LA 12-222

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March 16, 2012

Honorable Ben Bernanke
Chairman, Board of Governors
Federal Reserve System
Twentieth and Constitution Avenue, NW
Washington, DC 20551

Honorable Martin Gruenberg
Acting Chairman
Federal Deposit Insurance Corporation
550 Seventeenth Street, NW
Washington, DC 20429

Honorable Gary Gensler
Chairman
Commodities Futures Trading Commission
Twenty First Street, NW
Washington, DC 20581

Honorable Mary Schapiro
Chairman
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Honorable John Walsh
Acting Comptroller of the Currency
U.S. Department of Treasury
250 E Street, SW Room 9048
Washington, DC 20219

Dear Chairman Bernanke, Acting Chairman Gruenberg, Chairman Gensler, Chairman Schapiro, Acting Chairman Walsh:

I respect the difficult task thrust upon the regulators in promulgating the Volcker Rule. As you review the comments you have received and work toward a final rule, I wanted to highlight a colloquy I shared on the House floor with Chairman Frank related to the Volcker Rule's application to wholly owned or controlled subsidiaries and joint ventures used to hold investments.

As you know, hedge funds and private equity funds, now prohibited investments under the statute, have been notoriously difficult to define with any type of bright line rule. The statutory definition begins with a broad category of entities that rely on specific exemptions under the Investment Company Act of 1940, but then provides regulators with significant discretion to tailor that definition as they may determine. I confirmed in that colloquy that in passing the Wall Street Reform and Consumer Protection Act, Congress did not intend the Volcker Rule to deem wholly owned or controlled subsidiaries and joint ventures used to hold other investments as private equity or hedge funds. To do so would disrupt the way that firms structure their normal investment holdings. If those vehicles were included, virtually any corporate subsidiary or affiliate could be prohibited under the rule if it fits within a broad group of entities under the Investment Company Act. This would include many joint ventures, credit funds and even wholly owned subsidiaries, where there is only one investor – entities that are clearly not thought of as traditional private equity or hedge funds.

Companies must be able to form joint ventures and wholly owned subsidiaries in order to engage in ordinary course investing and lending currently allowed by the Volcker Rule and more broadly by Dodd Frank—including making extensions of credit, providing internal funding within an organization, and hedging risk. Such transactions should not be disallowed simply because they are made through a corporate subsidiary. Corporate subsidiaries assure that these normal corporate activities are properly overseen within the larger corporate structure, allow non-affiliated companies to partner to spread risk beyond a single entity, and help reduce the risk any given transaction could cause harm to the entire corporation. Eliminating these structural necessities, therefore, increases, not decreases, risk to the institutions the rule seeks to protect.

The proposed rule does acknowledge this problem and provides some relief, but that relief is insufficient in two respects. First, the exceptions for wholly owned liquidity management subsidiaries cover only a small fraction of the wholly owned subs that would be disrupted. Second, by using exceptions to the prohibition, rather than carving these entities out of the definition itself, the proposed rule subjects these entities to the so called "Super 23A" limitations on transactions with the banking entity. These limitations may render the excepted entities useless – essentially allowing the entity to be maintained, but without permitting the entity from conducting any business transactions back with the larger group.

Further, if the "covered funds" definition remains as proposed, non-financial companies that are covered under the rule due to their affiliation with a banking entity will be impeded by these restrictions. The Volcker rule was designed to limit risks at insured depositories and their holding companies, not at industrial or commercial companies that share an affiliation with depositories.

Accordingly, I encourage you to further define "covered funds" in a way that would specifically exclude all wholly owned subsidiaries and joint ventures used for ordinary course investing and transactions otherwise permitted by the Volcker Rule. Failure to do so could ultimately cause severe disruptions to the same banking system that the rule was designed to protect.

Again, I respect the enormity and the complexity of the task at hand. I encourage you to continue to work with the Congress to assure that the Congressional intent is accurately reflected in any final rulemaking. I appreciate your attention to this matter.

Sincerely,

Jim Himes
Member of Congress