption that an investment held for less than 60 days is for such purposes. On the basis of this presumption, we do not find any reason why an insurance company could not have the benefit of the same exemption when it wishes to invest in a covered fund - especially for a period longer than 60 days.

It is crucial to remember that investments made by insurance companies are not economically made for the own account of the insurance company. The money invested by the insurance company, either directly or through covered funds, comes from its policy holders. By no means should these investments be analyzed as engaging the insurance companies’ own money. This is the reason why these investments by insurance companies are not covered by the proprietary trading prohibition and it is also the reason why they should also be excluded from the prohibition to invest in covered funds.

Limiting this exemption to the sole proprietary trading prohibition would have the consequence of forbidding insurance companies to invest in certain types of management and assets that are necessary to hedge and diversify their insurance liabilities.

### 4. Clarification is required on direct or through funds of funds investments

A Banking Entity may invest in covered funds (the Target Funds) directly or via a fund of funds dedicated to it. Our understanding is that the rules applying to a banking entity directly investing in a covered fund also apply to the case of a banking entity investing in a covered...
fund via a dedicated fund, entirely subscribed by such banking entity - even though such
dedicated fund is managed by a third party (or affiliate, as the case may be) manager.

The target Funds are from any and all jurisdictions within Europe and worldwide and active in
all sectors. Whatever the jurisdiction in which a Target Fund is incorporated/located, it is
extremely rare that it is not offered for sale to US residents (even if not actually subscribed by
US residents).

In practice, the prohibition for a Banking entity to invest in a fund which is offered for sale to
US residents results in prohibiting the Banking Entities from pursuing any investment in
private equity or hedge funds, even when those funds have no actual US investors or for a
very insignificant part.

It is crucial to get some flexibility. We therefore suggest:

- To exempt investments in covered funds for insurance companies, on the same terms
  as for proprietary trading (see above).

- Regarding the “solely outside the US” exemption:
  (a) When appreciating the “solely outside the US” : to allow a possibility for US residents
to subscribe so long as the permitted investment by US residents remains below a
percentage of the total interests based on a reasonable belief.
  (b) To Confirm that a Banking Entity which invests in a fund which is not offered or sold
to US residents, but which is organized in the US and/or investing in US companies,
can benefit from the “solely outside the US exemption.
  (c) To allow banking entities to invest in parallel funds the interests of which are
expressly prohibited from being sold to US residents but which co-invest with funds
managed by the same investment team and which interests could be sold to US
residents.
  (d) Regarding grand-fathering: The prohibition forces banking entities to sell their current
investment in dreadful financial conditions. It is crucial (i) that the condition “solely
outside the US” be appreciated exclusively with regards to the actual US investors in
the fund (by opposition to the fact that the fund was potentially offered for
subscription to US residents) (ii) to obtain a threshold of US residents below which the
banking entity could keep its investment and (iii) to allow the banking entities to rely
on a “reasonable belief “ when appreciating the presence of US residents among the
investors of the covered funds.

5. An exemption for national pension schemes and employee saving schemes should be
introduced

AFG response to question 215

In the same way the Agencies provide a specific carve-out for “qualified plans” under IRC
section 401, they should provide as a matter of fairness a carve-out for foreign equivalents of
those plans i.e. for foreign national pension schemes and employee saving schemes such as
the French FCPE (Fonds Communs de Placement d’Entreprise / Employee Savings Funds).
This exemption should apply whether beneficiaries are US residents or not, as employees may change domiciles during their working life.

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*We thank in advance the Agencies very much for taking into consideration our comments and remain available for any further questions. Please feel free to contact myself at +33 1 44 94 94 14 (e-mail: p.bollon@afg.asso.fr), our Head of International Affairs Division, Stéphane Janin, at +33 1 44 94 94 04 (e-mail: s.janin@afg.asso.fr), or his deputy Carine Delfrayssi at +33 1 44 94 96 58 (e-mail: c.delfrayssi@afg.asso.fr).

Yours sincerely,

(Signed)

Pierre Bollon