CENTER FOR CAPITAL MARKETS COMPETITIVENESS

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November 7, 2013

The Honorable Ben Bernanke
Chairman
Board of Governors of the
Federal Reserve
20th Street and Constitution Avenue
Washington, DC 20551

The Honorable Martin Gruenberg
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

The Honorable Mary Jo White
Chair
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

The Honorable Thomas Curry
Comptroller of the Currency
250 E Street, SW
Washington, DC 20219

The Honorable Gary Gensler
Chairman
Commodity Futures Trading
Commission
Three Lafayette Center
1155 21st Street, NW
Washington, DC 20581

Re: Prohibitions and Restrictions on Proprietary Trading and Certain Interests in and Relationships With, Hedge Funds and Private Equity Funds. Docket ID OCC-2011-0014, RIN 1557-AD44; Docket No. R-1432, RIN 7100 AD 82; RIN 3064-AD85; Release No. 34, RIN 3235-AL07; File Number S7-41-11.

Dear Chairman Bernanke, Chairman Gruenberg, Chair White, Comptroller Curry, and Chairman Gensler:

The U.S. Chamber of Commerce ("Chamber") is the world's largest business federation representing the interests of over three million companies of every size, sector and region. The Chamber created the Center for Capital Markets

Competitiveness ("CCMC") to promote a modern and effective regulatory structure for the capital markets to fully function in a 21st century economy. The CCMC welcomes the opportunity to provide input and comment on the proposed rule, ***Prohibitions and Restrictions on Proprietary Trading and Certain Interests in and Relationships With, Hedge Funds and Private Equity Funds*** ("the Volcker Rule Proposal") issued by the Board of Governors of the Federal Reserve ("Federal Reserve"), Federal Deposit Insurance Corporation ("FDIC"), Securities and Exchange Commission ("SEC"), Office of the Comptroller of the Currency ("OCC"), and the Commodity Futures Trading Commission ("CFTC") (also collectively "the regulators").

The CCMC has previously written[1] comment letters expressing concerns that the Volcker Rule, as proposed, will have far reaching, negative consequences. Most importantly, the Volcker Rule proposal will impede the ability and increase the cost of non-financial businesses to raise capital and manage risk.

The CCMC does not see how these concerns can be addressed by any final rule that is a logical outgrowth of the proposed rule that the regulators published for comment. Accordingly, the CCMC respectfully requests that the Volcker Rule be re-proposed before it is finalized as this is the only way to address the fundamental issues raised during and after the comment period and ensure a meaningful opportunity for comment on what must certainly be a substantially altered rule that may itself result in unintended consequences that are of a different nature and magnitude than the many fundamental issues raised by the initial Volcker Rule Proposal. These concerns are centered on the following:

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[1] *See* comment letters of October 11, 2011, November 17, 2011, December 15, 2011, January 17, 2012, February 13, 2012, February 14, 2012, February 21, 2012, April 16, 2012, November 16, 2012 and September 25, 2013 from the U.S. Chamber of Commerce to the regulators and FSOC.

I. Deficiencies with the Cost-Benefit Analysis;

II. Fundamental Issues Raised During the Comment Period for Which Any Proposed Solution Requires Public Comment to Avoid Serious Unintended Consequences, specifically:

- **In releasing the proposed Volcker Rule, regulators have failed to take into consideration the adverse impacts the proposal will have on the ability of companies to raise capital;**
- **The Volcker Rule Proposal will force commercial companies that own banks to build and maintain compliance programs though they have never engaged in proprietary trading;**
- **The Volcker Rule Proposal creates ambiguity as to permissible market making and underwriting, thereby increasing risk and reducing liquidity for companies;**
- **The Volcker Rule Proposal places the American economy at a competitive disadvantage and may in fact violate existing trade agreements; and**
- **The Volcker Rule Proposal may endanger infrastructure projects and the businesses that work on them by impacting the ability of State and Municipal governments and agencies to raise capital;**

III. Issues that have Arisen Following the Comment Period that Need to be Considered in any Final Rule and Weigh in Favor of a Re-proposal;

IV. The Complexity of the Volcker Rule and the Burdens Imposed Upon the Business Community; and

V. Implementation Issues.

The release of the Volcker Rule as an interim final rule would not address these concerns.

Discussion

On January 21, 2010, President Barack Obama proposed a ban on proprietary trading and named it after former Federal Reserve Chairman Paul Volcker, its chief architect. The Volcker Rule was eventually made a part of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").

On October 11, 2011, the Board of Governors of the Federal Reserve, FDIC, SEC, and OCC voted to release a joint Volcker Rule proposal. This joint rulemaking, encompassing 298 pages and over 1,200 questions, was published in the *Federal Register* on November 7, 2011. The CFTC voted to release its version of the Volcker Rule Proposal on January 11, 2012, almost 90 days after similar action by the Federal Reserve, FDIC, SEC, and OCC.

While much of the focus of the legislative language and regulatory implementation of the Volcker Rule has been concentrated on the financial sector, little attention has been paid to the impact that this proposal will have on capital formation for non-financial companies. Indeed, for the full impacts of the Volcker Rule to be understood, one must consider the proposal in conjunction with proposed derivatives regulations and their impact upon end-users, the potential reduction in the utility and viability of money market funds expected to result from the pending proposals issued by the SEC, the impact on commercial lending by proposed credit

risk retention rules, and new lending and liquidity standards required by the Basel III capital accords.

For non-financial companies, any one of these changes will cause the cost of capital to rise. The cumulative impact of all of these impending changes plus the Volcker Rule is that many firms, particularly smaller ones, will likely be completely shut out of capital markets. Others may not be able to access bank lending or find they are unable to adequately hedge risk in certain circumstances. This will make the overall economy less stable and less conducive to growth

1. Deficiencies with the Cost-Benefit Analysis

The regulators have failed to submit for public analysis and comment any meaningful empirical or cost benefit analysis to determine the adverse effects to market liquidity of the proposed regulations.[2] This defies congressional intent. Congressman Barney Frank, in fact, stated in a congressional hearing on the Volcker Rule that cost benefit analysis "has to be applied" to the Volcker Rule Proposal.[3] The Volcker Rule proposal's shortcoming in this regard would appear to violate several applicable legal requirements and underscores the concern that the proposed regulations will have a dramatic negative effect on the financial markets.

Among other requirements, the SEC is statutorily required to consider the effects of certain rules on "efficiency, competition, and capital formation." These required considerations—particularly the effects on "capital formation"—are critical in connection with this rulemaking given the fundamental role that market making and related activities have on market liquidity and the efficiency of the capital markets. In discharging these responsibilities, the SEC must "determine as best it can the

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[2] *See* letter of December 15, 2011 from the CCMC to the Federal Reserve, FDIC, OCC and SEC.
[3] *Joint Hearing on the Volcker Rule before the House Financial Services Subcomm. on Capital Markets and Government Sponsored Enterprises and the Subcomm. on Financial Institutions and Consumer Credit* (Jan. 18, 2012) (opening statement of Rep. Barney Frank).

economic implications of the rule it has proposed," *Chamber of Commerce v. SEC*, 412 F.3d 133, 143 (D.C. Cir. 2005), and subject that analysis to public comment, *see Chamber of Commerce v. SEC (Chamber II)*, 443 F.3d 890, 905 (D.C. Cir. 2006).

These effects on capital formation and market liquidity must be examined with more exacting review to better inform the agencies' analysis and to help minimize unnecessary regulatory burdens to companies and unintended consequences for capital formation.[4]

The regulators have provided no analysis of costs and benefits that would result from the proposed regulations. Instead, they have asked the public to provide this analysis. *See, e.g.*, 76 Fed. Reg. at 68,869-70 (asking for comments on the costs and benefits of proposed market making definition without providing any indication of the agencies' views); *id.* at 68,926 ("We seek comment on whether, in order to comply with the statutory prohibition on proprietary trading, some banking entities may be inclined to abstain from some market making activities [and] this could result in reduced liquidity for certain types of trades or for certain less liquid instruments.").[5]

The Federal Reserve, as recently as October 24, 2011, after the release of the Volcker Rule proposal was voted on, and before it was published in the Federal Register, wrote a letter to the Government Accountability Office acknowledging the need to engage in a cost-benefit analysis and how the Federal Reserve's use of such an

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[4] Ibid, testimony of Anthony Carfang that non-financial businesses may have to increase cash reserves by $1 trillion to manage the impacts of the Volcker Rule Proposal. An increase in cash reserves of this magnitude would have adverse consequences upon business operations and economic growth.

[5] Ibid; *Joint Hearing* at 46-47 (Chairman Schapiro and Mr. Turner, in response to question by Rep. Gutierrez, asserting that agencies have requested commenters to provide pertinent economic analysis).

analysis, since 1979[6], has mirrored the provisions of regulatory reform as articulated in Executive Order 13563.[7]

The agencies cannot rely on the cost-benefit analyses submitted by commenters in promulgating a final rule because they have not been subject to public comment. *See Chamber II*, 443 F.3d at 899-901. And as noted above, new developments since the comment period closed dramatically alter any such analyses the agencies received. The opportunity for the public to review, comment upon, and inform the analysis underlying an agency's action is, of course, the essence of notice and comment rulemaking under the Administrative Procedure Act. *See id.* (public was entitled to notice of and an opportunity to comment on certain materials underlying the agency's analysis); *Engine Mfrs. Ass'n v. EPA*, 20 F.3d 1177, 1182 (D.C. Cir. 1994) (invalidating rule because materials provided to public were too "opaque" and "[t]here [was] no way to know the agency's methodology from what little it reveal[ed] in the cost analysis"); *Prometheus Radio Project v. FCC*, 652 F.3d 431, 447-53 (3d Cir. 2011) (vacating and remanding an FCC rule because the FCC released "several additional peer review comments, 'revised' versions of four of the studies, and new peer review studies" on the last day for comments). Whether the agencies develop a more robust economic analysis on their own to inform their regulatory determinations, or through submissions by commenters, they must re-propose the rule with that additional analysis. *See Portland Cement Ass'n v. Ruckelshaus*, 486 F.2d 375, 393 (D.C. Cir. 1973).

The Volcker Rule Proposal also fails to satisfy other cost-benefit requirements that apply to the rulemaking. For example, the Regulatory Flexibility Act, 5 U.S.C. § 601 *et seq*. ("RFA"), "imposes procedural requirements on agency rulemaking, in particular the preparation of a 'final regulatory flexibility analysis' regarding the effect of the rule on small businesses," *United States Telecom Ass'n v. FCC*, 400 F.3d 29, 42

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[6] Board of Governors of the Federal Reserve System, Statement of Policy Regarding Expanded Rulemaking procedures, 44 Fed. Reg. 3957 (1979)

[7] *See* letter from Scott Alvarez, General Counsel of the Federal Reserve, to Nicole Clowers, Director of Financial Markets and Community Investment of the General Accountability Office.

(D.C. Cir. 2005) (quoting 5 U.S.C. § 604), unless the agency certifies (accurately) "that the rule will not, if promulgated, have a significant economic impact on a substantial number of small entities," 5 U.S.C. § 605(b). In the Volcker Rule proposal, the agencies state that a RFA analysis is not required because "[t]he proposed rule would not appear to have a significant economic impact on small entities." 76 Fed. Reg. at 68,938.

Similarly, the Unfunded Mandates Reform Act, 2 U.S.C. § 1501 *et seq.* , requires agencies to prepare a budgetary impact statement for any rule likely to result in expenditures by state and local governments and private actors of $100 million or more annually. *Id.* § 1532. The OCC determined that these cost thresholds would not be exceeded under the proposed regulations, 76 Fed. Reg. at 68,939, even though the agencies calculated that the recordkeeping and compliance requirements alone will require over 6.5 million man-hours, *id.* at 68,938. Coupled with the significant effects to market liquidity and to the business activities of all companies, the OCC's determination is clearly erroneous and an Unfunded Mandates Reform Act analysis is required.

2. Fundamental Issues Raised During the Comment Period For Which Any Proposed Solution Requires Public Comment to Avoid Serious Unintended Consequences

The Volcker Rule Proposal creates ambiguities as to appropriate market making and underwriting activities that are critical to capital formation for non-financial businesses. As we have commented before[8], the Volcker Rule Proposal is

[8] *See* letters of February 13, 2013 from the CCMC to the Federal Reserve, FDIC, OCC and SEC; February 21, 2012 from Abbott Laboratories, American Insurance Association, Anadarko Petroleum Corporation, Arch Coal, Inc., Association for Financial Professional, Business Roundtable, Caterpillar Inc., Chesapeake Energy Corporation, Convergys, Darden Restaurants, Inc., Devon Energy Corporation, Dominion Resources Inc., DuPont Co., Eaton Corporation, Financial Executives International, FMC, GE, Goodrich, HCA, Macy's, Inc., National Association of Manufacturers, Nissan Motor Acceptance Corporation, Qualcomm Incorporated, Safeway Inc., The

likely to severely curtail these essential capital raising and risk management services and result in the following five major negative consequences for businesses:

- In releasing the proposed Volcker Rule, regulators have failed to take into consideration the adverse impacts the proposal will have on the ability of companies to raise capital;

- The Volcker Rule Proposal will force commercial companies that own banks to build and maintain compliance programs though they have never engaged in proprietary trading;

- The Volcker Rule Proposal creates ambiguity as to permissible market making and underwriting, thereby increasing risk and reducing liquidity for companies;

- The Volcker Rule Proposal places the American economy at a competitive disadvantage and may in fact violate existing trade agreements; and

- The Volcker Rule Proposal may endanger infrastructure projects and the businesses that work on them by impacting the ability of State and Municipal governments and agencies to raise capital.[9]

If these issues are not addressed in a final Volcker Rule, we believe that a complex regulatory structure may force financial institutions to curtail their

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Boeing Company, The Real Estate Roundtable, The U.S. Chamber of Commerce and Yocum Oil Company, Inc to the Federal Reserve, FDIC, SEC, OCC and CFTC; April 16, 2012 from CCMC to CFTC.

[9] These issues are addressed with more specificity in the CCMC's comment letters to the regulators of February 13, 2012 and April 16, 2012.

participation in markets in order to avoid potential violations of the law, or not engage in permissible activities in order to avoid a trade-by-trade regulatory compliance analysis. This could dramatically reduce the marketplace for corporate debt and equities, thereby reducing market liquidity which will cause typical transaction spreads to widen and place the U.S. capital markets at a competitive disadvantage as no other nations are imposing a Volcker Rule.

3. Issues that have Arisen Following the Comment Period that Need to be Considered in any Final Rule and Weigh in Favor of a Re-proposal

Although the comment period on the Volcker Rule Proposal closed on February 13, 2012, developments have occurred that regulators should contemplate and seek comment on before a final Volcker Rule is promulgated.[10]

The Volcker Rule Proposal includes insufficient analysis of the impacts that it could have on companies to which it *will* apply, companies to which it *could* apply and, by extension, on the markets they serve. Two recent developments have created additional concerns about the substance of the Volcker Rule Proposal and the adequacy of the rulemaking process.

First, the Federal Reserve finalized its Proposed Supplemental Rulemaking on the definition of "activities that are financial in nature" ("predominantly engaged test") for purposes of designating non-banks as "Systemically Important Financial Institutions" ("SIFI's"). The rules implementing the predominantly engaged test were finalized on April 3, 2013[11]—almost 14 months after the comment period on the Volcker Rule Proposal closed. Until the predominantly engaged test was finalized, it

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[10] *See* letter of September 25, 2013 from the CCMC to the regulators.
[11] It should also be noted that the rules implementing the predominantly engaged test were re-proposed for comment before they were promulgated.

was not possible to understand which non-bank financial companies are eligible for designation and potentially subject to the Volcker Rule. One collateral impact of the predominantly engaged test is the expansion of the potential universe of non-banks to which the Volcker Rule could apply far beyond the limits envisioned by Congress and by commenters during the original comment period on the Volcker Rule Proposal. Those who may be a part of this universe may have failed to comment initially because they did not think they would be swept into the definition and were acting reasonably at the time based on the clear language of the law.

The CCMC believes that the predominantly engaged test magnifies the scope of the Volcker Rule to a broader array of non-bank financial companies that had no reason to believe that they could be subject to the Volcker Rule and, accordingly, had insufficient notice and opportunity to comment on the Volcker Rule Proposal during the original comment period.

Second, the FSOC has designated the first non-banks as SIFIs. When the Volcker Rule Proposal was issued, the regulators specifically deferred consideration of how Section 619 of the Dodd-Frank Act would apply to designated non-banks because, at the time, the FSOC had not yet finalized the designation criteria, nor had it designated any non-banks.[12] In the absence of a proposal on how the regulators will apply Section 619 to designated non-banks, these companies, as well as those that could be designated in the future, have no information on the requirements that the regulators will impose and have not been given an opportunity to comment on the record.

4. The Complexity of the Volcker Rule and the Burdens Imposed Upon the Business Community

[12] *See* Volcker Rule Proposal, fn 4, pp. 66847-66848.

The sheer size and complexity of the Volcker Rule proposal and the fundamental issues on which it requested comment warrant a re-proposal. The Volcker Rule proposal was more akin to an Advance Notice of Proposed Rulemaking by which an agency seeks information prior to proposing a regulation than it was to an actual, concrete proposal on which substantive comment was being solicited. Additionally, the 17,000 comment letters received not only responded to the basic substantive issues raised by the regulators, they also raised numerous others that the Volcker Rule Proposal did not contemplate. It is not conceivable that the regulators can appropriately address all of the serious issues raised and data presented in the comment process by simply finalizing a rule. The scope and magnitude of any final rule addressing all of these matters would certainly not be a logical outgrowth of the substantive aspects of the Volcker Rule Proposal on which the agencies solicited comment. A second opportunity for comment would be necessary to satisfy the most basic standards of a responsible and informed rulemaking process.

Any final rule that is a logical outgrowth of the Volcker Rule Proposal will place enormous additional costs on businesses and their investors. For instance, the Paperwork Reduction burden estimates for the Volcker Rule, as issued by the regulators, stand at almost 6,600,000 hours per year. It should be noted that such burdens are normally underestimated by regulators. A prime example is the Conflict Minerals proposed rules where the SEC estimated the compliance costs to be $70 million, and that number later rose to $4 billion when it was promulgated. Businesses and even conflict minerals proponents have stated that compliance costs will be even higher than this revised estimate, with some calculating compliance costs as high as $14 billion.

The Volcker Rule Proposal sought comment on whether it was economically significant. It did not even attempt to quantify its impacts on non-financial businesses, such as public companies that issues debt and equity instruments, own a bank, or use derivatives to mitigate risk and cost fluctuations. This is a fundamental flaw in the Volcker Rule Proposal, given that its market making provisions will

obviously impact the ability of non-financial public companies to access debt and equity markets. The Volcker Rule Proposal will also require non-financial companies that own a bank to create Volcker Rule compliance program – even if that bank did not engage in proprietary trading.

5. Interim Final Rule

The CCMC also believes that a re-proposal is a superior procedure to develop a complex rule rather than the issuance of an interim final rule. A re-proposal will allow stakeholders and regulators to appropriately identify potential problems and fix them before a rule is implemented. While an interim final rule allows for additional comment, it will likely force the regulated community to take measures to deal with the negative consequences of the Volcker Rule, much of which cannot be retroactively corrected, and bear the associated transaction costs and dislocations to our economy before all of the consequences can be identified and corrected in a more thoughtful and comprehensive manner.

6. Implementation Issues

Regulations should provide clear rules of the road for businesses and market participants to operate and engage in a rational decision making process for the benefit of their investors and customers. How regulations are enforced is as important in providing the boundaries through which a rational decision making process can occur in the marketplace.

It appears that some of the regulators intend to enforce the Volcker Rule on a subjective touchstone by reviewing activity on a trade by trade basis, while other regulators have indicated that they will enforce the Volcker Rule on an objective footing. These polar opposite means of regulation would in essence create vastly different rules. Such implementation and interpretation differences amongst 5 regulators will cause confusion in the marketplace and wreak havoc on the capital

formation capabilities of businesses. It is important for all stakeholders to have a firm grasp on how the Volcker Rule will be implemented and interpreted amongst 5 regulatory agencies. This is necessary for the markets to react accordingly and for the Volcker Rule to operate effectively.

Conclusion

A failure to understand the implications of the Volcker Rule upon businesses may lead to negative consequences that can hamper the ability of companies to access capital, grow, and create jobs. Accordingly, we request that you re-propose the Volcker Rule in order to thoroughly evaluate the impact of additional regulation on American businesses, the broader economy and stop these negative consequences from occurring. It is more important to get this right than to meet an artificially imposed deadline.

The CCMC stands ready to assist you in that effort.

Sincerely,

David Hirschmann