SULLIVAN & CROMWELL LLP

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Volcker Rule

Federal Agencies Propose Amendments to Covered Funds Provisions

EXECUTIVE SUMMARY

Yesterday, the Board of Governors of the Federal Reserve System (the "Federal Reserve"), the Office of the Comptroller of the Currency (the "OCC"), the Federal Deposit Insurance Corporation (the "FDIC"), the Securities and Exchange Commission (the "SEC") and the Commodity Futures Trading Commission (the "CFTC") (collectively, the "Agencies") approved a notice of proposed rulemaking (the "NPR") to amend the regulations implementing the so-called "Volcker Rule" provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").[1]

The NPR proposes a number of targeted amendments to the Volcker Rule regulations, principally focused on the restrictions on "banking entities'" investments in and other relationships with "covered funds." Many of these amendments directly address aspects of the existing regulations that have proven in practice to be complex and burdensome or to have unintended consequences. The NPR aligns with the Agencies' ongoing commitment to tailor and streamline regulation and to ensure that both the benefits and costs of activities restrictions are carefully weighed. The NPR also incorporates and proposes to codify certain interpretive guidance and policy statements previously issued by the Agencies.

Among the most notable proposed amendments are the following:

- Credit funds, venture capital funds, family wealth management vehicles and customer facilitation vehicles would be excluded from the "covered fund" definition, subject to certain conditions and limitations.
- Conditions to qualify for the existing exclusions for foreign public funds, loan securitizations, public welfare investment funds and small business investment companies from the "covered fund" definition would be modified, generally with the effect of clarifying and simplifying compliance with these exclusions.

- The "Super 23A" provisions would be modified to include exemptions permitting certain transactions, including intraday credit extensions and payment, clearing and settlement transactions.
- Banking entities would be provided more flexibility to make investments alongside a covered fund, so long as they do so in compliance with other applicable laws and regulations (including the Volcker Rule's prohibition on proprietary trading and authority requirements under U.S. banking law).

The NPR includes extensive requests for comment, with 87 numbered questions (and multiple sub-questions) that shed light on the Agencies' deliberations leading to the NPR. Comments on the NPR must be received on or before April 1, 2020.

This Memorandum discusses the specific amendments proposed in the NPR and related discussion in the supplementary information accompanying the NPR (the "Preamble"). **Appendix A** provides a comparison of the text of the amended regulations proposed in the NPR (the "Proposed Rule") against the text of the currently effective regulations (the "Current Rule").

OVERVIEW

As implemented by the Agencies' initial final rule adopted on December 10, 2013, the Volcker Rule imposes broad restrictions on, and extensive compliance requirements with respect to, banking entities' ability to (i) engage in proprietary trading and (ii) invest in and sponsor private equity funds, hedge funds and certain other investment vehicles—collectively referred to as "covered funds." Subsequent to the initial final rule, the Agencies amended a number of provisions relating to the proprietary trading restriction, compliance program requirements and applicability of the Volcker Rule to smaller banking entities. These rulemakings included limited changes to the covered funds provisions, but provided extensive questions and requests for comment regarding those provisions, setting the stage for the current NPR.

Key aspects of the NPR and the Proposed Rule are as follows:

A. **New exclusions from the "covered fund" definition.** The following types of entities would be excluded from the Proposed Rule's definition of "covered fund," subject in each case to specified conditions. A banking entity's investment in and relationship with entities that qualify for any of these proposed exclusions would remain subject to the so-called "prudential backstop" limitations, as though the entities were covered funds, and would also be subject to restrictions designed to prevent "bail outs" of such entities.

- ***Credit funds.*** Funds the assets of which consist solely of loans, debt instruments, other assets that are related or incidental to acquiring, holding, servicing or selling loans (including certain equity securities and warrants), and certain interest rate or foreign exchange derivatives. Qualifying credit funds may not engage in prohibited proprietary trading, issue asset-backed securities or engage in any transactions with a sponsoring or advising banking entity that would be prohibited under Super 23A, as though the credit fund were a covered fund.
- ***Venture capital funds.*** Funds that meet the definition of a "venture capital fund" under the SEC's regulations under the Investment Advisers Act of 1940 (the "Advisers Act"), subject to

the conditions with respect to proprietary trading and Super 23A that also apply to credit funds, as described above.

- ***Family wealth management vehicles.*** Trusts the grantors of which are all family customers and certain non-trust entities that are owned by family customers and up to three "closely related persons" of the family customers (*e.g.*, estate planning vehicles and persons with a long-standing business or personal relationship with the family customers).
- ***Customer facilitation vehicles.*** Vehicles formed by, or at the request of, a banking entity's customer in order to provide exposure to a transaction, investment strategy or other service provided by the banking entity, so long as the vehicle is wholly owned by the customer and its affiliates (other than a de minimis amount that may be held by the banking entity).

B. Amendments to existing exclusions from the "covered fund" definition.

- ***Foreign public funds.*** The "home jurisdiction" requirement and the requirement that ownership interests be sold "predominantly" through public offerings would be eliminated. The exclusion would be available so long as the fund's ownership interests are offered and sold through at least one public offering, provided that the distribution is subject to substantive disclosure and retail investor protection laws or regulations in the jurisdiction in which it is made. In addition, with respect to a U.S. banking entity that sponsors a foreign public fund, the fund's ownership interests must be sold predominantly to persons other than the sponsoring banking entity or the issuer, or affiliates of either, and directors and senior executive officers of such entities.
- ***Loan securitizations.*** The Proposed Rule would permit a loan securitization to own non-loan assets of up to five percent of the issuer's total assets.
- ***Small business investment companies.*** The exclusion would remain available during the company's wind-down period, provided that the company makes no new investments after surrendering its license.

C. Investments alongside covered funds by banking entities and their director and employees. Subject to several conditions, banking entities would not be required to treat direct investments alongside covered funds as an investment in a covered fund, so long as the banking entity has independent authority to make such investments. In addition, the Agencies expect that direct investments by directors and employees alongside covered funds would not be required to be counted as investments in covered funds or be subject to the condition that such persons provide services to the relevant fund. As a result, these investments would be not be attributed to the banking entity, even if the banking entity arranged or provided financing for the transaction.

D. Exemptions from Super 23A for certain transactions. The so-called "Super 23A" provisions of the Volcker Rule, which prohibit banking entities from providing extensions of credit to and entering into certain other transactions with advised or sponsored covered funds, would be subject to exemptions to permit certain short-term extensions of credit and purchases of assets in connection with certain payment, clearing and settlement activities, as well as transactions that are exempted from the limitations of Section 23A of the Federal Reserve Act and Regulation W. The amended Super 23A provisions would apply to excluded credit funds and venture capital funds as though they were covered funds.

E. Exclusions from the "ownership interest" definition. Certain senior loans or senior debt instruments of a covered fund would qualify for a safe harbor from treatment as an ownership interest in a covered fund. In addition, a creditor's interest in a covered fund would not be deemed to be an ownership interest solely by reason of having the right to participate in the removal of an

investment manager for cause or to nominate or vote on a nominated replacement manager upon an investment manager's resignation or removal.

F. Permanent relief for qualifying foreign excluded funds. Activities of "qualifying foreign excluded funds," which are non-U.S. funds that are offered solely to foreign investors, would be exempted from both the proprietary trading restrictions and the covered funds provisions under the Current Rule, subject to certain conditions. This provision would make permanent the temporary relief the Agencies have provided with respect to the potential attribution of the activities and investments of certain foreign funds to a foreign banking entity that controls such a fund.

ENDNOTES

[1] The Federal Reserve approved the NPR by a vote of four to one (with Governor Brainard dissenting). Statements by Chair Powell, Vice Chair Quarles and Governor Brainard are available at https://www.federalreserve.gov/newsevents/pressreleases/bcreg20200130b.htm. Commissioner Otting approved the NPR. The FDIC approved the NPR by a vote of three to one (with Director Gruenberg dissenting). Director Gruenberg's statement is available at https://www.fdic.gov/news/news/speeches/spjan3020b.pdf. The SEC approved the NPR by a vote of three to two (with Commissioners Jackson and Lee dissenting). Chairman Clayton's statement is available at https://www.sec.gov/news/public-statement/clayton-volcker-rule-2020-01-30; a joint statement by Commissioners Roisman and Peirce is available at https://www.sec.gov/news/public-statement/roisman-peirce-volcker-rule-2020-01-30; Commissioner Lee's statement is available at https://www.sec.gov/news/public-statement/lee-volcker-rule-2020-01-30. The SEC approved the NPR by a vote of three to two (with Commissioners Behnam and Berkovitz dissenting). Chairman Tarbert's statement is available at https://cftc.gov/PressRoom/SpeechesTestimony/tarbertstatement013020b; Commissioner Behnam's statement is available at https://cftc.gov/PressRoom/SpeechesTestimony/behnamstatement013020b; Commissioner Berkovitz's statement is available at https://cftc.gov/PressRoom/SpeechesTestimony/berkovitzstatement013020.

Table of Contents

I. DEFINITION OF "COVERED FUND"

The Proposed Rule's substantive changes to the definition of "covered fund" fall into two categories, which are described in this Part I. The first category consists of four proposed exclusions for funds that meet specified criteria. The NPR explains that these proposals are based on the Agencies' experience implementing the regulations and have the objective of "address[ing] the potential over-breadth of the covered fund definition."[1] The second category of changes is intended to streamline the eligibility criteria for three existing exclusions from the definition of "covered fund," with the objective of facilitating banking entities' use of, and confirmation of compliance with, these exclusions.

Each of the four proposed exclusions discussed in Part I.A below is subject to the following conditions:

- The banking entity seeking to rely on the exclusion may not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of the issuer or of any entity to which such issuer extends credit or in which such issuer invests (the "Anti-Bailout Requirements");
- The banking entity must provide certain disclosures to actual and prospective investors that parallel those required under the organizing and offering exemptions, including disclosures with respect to the absence of a performance guarantee or insurance and the risk of loss (but with respect to credit funds and venture capital funds, solely if the banking entity serves as the sponsor or adviser to the fund) (the "Required Disclosures");[2] and
- The banking entity's ownership interest in and relationship with the issuer must comply with rules regarding material conflicts of interest, high-risk investments, and safety and soundness and financial stability (such provisions, the "Prudential Backstop").[3]

The Volcker Rule does not restrict banking entities from investing in non-covered funds, unless the investment constitutes prohibited proprietary trading, or from sponsoring or engaging in other relationships with non-covered funds, other than in the case of excluded credit funds and venture capital funds, which would be subject to Super 23A as though they were covered funds, and subject to the application of the Prudential Backstop to issuers that qualify for the new proposed exclusions. However, a non-covered fund that is "controlled" by a banking entity, as defined for purposes of the Bank Holding Company Act of 1956 (the "BHC Act"), would itself be treated as a banking entity and therefore would need to comply with the Volcker Rule's restrictions on proprietary trading and covered fund activities, subject to exceptions for certain types of entities that are neither covered funds nor subject to treatment as banking entities (*e.g.*, qualifying foreign excluded funds, as discussed in Part V below).

I.A. PROPOSED NEW EXCLUSIONS FROM THE DEFINITION OF "COVERED FUND"

I.A.1. Credit Funds

The Proposed Rule excludes from the definition of "covered fund" certain credit funds that make loans, invest in debt, or otherwise extend the type of credit that banking entities may provide directly under applicable banking law.[4] As described further below, qualifying for the proposed exclusion requires that the fund meet certain conditions relating to the composition of its assets and its activities, and any banking entity seeking to rely on the exclusion would need to comply with certain limitations and meet certain requirements with respect to the fund.

- ***Asset requirements.*** A qualifying credit fund's assets must be composed solely of the following:
    - loans (defined as any loan, lease, extension of credit, or secured or unsecured receivable that is not a security or derivative);
    - debt instruments, subject to restrictions discussed below;
    - rights and other assets that are related or incidental to acquiring, holding, servicing, or selling such loans or debt instruments, provided that any such rights or assets may not include any commodity forward contract and may include securities only if they are either (i) a cash equivalent (which means high quality, highly liquid investments whose maturity corresponds to the issuer's expected or potential need for funds and whose currency corresponds to either the underlying loans or debt instruments), (ii) a security received in lieu of debts previously contracted with respect to such loans or debt instruments; or (iii) an equity security (or right to acquire an equity security) received on customary terms in connection with such loans or debt instruments. The NPR notes that the Agencies expect that a specific quantitative limit on equity securities (or rights to acquire equity securities) may be appropriate and are considering imposing such a limit in a final rule;[5] and
    - interest rate or foreign exchange derivatives, but only if the written terms of the derivative directly relate to the loans, debt instruments or other rights or assets described above; and the derivative reduces the interest rate and/or foreign exchange risks related to the loans, debt instruments or other rights or assets described above.[6]

- ***Activity requirements.*** A qualifying credit fund may not engage in any activity that would constitute proprietary trading under the short-term intent prong of the Current Rule[7] or issue asset-backed securities.[8] Issuers of asset-backed securities may be able to qualify for one or more other exclusions from the covered fund definition, including the loan securitization exclusion (certain changes to which were proposed in the NPR, as described in Part I.B.2 of this Memorandum) and exemptions under the Investment Company Act of 1940 (the "Investment Company Act").[9]

- ***Additional conditions.*** In addition to the criteria described above, each of the following conditions must be satisfied in order for a banking entity to rely on the credit fund exclusion to invest in or sponsor any credit fund:
    - the banking entity complies with the limitations set forth in Super 23A with respect to the fund as if it were a covered fund;[10]
    - the banking entity's investment in and other relationships with the fund comply with the Anti-Bailout Requirements and the Prudential Backstop as if such fund were a covered fund;

- the banking entity provides the Required Disclosures to actual and prospective investors in the fund, if the banking entity serves as sponsor or adviser to the fund;
- the banking entity complies with the requirements of Section 23B of the Federal Reserve Act[11] as if the fund were an affiliate of the banking entity;
- the credit fund acquires only loans, debt instruments or equity securities that would be permissible for the banking entity to acquire and hold directly; and
- a banking entity that invests in or has a relationship with the fund continues to be subject to capital charges, safety and soundness standards[12] and other requirements under applicable banking law.[13]

I.A.2. Venture Capital Funds

The Proposed Rule excludes from the covered fund definition any "qualifying venture capital fund," which includes any "venture capital fund," as defined in the SEC's Rule 203(l)-1 under the Advisers Act,[14] that meets certain additional criteria set forth in the Proposed Rule. The criteria for this exclusion are:

- ***"Venture capital fund" under SEC Rule 203(l)-1.*** For purposes of the Advisers Act, a "venture capital fund" is an issuer that:
  - represents to investors and potential investors that it pursues a venture capital strategy;
  - holds no more than 20 percent of aggregate capital contributions and uncalled committed capital in assets other than "qualifying investments"[15]—which generally consist of equity securities of any "qualifying portfolio company" (*i.e.*, most private companies that are not themselves investment vehicles)[16]—or short-term holdings;
  - does not borrow, issue debt obligations, provide guarantees or otherwise incur leverage, in excess of 15 percent of aggregate capital contributions and uncalled committed capital, and any such indebtedness must generally be for a non-renewable term of no longer than 120 calendar days (except that any guarantee by the fund of a qualifying portfolio company's obligations up to the amount of the value of the fund's investment in the qualifying portfolio company is not subject to the 120 calendar day limit);
  - only issues securities that do not provide a holder with any right, except in extraordinary circumstances, to withdraw, redeem or require the repurchase of such securities, but may entitle holders to receive distributions made to all holders pro rata; and
  - is not registered as an investment company under the Investment Company Act, and has not elected to be treated as a business development company.[17]

- ***Additional conditions for "qualifying venture capital funds."*** In order for a venture capital fund that meets the above definition to qualify for the Proposed Rule's exclusion, the following additional conditions must also be satisfied:
  - the fund does not engage in any activity that would constitute proprietary trading under the short-term intent prong of the Current Rule[18];
  - the banking entity complies with the limitations set forth in Super 23A with respect to the fund as if it were a covered fund;
  - the banking entity's investment in and other relationships with the fund comply with the Anti-Bailout Requirements and the Prudential Backstop as if such fund were a covered fund;[19]

- the banking entity provides the Required Disclosures to actual and prospective investors in the fund, if the banking entity serves as sponsor or adviser to the fund;
- the banking entity complies with the requirements of Section 23B of the Federal Reserve Act as if the fund were an affiliate of the banking entity; and
- the banking entity's ownership interest in or other relationship with the fund is otherwise in compliance with, and subject to, applicable banking laws and regulations, including applicable safety and soundness standards.[20]

The Agencies note that they are considering whether the exclusion should be further limited to venture capital funds that do not invest in companies that, at the time of the investment, have more than a specified dollar amount of total annual revenue (*e.g.*, $50 million), calculated as of the last day of the calendar year.[21]

In addition, the Agencies request comment on whether to include a separate exclusion from the definition of "covered fund" for certain "long-term investment funds" that do not meet the aforementioned definition of "venture capital fund," subject to, among other requirements, a condition that the fund make investments that a banking entity could make directly with the intent to hold such investments for a minimum time period.[22]

I.A.3. Family Wealth Management Vehicles

The Proposed Rule excludes from the definition of "covered fund" any entity that acts as a "family wealth management vehicle,"[23] A family wealth management vehicle must be an entity that is not, and does not hold itself out as being, an entity or arrangement that raises money from investors primarily for the purpose of investing in securities for resale or other disposition or otherwise trading in securities.[24] If the entity is a trust, then all of the grantor(s) of the trust must be family customers. If the entity is not a trust, then (i) a majority of the voting interests in the entity must be owned, directly or indirectly, by family customers; and (ii) the entity must be owned solely by family customers and up to three closely related persons of the family customers.[25] For purposes of this exclusion, the following definitions apply:

- A "family customer" means (i) a family client (as defined below) or (ii) any natural person who is a father-in-law, mother-in-law, son-in-law or daughter-in-law of a family client, or a spouse or a spousal equivalent of any of the foregoing.
- A "family client" includes, among other things, any family member (including former family members), any key employee, certain family estates, certain non-profit organizations, charitable foundations and charitable trusts (subject to certain conditions in each case, including that all the funding of such entity come exclusively from other family clients) and various types of trusts (subject to certain conditions).[26]
- A "closely related" person means a natural person (including the estate and estate planning vehicles of such person) who has long-standing business or personal relationships with any family customer.

The following additional criteria must be satisfied in order for a banking entity to rely on the proposed exclusion with respect to a family wealth management vehicle:

- the banking entity or an affiliate thereof provides bona fide trust, fiduciary, investment advisory or commodity trading advisory services to the vehicle;
- the banking entity's investment in and other relationships with the vehicle comply with the Anti-Bailout Requirements and the Prudential Backstop as if such vehicle were a covered fund;
- the banking entity provides the Required Disclosures to actual and prospective investors in the vehicle;
- the banking entity complies with the requirements of Section 23B of the Federal Reserve Act[27] as if the vehicle were an affiliate of the banking entity;
- the banking entity does not acquire or retain, as principal, an ownership interest in the vehicle, other than up to 0.5 percent of the vehicle's outstanding ownership interests that may be held by the banking entity and its affiliates for the purpose of and to the extent necessary for establishing corporate separateness or addressing bankruptcy, insolvency or similar concerns;[28] and
- the banking entity complies with the prohibition on purchases of low-quality assets under the Federal Reserve's regulations implementing Section 23A of the Federal Reserve Act as if such banking entity and its affiliates were a member bank and the vehicle were an affiliate thereof.

I.A.4. Customer Facilitation Vehicles

The Proposed Rule excludes from the definition of "covered fund" certain customer facilitation vehicles that are formed by or at the request of a customer of the banking entity for the purpose of providing such customer (or one or more affiliates of such customer) with exposure to a transaction, investment strategy or other service provided by the banking entity.[29]

A banking entity may rely on this exclusion with respect to an issuer if each of the following conditions is satisfied:

- all of the ownership interests of the issuer are owned by the customer (or one or more of its affiliates) for whom the issuer was created, other than up to 0.5 percent of the issuer's outstanding ownership interests that may be held by the banking entity and its affiliates for the purpose of and to the extent necessary for establishing corporate separateness or addressing bankruptcy, insolvency or similar concerns;
- the banking entity maintains documentation outlining how it intends to facilitate the customer's exposure to such transaction, investment strategy or other service;
- the banking entity's investment in and other relationships with the vehicle comply with the Anti-Bailout Requirements and the Prudential Backstop as if such vehicle were a covered fund;
- the banking entity provides the Required Disclosures to actual and prospective investors in the vehicle;
- the banking entity complies with the requirements of Section 23B of the Federal Reserve Act[30] as if the vehicle were an affiliate of the banking entity;

- the banking entity complies with the prohibition on purchases of low-quality assets under the Federal Reserve's regulations implementing Section 23A of the Federal Reserve Act[31] as if such banking entity and its affiliates were a member bank and the vehicle were an affiliate thereof.[32]

Although the NPR states that the proposed exclusion "would require that the vehicle be formed by or at the request of the customer" (in order to differentiate such vehicles from covered funds that are organized and offered by the banking entity), the NPR nonetheless makes clear that that condition "would not preclude a banking entity from marketing its services through the use of customer facilitation vehicles or discussing with its customers prior to formation of the customer facilitation vehicle the potential benefits of structuring such services through a vehicle."[33]

I.B. CHANGES TO EXISTING EXCLUSIONS FROM THE DEFINITION OF "COVERED FUND"

I.B.1. Foreign Public Funds

Under the Current Rule, "covered fund" excludes a "foreign public fund," defined as any issuer that: (i) is organized or established outside the United States; (ii) is authorized to offer and sell ownership interests to retail investors in the issuer's home jurisdiction; and (iii) sells ownership interests predominantly through one or more "public offerings" outside the United States.[34]

The Proposed Rule amends and streamlines the foreign public funds exclusion with respect to the "home jurisdiction" requirement and the requirement that ownership interests be sold predominantly through public offerings. The Proposed Rule replaces these two requirements with a requirement that the fund be authorized to offer and sell ownership interests, and such interests are offered and sold, through one or more public offerings.[35] The Proposed Rule also modifies the definition of "public offering" to add a new requirement that the distribution be subject to substantive disclosure and retail investor protection laws or regulations.[36] The Proposed Rule only applies the condition that the distribution comply with all applicable requirements in the jurisdiction where it is made to instances in which the banking entity acts as the investment manager, investment adviser, commodity trading advisor, commodity pool operator or sponsor.[37]

As a result, the Proposed Rule no longer requires the fund to be authorized to be sold to retail investors in the home jurisdiction where it is organized. Additionally, while the fund would still be required to be offered and sold through one or more public offerings (which would require, among other things, that the distribution be made in a jurisdiction outside the United States that subjects the foreign public fund to substantive disclosure and retail investor protection laws or regulations), the Proposed Rule eliminates the requirement that it be sold "predominantly" through one or more public offerings.

The Proposed Rule also modifies the requirement, which applies solely with respect to a U.S. banking entity that serves as sponsor to a foreign public fund, on sales of ownership interests in the fund to employees of the sponsoring banking entity, the issuer or affiliates of such entities.[38] Under the proposal, the fund must be sold predominantly to persons other than the sponsoring U.S. banking entity or the issuer (or affiliates of the sponsoring banking entity or issuer), and directors and senior executive officers—rather than all employees—of such entities.[39] Employees of such entities who are not directors or senior executive officers therefore could be counted towards the "predominantly sold" condition. This modification should simplify the task of monitoring compliance with this condition; however, in light of the expansive definition of "affiliate" for purposes of the Volcker Rule,[40] identifying and monitoring compliance with respect to the relevant personnel of "affiliates" of the banking entity and the issuer may continue to be a material compliance burden.

I.B.2. Loan Securitizations

The Proposed Rule permits a loan securitization vehicle to hold up to five percent of its assets in non-loan assets.[41] This proposal would modify the Current Rule's requirement that a loan securitization's assets be composed exclusively of loans and not include any securities or derivatives (subject to limited exceptions for cash equivalents and foreign exchange and interest rate derivatives). The Proposed Rule also codifies the Agencies' FAQs which clarified that (i) the scope of permissible servicing assets is not limited to securities,[42] and (ii) "cash equivalents" means high quality, highly liquid investments whose maturity corresponds to the securitization's expected or potential need for funds and whose currency corresponds to either the underlying loans or the asset-backed securities[43] (but without any requirement that cash equivalents be "short-term").[44]

I.B.3. Public Welfare Investment Funds and Small Business Investment Companies

Under the Current Rule, a "covered fund" does not include small business investment companies ("SBICs") or companies that have received notice from the Small Business Administration to proceed to qualify for a license as an SBIC (which notice or license has not been revoked).[45] This exclusion also covers an issuer the business of which is to make investments that are: (i) designed primarily to promote the public welfare, including the welfare of low- and moderate-income communities or families (such as providing housing, services or jobs), of the type permitted for national banks under the National Bank Act;[46] or (ii) "qualified rehabilitation expenditures" with respect to a "qualified rehabilitated building" or "certified historic structure," as such terms are defined in Section 47 of the Internal Revenue Code of 1986 or a similar U.S. state historic tax credit program.[47] These types of investments often play a significant role in banking entities' Community Reinvestment Act objectives, particularly in the case of regional and community banking organizations.

The Proposed Rule does not make any changes with respect to the exclusion for public welfare investment funds, but requests comment on whether any change should be made to clarify that all permissible public

welfare investments, under any agency's regulation, are excluded from the covered fund restrictions.[48] In particular, the Agencies requested comment on whether "qualified opportunity funds" (in respect of the "opportunity zone" program established by the Tax Cuts and Jobs Act) should be provided an express exclusion from the definition of "covered fund."[49]

The Proposed Rule includes certain changes with respect to the exclusion for SBICs. The Proposed Rule revises the exclusion for SBICs to clarify how the exclusion would apply to SBICs that surrender their licenses during wind-down phases.[50] The Proposed Rule specifies that the exclusion for SBICs continues to apply to an issuer that was formerly an SBIC, but which has voluntarily surrendered its license to operate as a SBIC[51] and does not make new investments (other than investments in cash equivalents) after such voluntary surrender.[52] Additionally, the Proposed Rule includes conditions which the Agencies state are designed to ensure that the revised exclusion is not abused. In particular, the requirement that an issuer does not make new investments after surrendering its license is intended to ensure that the exclusion would only apply to funds that are actually winding down and not funds that are making new investments (including follow-on investments to existing investments) or that are engaged in speculative activities. In addition, the exclusion only applies to an issuer that surrenders its SBIC license and does not extend to an issuer if its SBIC license has been revoked.

II. INVESTMENTS ALONGSIDE COVERED FUNDS BY BANKING ENTITIES AND THEIR DIRECTORS AND EMPLOYEES

The Proposed Rule includes a rule of construction that a banking entity's investment alongside a covered fund is not treated as an investment in the covered fund for purposes of calculating the quantitative limitations on a banking entity's permitted investments in covered funds. These limitations restrict a banking entity's ownership interest in a single covered fund that it organizes and offers to no more than 3 percent of the total outstanding "ownership interests" of the covered fund at any time more than one year after the date of establishment of the fund, and restrict the aggregate value of the banking entity's ownership interests held under the organizing and offering exemption to no more than 3 percent of the banking entity's Tier 1 capital.

The NPR and Proposed Rule introduce the following elements into the framework for calculating the investment limitations and the application of the Volcker Rule to direct investments that banking entities and their directors and investors make alongside[53] a covered fund.

- A banking entity would not be required to include in the calculation of the per-fund and aggregate limitations referred to above "any investment the banking entity makes alongside a covered fund" and would not be restricted under Section _.12 in the "amount of any investment the banking entity makes alongside a covered fund," in each case, as long as the investment is made in compliance with applicable laws and regulations, including applicable safety and soundness standards.[54]

- The Agencies expect that any direct investments made by a director or employee of a banking entity (or an affiliate thereof) alongside a covered fund (whether as a series of parallel investments or as a co-investment) would not be treated as an investment by the director or employee in the covered fund."[55] As a result, such an investment would not be attributed to the banking entity, "regardless of whether the banking entity arranged the transaction on behalf of the director or employee or provided financing for the investment."[56]
- Section ._11(a)(7) of the Current Rule, which provides that directors and employees are eligible to invest in a covered fund organized and offered by a banking entity only if they are "directly engaged" in providing services to the fund, applies only to directors' and employees' investments in covered funds, but not to their direct investments made alongside covered funds.[57]

The Agencies emphasize in the Preamble that any such direct investments would need to be made in compliance with applicable laws and regulations—therefore, banking entities would not be permitted to invest alongside a covered fund to the extent that doing so would result in the banking entity engaging in prohibited proprietary trading, nor could a banking entity make investments alongside a covered fund that the banking entity would not otherwise have the authority to make under applicable banking and other laws and regulations.[58]

The Agencies further clarify that the proposed rule of construction would not prohibit a banking entity from having "investment policies, arrangements or agreements to invest alongside a covered fund in all or substantially all of the investments made by the covered fund or to fund all or any portion of the investment opportunities made available by the covered fund to other investors." Accordingly, a banking entity could "market a covered fund it organizes and offers on the basis of the banking entity's expectation that it would invest in parallel with the covered fund in some or all of the same investments, or the expectation that the banking entity would fund one or more co-investment opportunities made available by the covered fund."[59] The Agencies expect, however, that any such investment policies, arrangement or agreements would "ensure that the banking entity has the ability to evaluate each investment on a case-by-case basis to confirm that the banking entity does not make any investment unless the investment complies with applicable laws and regulations, including any applicable safety and soundness standards."[60]

Finally, the Proposed Rule provides that an investment by a banking entity's director or employee who acquires a restricted profit interest in his or her personal capacity in a covered fund sponsored by the banking entity will be attributed to the banking entity if the banking entity, directly or indirectly, extends financing for the purpose of enabling the director or employee to acquire the restricted profit interest in the fund and the financing is used to acquire such ownership interest in the covered fund.[61] The Preamble states that the Proposed Rule "would not change the treatment of the banking entity's or its affiliates' ownership of a restricted profit interest under the [Current Rule]."[62]

III. "SUPER 23A" – LIMITATIONS ON RELATIONSHIPS WITH CERTAIN COVERED FUNDS

The Proposed Rule adds two categories of exemptions to the "Super 23A" provisions, which prohibit a banking entity from engaging in any "covered transactions," as defined under Section 23A of the Federal Reserve Act,[63] with a covered fund for which the banking entity serves, directly or indirectly, as the investment manager, investment adviser, commodity trading advisor or sponsor, or that the banking entity organizes and offers (and other covered funds controlled by such a covered fund).

- First, Super 23A under the Proposed Rule would incorporate the exemptions under Section 23A of the Federal Reserve Act for certain transactions that are not subject to the quantitative limits, collateral requirements and low-quality asset prohibition, including the following:[64]
    - intraday extensions of credit to the fund, so long as the bank has safety and soundness policies designed to manage the risk exposure and only if the bank has no reason to believe the fund cannot repay the credit;
    - transactions with the fund that are secured by cash or U.S. government securities;
    - purchasing from the fund an extension of credit subject to a repurchase agreement; and
    - purchasing from the fund an extension of credit (provided that certain conditions are satisfied, including certain quantitative limits and only if the banking entity makes an independent evaluation of the borrower's creditworthiness).
- Second, Super 23A would also include exemptions for a banking entity's short-term extensions of credit to, and purchase assets from, a covered fund, subject to the following conditions:[65]
    - the extension of credit or purchase of assets must be made in the ordinary course of business in connection with payment transactions, securities, derivatives, or futures clearing, or settlement services;[66]
    - any extension of credit must be repaid, sold or terminated no later than five business days after it was originated;[67] and
    - any extensions of credit must meet requirements applicable to intraday extensions of credit under Regulation W (as if the extension of credit were an intraday extension of credit, regardless of its actual duration).[68]

Any transactions or activities permitted by the exemptions described above would be subject to the Prudential Backstop.[69]

IV. EXCLUSIONS FROM THE DEFINITION OF "OWNERSHIP INTEREST"

The Proposed Rule modifies the definition of "ownership interest" in two respects, both of which are intended to clarify that a debt relationship with a covered fund would typically not constitute an "ownership interest" in the fund.

First, the Proposed Rule provides a safe harbor from the "ownership interest" definition for senior loans or senior debt instruments that meet the following conditions:[70]

- Holders of the interest do not have the right to receive a share of the income, gains or profits of the covered fund, but are entitled to receive only: (i) interest at a stated interest rate, as well as commitment fees or other fees, which are not determined by reference to the performance of the underlying assets of the covered fund; and (ii) fixed principal payments on or before a maturity date (which may include prepayment premiums intended solely to reflect, and compensate holders of the interest for, foregone income resulting from an early prepayment);
- The entitlement to payments under the terms of the interest are absolute and could not be reduced based on losses arising from the underlying assets of the covered fund, such as allocation of losses, write-downs or charge-offs of the outstanding principal balance, or reductions in the amount of interest due and payable on the interest; and
- The holders of the interest are not entitled to receive the underlying assets of the covered fund after all other interests have been redeemed or paid in full (excluding the rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event).[71]

In addition, the Proposed Rule clarifies that the right to participate in the removal of an investment manager for cause or to nominate or vote on a nominated replacement manager upon an investment manager's resignation or removal would not, on its own, cause an interest to be considered an "ownership interest."[72] It would continue to be the case, as under the Current Rule, that the definition of "ownership interest" includes other types of interests that have the right to participate in the selection or removal of a general partner, managing member, member of the board of directors or trustees, investment manager, investment adviser, or commodity trading advisor of the covered fund, but excluding the rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event.[73]

V. QUALIFYING FOREIGN EXCLUDED FUNDS

The Proposed Rule makes permanent the temporary relief that the Agencies have provided in policy statements[74] with respect to the potential attribution of the activities and investments of qualifying foreign excluded funds to a foreign banking entity that controls such a fund due to interaction between the definitions of "covered fund" and "banking entity."[75] Consistent with these policy statements, the Proposed Rule exempts a foreign fund from the proprietary trading prohibition and restrictions on investments in and

sponsorship of covered funds (and would not attribute the fund's activities to a foreign banking entity that invests in or sponsors the fund) if the following conditions are satisfied:

- The foreign banking entity's investment or sponsorship in the fund complies with the exemption for certain covered fund activities conducted "solely outside of the United States" (commonly referred to as the "SOTUS" exemption).[76]
- The fund meets the following conditions:
  - is organized or established outside the United States and its ownership interests are offered and sold solely outside the United States;
  - would be a covered fund were the entity organized or established in the United States, or is, or holds itself out as being, an entity or arrangement that raises money from investors primarily for the purpose of investing in financial instruments for resale or other disposition or otherwise trading in financial instruments;
  - would not otherwise be a banking entity except by virtue of the foreign banking entity's acquisition or retention of an ownership interest in, or sponsorship of, the entity;
  - is established and operated as part of a bona fide asset management business; and
  - is not operated in a manner that enables the foreign banking entity to evade the requirements of the Volcker Rule or the implementing regulations. [77]

VI. SELECTED QUESTIONS RAISED BY AGENCIES FOR PUBLIC COMMENT

In the Preamble, the Agencies pose 87 numbered questions for public comment, many of which consist of multiple sub-questions, relating to specific aspects of the Proposed Rule. The Agencies' questions highlight a number of issues that are not addressed through specific amendments in the Proposed Rule, although in many cases, the questions appear to be designed to inform the Agencies' consideration of further potential revisions to significant elements of the Proposed Rule.

The table below provides a high-level, non-comprehensive overview of certain topics that the Agencies identified for comment and a summary of selected questions they pose on each such topic.

Topic	Areas Identified for Comment and Questions Posed
Additional Exclusions from the "Covered Fund" Definition	
Venture capital funds	• Whether it is appropriate to expand or narrow the vehicles for which banking entities would be permitted to make use of the exclusion • Whether the requirements for a qualifying venture capital fund are sufficient to distinguish these types of funds from covered funds • Whether an additional proposed revenue requirement for portfolio companies (for example, total annual revenue of no more than $50 million) should be added to the venture capital fund exclusion to help

Topic	Areas Identified for Comment and Questions Posed
	ensure that the investments made by excluded venture capital funds are truly made in small and early-stage companies • Whether the proposed venture capital fund exclusion should require that 100 percent of the fund's holdings, other than short-term holdings, be in qualifying investments instead of 80 percent • Whether there are provisions or conditions of the definition under Rule 203(*l*)-1 under the Advisers Act that are inappropriate for purposes of determining an exclusion from the "covered fund" definition in Section _.10 • Whether it is sufficiently clear what kind of assets or investments would result in a conflict of interest or an exposure to a high-risk asset or high-risk trading strategy in the context of a qualifying venture capital fund • Whether the Agencies should exclude from the definition of covered fund, or otherwise permit the activities of, certain long-term investment funds (a potential definition for which is described in Question #50 of the NPR)
Family wealth management vehicles	• Whether the Agencies' proposed definition of "family wealth management vehicle" includes the appropriate vehicles or whether alternatives approaches should be taken more generally • Whether the exclusion should permit closely related persons to invest in family wealth management vehicles or be modified in any way • Whether the Agencies should permit an up to 0.5 percent ownership interest to be held by a third party that is unaffiliated with either the banking entity or the family customer
Credit funds	• Determine the types of loans and permissible debt instruments or some subset of those assets, if any, that a credit fund should be able to hold • Whether credit funds should be able to hold small amounts of equity securities (or rights to acquire equity securities) received on customary terms in connection with the credit fund's loans or debt instruments and what the calculation methodology should be • Whether credit funds should be allowed to hold any types of derivatives • Whether it is appropriate to require a banking entity that sponsors or serves as an investment adviser or commodity trading advisor to a credit fund, to comply with the disclosure requirements of Section _.11(a)(8) as if the credit fund were a covered fund • Whether the definition of proprietary trading is properly scoped • Whether the Agencies should combine the proposed credit fund exclusion with the current loan securitization exclusion

Topic	Areas Identified for Comment and Questions Posed
Customer facilitation vehicles	• Whether the Agencies should expand or narrow the vehicles for which banking entities would be permitted to make use of the exclusion • Whether the Agencies should specify which types of transaction, investment strategy or other service such a customer facilitation vehicle could be formed to facilitate exposure to • Whether the Agencies should permit an up to 0.5 percent ownership interest to be held by a third party that is unaffiliated with either the banking entity or the customer
Amendments to Current Exclusions from the "Covered Fund" Definition	
Foreign public funds	• Whether foreign funds that satisfy the proposed conditions in the foreign public fund exclusion sufficiently similar to U.S. registered investment companies such that it is appropriate to exclude these funds from the covered fund definition • Whether the proposed replacement of the home jurisdiction requirement and the requirement that ownership interests be sold predominantly through public offerings with a requirement that the fund is authorized to offer and sell ownership interests, and such interests are offered and sold through one or more public offerings address compliance concerns • Whether the condition that the "public offering" definition requiring the distribution be subject to substantive disclosure and retail investor protection laws or regulations is sufficiently clear • Whether it is difficult for a banking entity to determine whether a fund satisfies the implementing regulations' condition of the "public offering" definition requiring that the distribution comply with all applicable requirements in the jurisdiction in which the distribution is made and whether the Agencies should eliminate or modify this requirement (in particular, with respect a banking entity not acting as sponsor or adviser to the fund) • Whether the proposed requirement that the fund's ownership interests are sold predominantly to persons other than the sponsoring banking entity or the issuer (or affiliates of the sponsoring banking entity or issuer), and directors and senior executive officers of such entities is necessary to prevent evasion of the requirements of the Volcker Rule
Loan Securitizations	• Whether the loan securitization exclusion should permit loan securitization issuers to hold a certain percentage (*e.g.*, 5 percent of 10 percent) of non-loan assets • Determine the appropriate method of calculating compliance with the limit (*e.g.*, market value, par value, principal balance, or some other measure) • Whether the Agencies should limit the type of permissible non-loan assets to certain classes or structures

Topic	Areas Identified for Comment and Questions Posed
Public Welfare and Small Business Funds	• Whether the scope of the current public welfare investment fund exclusion is properly calibrated • Whether the Agencies should establish a separate exclusion for CRA-qualified investments or incorporate such an exclusion into the exclusion for public welfare investments • Whether the Agencies should provide an express exclusion from the definition of covered fund for rural business investment companies, similar to the exclusion for SBICs • Whether the Agencies should provide an express exclusion from the definition of covered fund for qualified opportunity funds • Whether the proposed exclusion for issuers that surrender their SBIC licenses should include a requirement that the issuer operate pursuant to a written plan to dissolve within a set period of time • Whether the rule should specify the specific activities or investments, if any, that an issuer that surrenders its SBIC license should be expressly permitted to engage in during wind-down phases
Limitations on Relationships with a Covered Fund	
Potential Additional Exclusions	• Whether there are any additional services that a banking entity typically provides to sponsored funds (or funds for which it acts as an investment adviser) that are still prohibited under the Proposed Rule • Appropriateness of amending Section _.14 to permit banking entities to engage in additional covered transactions relating to payment, clearing and settlement services
Transactions with Covered Funds	• Whether the requirement that all payment, clearing, or settlement activity be settled within five business days is sufficient to give effect to the proposed exemption's purpose • Whether the Agencies should, in connection with the proposed exemption referenced above, require banking entities to comply with the prohibition on purchases of low-quality assets under the Federal Reserve's regulations implementing Section 23A of the Federal Reserve Act
Parallel Investments	
Direct Investments by Banking Entities Alongside Covered Funds	• Whether the proposed rule of construction creates opportunities for evasion by allowing banking entities to structure parallel investments and co-investments to evade the Volcker Rule • Whether the Agencies should place restrictions on a banking entity's policies and agreements regarding parallel investments and co-investments
Investments by Directors and	• Whether further modifications to the Proposed Rule's treatment of director and employee investments is needed in order to

Topic	Areas Identified for Comment and Questions Posed
Employees Alongside Covered Funds	accommodate certain arrangements, including employee securities companies • Whether the interpretation of Section _.11(a)(7) as not reaching director and employee investments alongside covered funds is correct or whether the Agencies should provide additional rule text addressing such investments
Definition of "Ownership Interest"	
Features of the Definition of Ownership	• Whether to allow interest holders to participate in the removal or replacement of an investment manager outside of the occurrence of an event of default or an acceleration event without being deemed to have an ownership interest • Whether to change the Proposed Rule's definition of ownership interest from the right to receive a share of the income, gains or profits of a covered to clarify that only an interest with the right to a receive a share of the *net* income, gains or profits of the covered fund is an ownership interest
Safe Harbor from Definition of Ownership Interest	• Whether the safe harbor effectively addresses concerns that debt instruments may be deemed to be ownership interests. In particular whether the phrase "fixed principal payments" should be replaced with "contractually determined principal payments," "repayment of a fixed principal amount," or some other wording • Appropriateness of limiting the safe harbor to senior debt instruments
Qualifying Foreign Excluded Funds	
Effectiveness of the Proposed Exclusion	• Whether the Agencies should make any additional related amendments or include any additional parameters • Whether the amendments related to foreign excluded funds address the unintended consequences and extraterritorial impact of the Current Rule
Consequences of the Qualifying Foreign Excluded Funds Exclusion	• Whether the proposed amendments related to foreign excluded funds promote and protect safety and soundness and U.S. financial stability

* * *

ENDNOTES

1 Preamble at 16.

2 The disclosures must be provided in writing to any prospective and actual investor and parallel the disclosures required under the organizing and offering exception. Proposed Rule § _.11(a)(8).

3 Current Rule § _.15.

4 Proposed Rule § _.10(c)(15); Preamble at 46.

5 Preamble at 49.

6 Proposed Rule § _.10(c)(15)(i).

7 Proposed Rule § _.10(c)(15)(ii)(A). Under this requirement, a qualifying venture capital fund could not engage in any activities that are principally for the purpose of short-term resale, benefitting from actual or expected short-term price movements, realizing short-term arbitrage profits, or hedging one or more of the positions resulting from such purchases or sales.

8 Proposed Rule § _.10(c)(15)(ii)(B).

9 17 CFR § 270.3a-7; *see also* SEC, *Treatment of Asset-Backed Issuers Under the Investment Company Act*, 76 Fed. Reg. 55308, 55310-11 (Sept. 7, 2011).

10 Proposed Rule § _.10(c)(15)(iv)(A).

11 Proposed Rule § _.10(c)(15)(iv). The principal restrictions of Section 23B include (1) a requirement that most transactions between an insured depository institution ("IDI") and its affiliates be on terms and circumstances that are substantially the same as those prevailing at the time for comparable transactions with nonaffiliates; (2) a restriction on an IDI's purchase, as fiduciary, of assets from an affiliate unless certain criteria are met; (3) a restriction on an IDI's purchase, during the existence of an underwriting syndicate, of any security if a principal underwriter of the security is an affiliate; and (4) a prohibition on publishing an advertisement or entering into an agreement stating that an IDI will be responsible for the obligations of its affiliates. Federal Reserve, BHC Supervision Manual § 2020.1.15 (Jul. 2009).

12 Proposed Rule § _.10(c)(15)(iii)-(v). The Preamble notes that, for example, a banking entity's investment in or relationship with a credit fund could be subject to the regulatory capital adjustments and deductions relating to investments in financial subsidiaries or in the capital of unconsolidated financial institutions, if applicable. Preamble at 51 n.108.

13 Preamble at 51. For example, a banking entity's investment in or relationship with a credit fund could be subject to the regulatory capital adjustments and deductions relating to investments in financial subsidiaries or in the capital of unconsolidated financial institutions, if applicable. *See* 12 CFR 217.22.

14 *See* 17 CFR § 275.203(*l*)-1.

15 "Qualifying investment" is defined in the SEC's regulation to be: (1) an equity security issued by a qualifying portfolio company that has been acquired directly by the private fund from the qualifying portfolio company; (2) any equity security issued by a qualifying portfolio company in exchange for an equity security issued by the qualifying portfolio company described in (1); or (3) any equity security issued by a company of which a qualifying portfolio company is a majority-owned subsidiary, as defined in Section 2(a)(24) of the Investment Company Act, or a predecessor, and is acquired by the private fund in exchange for an equity security described in (1) or (2). *See* 17 CFR 275.203(*l*)-1(c)(3).

16 In particular, "qualifying portfolio company" is defined in the SEC's regulation to be a company that: (1) at the time of any investment by the private fund, is not reporting or foreign traded and does not control, is not controlled by or under common control with another company, directly or indirectly, that is reporting or foreign traded; (2) does not borrow or issue debt obligations in connection with the private fund's investment in such company and distribute to the private fund the proceeds of such borrowing or issuance in exchange for the private fund's investment; and (3) is not an investment company, a private fund, an issuer that would be an investment company but for the exemption provided by 17 CFR § 270.3a–7, or a commodity pool. *See* 17 CFR 275.203(*l*)-1(c)(4).

ENDNOTES (CONTINUED)

17 17 CFR 275.203(*l*)–1(a).

18 Current Rule § _.3(b)(1)(i).

19 Proposed Rule § _.10(c)(16)(ii)-(iv).

20 Proposed Rule § _.10(c)(16)(iv).

21 Preamble at 66.

22 Preamble at 73.

23 Proposed Rule § _.10(c)(17).

24 Proposed Rule § _.10(c)(17)(i).

25 Proposed Rule § _.10(c)(17)(i).

26 Rule 202(a)(11)(G)-1(d)(4).

27 Proposed Rule § _.10(c)(17)(ii).

28 Proposed Rule § _.10(c)(17)(ii)(D).

29 Proposed Rule § _.10(c)(18)(i).

30 Proposed Rule § _.10(c)(18)(ii)(B)(5).

31 Proposed Rule § _.15(a).

32 Proposed Rule § _.10(c)(18)(ii).

33 Preamble at 85-86.

34 Proposed Rule § _.10(c)(1).

35 Proposed Rule § _.10(c)(1)(i); Preamble at 28.

36 Proposed Rule § _.10(c)(1)(iii); Preamble at 28.

37 Proposed Rule § _.10(c)(1)(iii); Preamble at 28-29.

38 Preamble at 29-30.

39 Preamble at 30.

40 The Volcker Rule defines the term "affiliate" to have the same meanings as under Section 2 of the BHC Act. BHC Act § 2(a)(2).

41 Proposed Rule § _.10(c)(8)(i); Preamble at 37.

42 *See* FAQ #4, available at https://www.federalreserve.gov/supervisionreg/faq.htm#4. *See also* Preamble at 35.

43 *See* FAQ #4; Preamble at 38.

44 Preamble at 38.

45 Current Rule § _.10(c)(11)(i).

46 Current Rule § _.10(c)(11)(ii)(A). Under the National Bank Act, a national bank "shall not make any such investment if the investment would expose the [bank] to unlimited liability," for example, and such investments are subject to certain aggregate limits determined by the OCC. 12 U.S.C. § 24 (Eleventh). OCC regulations also provide specific examples of qualifying public welfare investments under the National Bank Act, including with respect to affordable housing projects, economic development and job creation investments, investments in "community and economic development entities" and other public welfare investments. *See* 12 CFR § 24.6.

47 Current Rule § _.10(c)(11)(ii). "Qualified rehabilitated buildings" are certain buildings first placed in service before 1936, and "certified historic structures" are listed in the National Register or certified as being of historical significance to a registered historic district. 26 U.S.C. §§ 47(c)(1), 47(c)(3).

48 Preamble at 40.

ENDNOTES (CONTINUED)

49 Preamble at 42-43; Question 22.

50 Proposed Rule § _.10(c)(11)(i); Preamble at 44.

51 In accordance with 13 CFR 107.1900.

52 Proposed Rule § _.10(c)(11)(i); Preamble at 44-45. For purposes of this exclusion, "cash equivalents" would mean high quality, highly liquid investments whose maturity corresponds to the issuer's expected or potential need for funds and whose currency corresponds to the issuer's assets.

53 The Preamble states that, for purposes of these provisions, investments "alongside" a covered fund could include, for example, parallel investment—*i.e.*, a series of investments that are made side-by-side with a covered fund—as well as "co-investments"—*i.e.*, a specific investment opportunity that is made available to third parties where the covered fund does not have sufficient capital to make the entire investment. Preamble at 115 n.242.

54 Proposed Rule § _.12(b)(5)(i)-(ii).

55 Preamble at 118.

56 Preamble at 118. *See also* Proposed Rule at § _.12(b)(1)(iv) (which requires attribution of investments by directors and employees in covered funds).

57 Preamble at 118-19.

58 Preamble at 116.

59 Preamble at 119.

60 Preamble at 119.

61 Proposed Rule § _.12(c)(1)(i).

62 Preamble at 111.

63 Section 23A of the Federal Reserve Act defines "covered transaction" to mean the following with respect to an "affiliate" of a "member bank": (i) a loan or extension of credit to the affiliate, including a purchase of assets subject to an agreement to repurchase; (ii) a purchase of or an investment in securities issued by the affiliate; (iii) a purchase of assets *from* the affiliate, except such purchase of real and personal property as may be specifically exempted by the Federal Reserve; (iv) the acceptance of securities or other debt obligations issued by the affiliate as collateral for a loan or extension of credit to any person or company; (v) the issuance of a guarantee, acceptance or letter of credit, including an endorsement or standby letter of credit, on behalf of an affiliate; (vi) a transaction with an affiliate that involves the borrowing or lending of securities, to the extent that the transaction causes a member bank or a subsidiary to have credit exposure to the affiliate; or (vii) a "derivative transaction," as defined in paragraph (3) of Section 5200(b) of the Revised Statutes of the United States, with an affiliate, to the extent that the transaction causes a member bank or a subsidiary to have credit exposure to the affiliate. 12 USC § 371c(b)(7).

64 Preamble at 90, 96.

65 Proposed Rule § _.14(a)(2)(iv); Preamble at 90-91.

66 Proposed Rule § _.14(a)(2)(iv); Preamble at 98.

67 Proposed Rule § _.14(a)(2)(iv); Preamble at 98.

68 Proposed Rule § _.14(a)(2)(iv); Preamble at 98-99.

69 Proposed Rule § _.14(a)(3); Preamble at 96.

70 Preamble at 103.

71 Proposed Rule § _.10(d)(6)(i)(B). *See also* Preamble at 107-08.

72 Preamble at 107.

73 Preamble at 107.

74 Preamble at 19-20. For the first instance of relief, *see* Statement regarding Treatment of Certain Foreign Funds under the Rules Implementing Section 13 of the Bank Holding Company Act (July 21, 2017), available at

https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20170721a1.pdf. For the currently effective relief, *see* Statement regarding Treatment of Certain Foreign Funds under the Rules Implementing Section 13 of the Bank Holding Company Act (July 17, 2019), *available at* https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20190717a1.pdf.

75 Preamble at 18, 21.

76 Preamble at 21.

77 Preamble at 19-20.

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CONTACTS

New York

Thomas C. Baxter Jr.	+1-212-558-4324	baxtert@sullcrom.com
Whitney A. Chatterjee	+1-212-558-4883	chatterjeew@sullcrom.com
H. Rodgin Cohen	+1-212-558-3534	cohenhr@sullcrom.com
Elizabeth T. Davy	+1-212-558-7257	davye@sullcrom.com
Mitchell S. Eitel	+1-212-558-4960	eitelm@sullcrom.com
Michael T. Escue	+1-212-558-3721	escuem@sullcrom.com
Jared M. Fishman	+1-212-558-1689	fishmanj@sullcrom.com
C. Andrew Gerlach	+1-212-558-4789	gerlacha@sullcrom.com
Wendy M. Goldberg	+1-212-558-7915	goldbergw@sullcrom.com
Charles C. Gray	+1-212-558-4410	grayc@sullcrom.com
Joseph A. Hearn	+1-212-558-4457	hearnj@sullcrom.com
Shari D. Leventhal	+1-212-558-4354	leventhals@sullcrom.com
Marion Leydier	+1-212-558-7925	leydierm@sullcrom.com
Erik D. Lindauer	+1-212-558-3548	lindauere@sullcrom.com
Mark J. Menting	+1-212-558-4859	mentingm@sullcrom.com
Camille L. Orme	+1-212-558-3373	ormec@sullcrom.com
Stephen M. Salley	+1-212-558-4998	salleys@sullcrom.com
Rebecca J. Simmons	+1-212-558-3175	simmonsr@sullcrom.com
William D. Torchiana	+1-212-558-4056	torchianaw@sullcrom.com
Donald J. Toumey	+1-212-558-4077	toumeyd@sullcrom.com
Marc Trevino	+1-212-558-4239	trevinom@sullcrom.com
Benjamin H. Weiner	+1-212-558-7861	weinerb@sullcrom.com

Mark J. Welshimer	+1-212-558-3669	welshimerm@sullcrom.com
Michael M. Wiseman	+1-212-558-3846	wisemanm@sullcrom.com
Washington, D.C.		
Eric J. Kadel, Jr.	+1-202-956-7640	kadelej@sullcrom.com
William F. Kroener III	+1-202-956-7095	kroenerw@sullcrom.com
Stephen H. Meyer	+1-202-956-7605	meyerst@sullcrom.com
Jennifer L. Sutton	+1-202-956-7060	suttonj@sullcrom.com
Andrea R. Tokheim	+1-202-956-7015	tokheima@sullcrom.com
Samuel R. Woodall III	+1-202-956-7584	woodalls@sullcrom.com
Los Angeles		
Patrick S. Brown	+1-310-712-6603	brownp@sullcrom.com
William F. Kroener III	+1-310-712-6696	kroenerw@sullcrom.com
Paris		
William D. Torchiana	+33-1-7304-5890	torchianaw@sullcrom.com
Tokyo		
Keiji Hatano	+81-3-3213-6171	hatanok@sullcrom.com

APPENDIX A

(Textual Comparison of the Proposed Rule Against Amended Provisions of Currently Effective Regulations)

§ 248.1 Authority, purpose, scope, and relationship to other authorities.

(a) *Authority.* This part (Regulation VV) is issued by the Board under section 13 of the Bank Holding Company Act of 1956, as amended (12 U.S.C. 1851), as well as under the Federal Reserve Act, as amended (12 U.S.C. 221 *et seq.*); section 8 of the Federal Deposit Insurance Act, as amended (12 U.S.C. 1818); the Bank Holding Company Act of 1956, as amended (12 U.S.C. 1841 *et seq.*); and the International Banking Act of 1978, as amended (12 U.S.C. 3101 *et seq.*).

(b) *Purpose.* Section 13 of the Bank Holding Company Act establishes prohibitions and restrictions on proprietary trading and on investments in or relationships with covered funds by certain banking entities, including state member banks, bank holding companies, savings and loan holding companies, other companies that control an insured depository institution, foreign banking organizations, and certain subsidiaries thereof. This part implements section 13 of the Bank Holding Company Act by defining terms used in the statute and related terms, establishing prohibitions and restrictions on proprietary trading and on investments in or relationships with covered funds, and explaining the statute's requirements.

(c) *Scope.* This part implements section 13 of the Bank Holding Company Act with respect to banking entities for which the Board is authorized to issue regulations under section 13(b)(2) of the Bank Holding Company Act (12 U.S.C. 1851(b)(2)) and take actions under section 13(e) of that Act (12 U.S.C. 1851(e)). These include any state bank that is a member of the Federal Reserve System, any company that controls an insured depository institution (including a bank holding company and savings and loan holding company), any company that is treated as a bank holding company for purposes of section 8 of the International Banking Act (12 U.S.C. 3106), and any subsidiary of the foregoing other than a subsidiary for which the OCC, FDIC, CFTC, or SEC is the primary financial regulatory agency (as defined in section 2(12) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (12 U.S.C. 5301(12)), but do not include such entities to the extent they are not within the definition of banking entity in § 248.2(c).

(d) *Relationship to other authorities.* Except as otherwise provided under section 13 of the BHC Act or this part, and notwithstanding any other provision of law, the prohibitions and restrictions under section 13 of BHC Act and this part shall apply to the activities of a banking entity, even if such activities are authorized for the banking entity under other applicable provisions of law.

(e) *Preservation of authority.* Nothing in this part limits in any way the authority of the Board to impose on a banking entity identified in paragraph (c) of this section additional requirements or restrictions with respect to any activity, investment, or relationship covered under section 13 of the Bank Holding Company Act or this part, or additional penalties for violation of this part provided under any other applicable provision of law.

§ 248.2 Definitions.

UNLESS OTHERWISE SPECIFIED, FOR PURPOSES OF THIS PART:

(a) *Affiliate* has the same meaning as in section 2(k) of the Bank Holding Company Act of 1956 (12 U.S.C. 1841(k)).

(b) *Bank holding company* has the same meaning as in section 2 of the Bank Holding Company Act of 1956 (12 U.S.C. 1841).

(c) *Banking entity.* (1) Except as provided in paragraph (c)(2) of this section, *banking entity* means:

(i) Any insured depository institution;

(ii) Any company that controls an insured depository institution;

(iii) Any company that is treated as a bank holding company for purposes of section 8 of the International Banking Act of 1978 (12 U.S.C. 3106); and

(iv) Any affiliate or subsidiary of any entity described in paragraphs (c)(1)(i), (ii), or (iii) of this section.

(2) Banking entity does not include:

(i) A covered fund that is not itself a banking entity under paragraph (c)(1)(i), (ii), or (iii) of this section;

(ii) A portfolio company held under the authority contained in section 4(k)(4)(H) or (I) of the BHC Act (12 U.S.C. 1843(k)(4)(H), (I)), or any portfolio concern, as defined under 13 CFR 107.50, that is controlled by a small business investment company, as defined in section 103(3) of the Small Business Investment Act of 1958 (15 U.S.C. 662), so long as the portfolio company or portfolio concern is not itself a banking entity under paragraph (c)(1)(i), (ii), or (iii) of this section; or

(iii) The FDIC acting in its corporate capacity or as conservator or receiver under the Federal Deposit Insurance Act or Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

(d) *Board* means the Board of Governors of the Federal Reserve System.

(e) *CFTC* means the Commodity Futures Trading Commission.

(f) *Dealer* has the same meaning as in section 3(a)(5) of the Exchange Act (15 U.S.C. 78c(a)(5)).

(g) *Depository institution* has the same meaning as in section 3(c) of the Federal Deposit Insurance Act (12 U.S.C. 1813(c)).

(h) *Derivative.* (1) Except as provided in paragraph (h)(2) of this section, *derivative* means:

(i) Any swap, as that term is defined in section 1a(47) of the Commodity Exchange Act (7 U.S.C. 1a(47)), or security-based swap, as that term is defined in section 3(a)(68) of the Exchange Act (15 U.S.C. 78c(a)(68));

(ii) Any purchase or sale of a commodity, that is not an excluded commodity, for deferred shipment or delivery that is intended to be physically settled;

(iii) Any foreign exchange forward (as that term is defined in section 1a(24) of the Commodity Exchange Act (7 U.S.C. 1a(24)) or foreign exchange swap (as that term is defined in section 1a(25) of the Commodity Exchange Act (7 U.S.C. 1a(25));

(iv) Any agreement, contract, or transaction in foreign currency described in section 2(c)(2)(C)(i) of the Commodity Exchange Act (7 U.S.C. 2(c)(2)(C)(i));

(v) Any agreement, contract, or transaction in a commodity other than foreign currency described in section 2(c)(2)(D)(i) of the Commodity Exchange Act (7 U.S.C. 2(c)(2)(D)(i)); and

(vi) Any transaction authorized under section 19 of the Commodity Exchange Act (7 U.S.C. 23(a) or (b));

(2) A derivative does not include:

(i) Any consumer, commercial, or other agreement, contract, or transaction that the CFTC and SEC have further defined by joint regulation, interpretation, or other action as not within the definition of swap, as that term is defined in section 1a(47) of the Commodity Exchange Act (7 U.S.C. 1a(47)), or security-based swap, as that term is defined in section 3(a)(68) of the Exchange Act (15 U.S.C. 78c(a)(68)); or

(ii) Any identified banking product, as defined in section 402(b) of the Legal Certainty for Bank Products Act of 2000 (7 U.S.C. 27(b)), that is subject to section 403(a) of that Act (7 U.S.C. 27a(a)).

(i) *Employee* includes a member of the immediate family of the employee.

(j) *Exchange Act* means the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*).

(k) *Excluded commodity* has the same meaning as in section 1a(19) of the Commodity Exchange Act (7 U.S.C. 1a(19)).

(l) *FDIC* means the Federal Deposit Insurance Corporation.

(m) *Federal banking agencies* means the Board, the Office of the Comptroller of the Currency, and the FDIC.

(n) *Foreign banking organization* has the same meaning as in section 211.21(o) of the Board's Regulation K (12 CFR 211.21(o)), but does not include a foreign bank, as defined in section 1(b)(7) of the International Banking Act of 1978 (12 U.S.C. 3101(7)), that is organized under the laws of the Commonwealth of Puerto Rico, Guam, American Samoa, the United States Virgin Islands, or the Commonwealth of the Northern Mariana Islands.

(o) *Foreign insurance regulator* means the insurance commissioner, or a similar official or agency, of any country other than the United States that is engaged in the supervision of insurance companies under foreign insurance law.

(p) *General account* means all of the assets of an insurance company except those allocated to one or more separate accounts.

(q) *Insurance company* means a company that is organized as an insurance company, primarily and predominantly engaged in writing insurance or reinsuring risks underwritten by insurance companies, subject to supervision as such by a state insurance regulator or a foreign insurance regulator, and not operated for the purpose of evading the provisions of section 13 of the BHC Act (12 U.S.C. 1851).

(r) *Insured depository institution* has the same meaning as in section 3(c) of the Federal Deposit Insurance Act (12 U.S.C. 1813(c)), but does not include:

(1) An insured depository institution that is described in section 2(c)(2)(D) of the BHC Act (12 U.S.C. 1841(c)(2)(D)); or

(2) An insured depository institution if it has, and if every company that controls it has, total consolidated assets of $10 billion or less and total trading assets and trading liabilities, on a consolidated basis, that are 5 percent or less of total consolidated assets.

(s) *Limited trading assets and liabilities* means with respect to a banking entity that:

(1) (i) The banking entity has, together with its affiliates and subsidiaries, trading assets and liabilities (excluding trading assets and liabilities attributable to trading activities permitted pursuant to § 248.6(a)(1) and (2) of subpart B) the average gross sum of which

over the previous consecutive four quarters, as measured as of the last day of each of the four previous calendar quarters, is less than $1 billion; and

(ii) The Board has not determined pursuant to § 248.20(g) or (h) of this part that the banking entity should not be treated as having limited trading assets and liabilities.

(2) With respect to a banking entity other than a banking entity described in paragraph (s)(3) of this section, trading assets and liabilities for purposes of this paragraph (s) means trading assets and liabilities (excluding trading assets and liabilities attributable to trading activities permitted pursuant to § 248.6(a)(1) and (2) of subpart B) on a worldwide consolidated basis.

(3) (i) With respect to a banking entity that is a foreign banking organization or a subsidiary of a foreign banking organization, trading assets and liabilities for purposes of this paragraph (s) means the trading assets and liabilities (excluding trading assets and liabilities attributable to trading activities permitted pursuant to § 248.6(a)(1) and (2) of subpart B) of the combined U.S. operations of the top-tier foreign banking organization (including all subsidiaries, affiliates, branches, and agencies of the foreign banking organization operating, located, or organized in the United States).

(ii) For purposes of paragraph (s)(3)(i) of this section, a U.S. branch, agency, or subsidiary of a banking entity is located in the United States; however, the foreign bank that operates or controls that branch, agency, or subsidiary is not considered to be located in the United States solely by virtue of operating or controlling the U.S. branch, agency, or subsidiary. For purposes of paragraph (s)(3)(i) of this section, all foreign operations of a U.S. agency, branch, or subsidiary of a foreign banking organization are considered to be located in the United States, including branches outside the United States that are managed or controlled by a U.S. branch or agency of the foreign banking organization, for purposes of calculating the banking entity's U.S. trading assets and liabilities.

(t) *Loan* means any loan, lease, extension of credit, or secured or unsecured receivable that is not a security or derivative.

(u) *Moderate trading assets and liabilities* means, with respect to a banking entity, that the banking entity does not have significant trading assets and liabilities or limited trading assets and liabilities.

(v) *Primary financial regulatory agency* has the same meaning as in section 2(12) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (12 U.S.C. 5301(12)).

(w) *Purchase* includes any contract to buy, purchase, or otherwise acquire. For security futures products, purchase includes any contract, agreement, or transaction for future delivery. With respect to a commodity future, purchase includes any contract, agreement, or transaction for future delivery. With respect to a derivative, purchase includes the execution, termination (prior to its scheduled maturity date), assignment, exchange, or similar transfer or conveyance of, or extinguishing of rights or obligations under, a derivative, as the context may require.

(x) *Qualifying foreign banking organization* means a foreign banking organization that qualifies as such under section 211.23(a), (c) or (e) of the Board's Regulation K (12 CFR 211.23(a), (c), or (e)).

(y) *SEC* means the Securities and Exchange Commission.

(z) *Sale* and *sell* each include any contract to sell or otherwise dispose of. For security futures products, such terms include any contract, agreement, or transaction for future delivery. With respect to a commodity future, such terms include any contract, agreement, or transaction for

future delivery. With respect to a derivative, such terms include the execution, termination (prior to its scheduled maturity date), assignment, exchange, or similar transfer or conveyance of, or extinguishing of rights or obligations under, a derivative, as the context may require.

(aa) *Security* has the meaning specified in section 3(a)(10) of the Exchange Act (15 U.S.C. 78c(a)(10)).

(bb) *Security-based swap dealer* has the same meaning as in section 3(a)(71) of the Exchange Act (15 U.S.C. 78c(a)(71)).

(cc) *Security future* has the meaning specified in section 3(a)(55) of the Exchange Act (15 U.S.C. 78c(a)(55)).

(dd) *Separate account* means an account established and maintained by an insurance company in connection with one or more insurance contracts to hold assets that are legally segregated from the insurance company's other assets, under which income, gains, and losses, whether or not realized, from assets allocated to such account, are, in accordance with the applicable contract, credited to or charged against such account without regard to other income, gains, or losses of the insurance company.

(ee) *Significant trading assets and liabilities* means with respect to a banking entity that:

(1) (i) The banking entity has, together with its affiliates and subsidiaries, trading assets and liabilities the average gross sum of which over the previous consecutive four quarters, as measured as of the last day of each of the four previous calendar quarters, equals or exceeds $20 billion; or

(ii) The Board has determined pursuant to § 248.20(h) of this part that the banking entity should be treated as having significant trading assets and liabilities.

(2) With respect to a banking entity, other than a banking entity described in paragraph (ee)(3) of this section, trading assets and liabilities for purposes of this paragraph (ee) means trading assets and liabilities (excluding trading assets and liabilities attributable to trading activities permitted pursuant to § 248.6(a)(1) and (2) of subpart B) on a worldwide consolidated basis.

(3) (i) With respect to a banking entity that is a foreign banking organization or a subsidiary of a foreign banking organization, trading assets and liabilities for purposes of this paragraph (ee) means the trading assets and liabilities (excluding trading assets and liabilities attributable to trading activities permitted pursuant to § 248.6(a)(1) and (2) of subpart (B) of the combined U.S. operations of the top-tier foreign banking organization (including all subsidiaries, affiliates, branches, and agencies of the foreign banking organization operating, located, or organized in the United States as well as branches outside the United States that are managed or controlled by a branch or agency of the foreign banking entity operating, located or organized in the United States).

(ii) For purposes of paragraph (ee)(3)(i) of this section, a U.S. branch, agency, or subsidiary of a banking entity is located in the United States; however, the foreign bank that operates or controls that branch, agency, or subsidiary is not considered to be located in the United States solely by virtue of operating or controlling the U.S. branch, agency, or subsidiary. For purposes of paragraph (ee)(3)(i) of this section, all foreign operations of a U.S. agency, branch, or subsidiary of a foreign banking organization are considered to be located in the United States for purposes of calculating the banking entity's U.S. trading assets and liabilities.

(ff) *State* means any State, the District of Columbia, the Commonwealth of Puerto Rico, Guam, American Samoa, the United States Virgin Islands, and the Commonwealth of the Northern Mariana Islands.

(gg) *Subsidiary* has the same meaning as in section 2(d) of the Bank Holding Company Act of 1956 (12 U.S.C. 1841(d)).

(hh) *State insurance regulator* means the insurance commissioner, or a similar official or agency, of a State that is engaged in the supervision of insurance companies under State insurance law.

(ii) *Swap dealer* has the same meaning as in section 1(a)(49) of the Commodity Exchange Act (7 U.S.C. 1a(49)).

* * * * *

§ 248.6 Other permitted proprietary trading activities.

* * * * *

(f) *Permitted trading activities of qualifying foreign excluded funds*. The prohibition contained in § 248.3(a) does not apply to the purchase or sale of a financial instrument by a qualifying foreign excluded fund. For purposes of this paragraph (f), a qualifying foreign excluded fund means a banking entity that:

(1) Is organized or established outside the United States, and the ownership interests of which are offered and sold solely outside the United States;

(2) (i) Would be a covered fund if the entity were organized or established in the United States, or

(ii) Is, or holds itself out as being, an entity or arrangement that raises money from investors primarily for the purpose of investing in financial instruments for resale or other disposition or otherwise trading in financial instruments;

(3) Would not otherwise be a banking entity except by virtue of the acquisition or retention of an ownership interest in, sponsorship of, or relationship with the entity, by another banking entity that meets the following:

(i) The banking entity is not organized, or directly or indirectly controlled by a banking entity that is organized, under the laws of the United States or of any State; and

(ii) The banking entity's acquisition or retention of an ownership interest in or sponsorship of the fund meets the requirements for permitted covered fund activities and investments solely outside the United States, as provided in section 248.13(b);

(4) Is established and operated as part of a bona fide asset management business; and

(5) Is not operated in a manner that enables any other banking entity to evade the requirements of section 13 of the BHC Act or this part.

* * * * *

Subpart C—Covered Funds Activities and Investments

§ 248.10 Prohibition on acquiring or retaining an ownership interest in and having certain relationships with a covered fund.

(a) *Prohibition.* (1) Except as otherwise provided in this subpart, a banking entity may not, as principal, directly or indirectly, acquire or retain any ownership interest in or sponsor a covered fund.

(2) Paragraph (a)(1) of this section does not include acquiring or retaining an ownership interest in a covered fund by a banking entity:

(i) Acting solely as agent, broker, or custodian, so long as;

(A) The activity is conducted for the account of, or on behalf of, a customer; and

(B) The banking entity and its affiliates do not have or retain beneficial ownership of such ownership interest;

(ii) Through a deferred compensation, stock-bonus, profit-sharing, or pension plan of the banking entity (or an affiliate thereof) that is established and administered in accordance with the law of the United States or a foreign sovereign, if the ownership interest is held or controlled directly or indirectly by the banking entity as trustee for the benefit of persons who are or were employees of the banking entity (or an affiliate thereof);

(iii) In the ordinary course of collecting a debt previously contracted in good faith, provided that the banking entity divests the ownership interest as soon as practicable, and in no event may the banking entity retain such ownership interest for longer than such period permitted by the Board; or

(iv) On behalf of customers as trustee or in a similar fiduciary capacity for a customer that is not a covered fund, so long as:

(A) The activity is conducted for the account of, or on behalf of, the customer; and

(B) The banking entity and its affiliates do not have or retain beneficial ownership of such ownership interest.

(b) *Definition of covered fund.* (1) Except as provided in paragraph (c) of this section, covered fund means:

(i) An issuer that would be an investment company, as defined in the Investment Company Act of 1940 (15 U.S.C. 80a–1 *et seq.*), *but for* section 3(c)(1) or 3(c)(7) of that Act (15 U.S.C. 80a–3(c)(1) or (7));

(ii) Any commodity pool under section 1a(10) of the Commodity Exchange Act (7 U.S.C. 1a(10)) for which:

(A) The commodity pool operator has claimed an exemption under 17 CFR 4.7; or

(B) (*1*) A commodity pool operator is registered with the CFTC as a commodity pool operator in connection with the operation of the commodity pool;

(2) Substantially all participation units of the commodity pool are owned by qualified eligible persons under 17 CFR 4.7(a)(2) and (3); and

(3) Participation units of the commodity pool have not been publicly offered to persons who are not qualified eligible persons under 17 CFR 4.7(a)(2) and (3); or

(iii) For any banking entity that is, or is controlled directly or indirectly by a banking entity that is, located in or organized under the laws of the United States or of any State, an entity that:

(A) Is organized or established outside the United States and the ownership interests of which are offered and sold solely outside the United States;

(B) Is, or holds itself out as being, an entity or arrangement that raises money from investors primarily for the purpose of investing in securities for resale or other disposition or otherwise trading in securities; and

(C) *(1)* Has as its sponsor that banking entity (or an affiliate thereof); or

(2) Has issued an ownership interest that is owned directly or indirectly by that banking entity (or an affiliate thereof).

(2) An issuer shall not be deemed to be a covered fund under paragraph (b)(1)(iii) of this section if, were the issuer subject to U.S. securities laws, the issuer could rely on an exclusion or exemption from the definition of "investment company" under the Investment Company Act of 1940 (15 U.S.C. 80a–1 et seq.) other than the exclusions contained in section 3(c)(1) and 3(c)(7) of that Act.

(3) For purposes of paragraph (b)(1)(iii) of this section, a U.S. branch, agency, or subsidiary of a foreign banking entity is located in the United States; however, the foreign bank that operates or controls that branch, agency, or subsidiary is not considered to be located in the United States solely by virtue of operating or controlling the U.S. branch, agency, or subsidiary.

(c) Notwithstanding paragraph (b) of this section, unless the appropriate Federal banking agencies, the SEC, and the CFTC jointly determine otherwise, a covered fund does not include:

(1) *Foreign public funds*.

(i) Subject to paragraphs (ii) and (iii) below, an issuer that:

(A) Is organized or established outside of the United States; and

(B) Is authorized to offer and sell ownership interests, ~~to retail investors in the issuer's home jurisdiction; and~~ and such interests are offered and sold, through one or more public offerings.

~~(C) Sells ownership interests predominantly through one or more public offerings outside of the United States.~~

(ii) With respect to a banking entity that is, or is controlled directly or indirectly by a banking entity that is, located in or organized under the laws of the United States or of any State and any issuer for which such banking entity acts as sponsor, the sponsoring banking entity may not rely on the exemption in paragraph (c)(1)(i) of this section for such issuer unless ownership interests in the issuer are sold predominantly to persons other than:

(A) Such sponsoring banking entity;

(B) Such issuer;

(C) Affiliates of such sponsoring banking entity or such issuer; and

(D) Directors and ~~employees~~senior executive officers as defined in section 225.71(c) of the Board's Regulation Y (12 CFR 225.71(c)) of such entities.

(iii) For purposes of paragraph (c)(1)(i)(~~C~~B) of this section, the term "public offering" means a distribution (as defined in § 248.4(a)(3) of subpart B) of securities in any jurisdiction outside the United States to investors, including retail investors, provided that:

(A) The distribution ~~complies with all applicable requirements in the jurisdiction in which such distribution is being made~~is subject to substantive disclosure and retail investor protection laws or regulations;

(B) With respect to an issuer for which the banking entity serves as the investment manager, investment adviser, commodity trading adviser, commodity pool operator, or sponsor, the distribution complies with all applicable requirements in the jurisdiction in which such distribution is being made;

(~~B~~C) The distribution does not restrict availability to investors having a minimum level of net worth or net investment assets; and

(~~C~~D) The issuer has filed or submitted, with the appropriate regulatory authority in such jurisdiction, offering disclosure documents that are publicly available.

(2) *Wholly-owned subsidiaries.* An entity, all of the outstanding ownership interests of which are owned directly or indirectly by the banking entity (or an affiliate thereof), except that:

(i) Up to five percent of the entity's outstanding ownership interests, less any amounts outstanding under paragraph (c)(2)(ii) of this section, may be held by employees or directors of the banking entity or such affiliate (including former employees or directors if their ownership interest was acquired while employed by or in the service of the banking entity); and

(ii) Up to 0.5 percent of the entity's outstanding ownership interests may be held by a third party if the ownership interest is acquired or retained by the third party for the purpose of establishing corporate separateness or addressing bankruptcy, insolvency, or similar concerns.

(3) *Joint ventures.* A joint venture between a banking entity or any of its affiliates and one or more unaffiliated persons, provided that the joint venture:

(i) Is ~~comprised~~ composed of no more than 10 unaffiliated co-venturers;

(ii) Is in the business of engaging in activities that are permissible for the banking entity or affiliate, other than investing in securities for resale or other disposition; and

(iii) Is not, and does not hold itself out as being, an entity or arrangement that raises money from investors primarily for the purpose of investing in securities for resale or other disposition or otherwise trading in securities.

(4) *Acquisition vehicles*. An issuer:

(i) Formed solely for the purpose of engaging in a *bona fide* merger or acquisition transaction; and

(ii) That exists only for such period as necessary to effectuate the transaction.

(5) *Foreign pension or retirement funds.* A plan, fund, or program providing pension, retirement, or similar benefits that is:

(i) Organized and administered outside the United States;

(ii) A broad-based plan for employees or citizens that is subject to regulation as a pension, retirement, or similar plan under the laws of the jurisdiction in which the plan, fund, or program is organized and administered; and

(iii) Established for the benefit of citizens or residents of one or more foreign sovereigns or any political subdivision thereof.

(6) *Insurance company separate accounts.* A separate account, provided that no banking entity other than the insurance company participates in the account's profits and losses.

(7) *Bank owned life insurance.* A separate account that is used solely for the purpose of allowing one or more banking entities to purchase a life insurance policy for which the banking entity or entities is beneficiary, provided that no banking entity that purchases the policy:

(i) Controls the investment decisions regarding the underlying assets or holdings of the separate account; or

(ii) Participates in the profits and losses of the separate account other than in compliance with applicable requirements regarding bank owned life insurance.

(8) *Loan securitizations*—(i) *Scope.* An issuing entity for asset-backed securities that satisfies all the conditions of this paragraph (c)(8) and the assets or holdings of which are ~~comprised~~composed solely of:

(A) Loans as defined in § 248.2(t) of subpart A;

(B) Rights or other assets designed to assure the servicing or timely distribution of proceeds to holders of such securities and rights or other assets that are related or incidental to purchasing or otherwise acquiring and holding the loans, provided that each asset that is a security (other than special units of beneficial interest and collateral certificates meeting the requirements of paragraph (c)(8)(v) of this section) meets the requirements of paragraph (c)(8)(iii) of this section;

(C) Interest rate or foreign exchange derivatives that meet the requirements of paragraph (c)(8)(iv) of this section; and

(D) Special units of beneficial interest and collateral certificates that meet the requirements of paragraph (c)(8)(v) of this section.

(E) Any other assets, provided that the aggregate value of any such other assets that do not meet the criteria specified in paragraphs (c)(8)(i)(A) through (c)(8)(i)(D) above do not exceed five percent of the aggregate value of the issuing entity's assets.

(ii) *Impermissible assets*. For purposes of this paragraph (c)(8), except as permitted under paragraph (c)(8)(i)(E) above, the assets or holdings of the issuing entity shall not include any of the following:

(A) A security, including an asset-backed security, or an interest in an equity or debt security other than as permitted in paragraphparagraphs (c)(8)(iii), (iv), or (v) of this section;

(B) A derivative, other than a derivative that meets the requirements of paragraph (c)(8)(iv) of this section; or

(C) A commodity forward contract.

(iii) *Permitted securities*. Notwithstanding paragraph (c)(8)(ii)(A) of this section, the issuing entity may hold securities if those securities are:

(A) Cash equivalents – which, for the purposes of this paragraph, means high quality, highly liquid investments whose maturity corresponds to the securitization's expected or potential need for funds and whose currency corresponds to either the underlying loans or the asset-backed securities – for purposes of the rights and assets in paragraph (c)(8)(i)(B) of this section; or

(B) Securities received in lieu of debts previously contracted with respect to the loans supporting the asset-backed securities.

(iv) *Derivatives.* The holdings of derivatives by the issuing entity shall be limited to interest rate or foreign exchange derivatives that satisfy all of the following conditions:

(A) The written terms of the derivativederivatives directly relate to the loans, the asset-backed securities, or the contractual rights ofor other assets described in paragraph (c)(8)(i)(B) of this section; and

(B) The derivatives reduce the interest rate and/or foreign exchange risks related to the loans, the asset-backed securities, or the contractual rights or other assets described in paragraph (c)(8)(i)(B) of this section.

(v) *Special units of beneficial interest and collateral certificates*. The assets or holdings of the issuing entity may include collateral certificates and special units of beneficial interest issued by a special purpose vehicle, provided that:

(A) The special purpose vehicle that issues the special unit of beneficial interest or collateral certificate meets the requirements in this paragraph (c)(8);

(B) The special unit of beneficial interest or collateral certificate is used for the sole purpose of transferring to the issuing entity for the loan securitization the economic risks and benefits of the assets that are permissible for loan securitizations under this paragraph (c)(8) and does not directly or indirectly transfer any interest in any other economic or financial exposure;

(C) The special unit of beneficial interest or collateral certificate is created solely to satisfy legal requirements or otherwise facilitate the structuring of the loan securitization; and

(D) The special purpose vehicle that issues the special unit of beneficial interest or collateral certificate and the issuing entity are established under the direction of the same entity that initiated the loan securitization.

(9) *Qualifying asset-backed commercial paper conduits.* (i) An issuing entity for asset-backed commercial paper that satisfies all of the following requirements:

(A) The asset-backed commercial paper conduit holds only:

(*1*) Loans and other assets permissible for a loan securitization under paragraph (c)(8)(i) of this section; and

(*2*) Asset-backed securities supported solely by assets that are permissible for loan securitizations under paragraph (c)(8)(i) of this section and acquired by the asset-backed commercial paper conduit as part of an initial issuance either directly from the issuing entity of the asset-backed securities or directly from an underwriter in the distribution of the asset-backed securities;

(B) The asset-backed commercial paper conduit issues only asset-backed securities, comprised of a residual interest and securities with a legal maturity of 397 days or less; and

(C) A regulated liquidity provider has entered into a legally binding commitment to provide full and unconditional liquidity coverage with respect to all of the outstanding asset- backed securities issued by the asset- backed commercial paper conduit (other than any residual interest) in the event that funds are required to redeem maturing asset-backed securities.

(ii) For purposes of this paragraph (c)(9), a regulated liquidity provider means:

(A) A depository institution, as defined in section 3(c) of the Federal Deposit Insurance Act (12 U.S.C. 1813(c));

(B) A bank holding company, as defined in section 2(a) of the Bank Holding Company Act of 1956 (12 U.S.C. 1841(a)), or a subsidiary thereof;

(C) A savings and loan holding company, as defined in section 10a of the Home Owners' Loan Act (12 U.S.C. 1467a), provided all or substantially all of the holding company's activities are permissible for a financial holding company under section 4(k) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(k)), or a subsidiary thereof;

(D) A foreign bank whose home country supervisor, as defined in § 211.21(q) of the Board's Regulation K (12 CFR 211.21(q)), has adopted capital standards consistent with the Capital Accord for the Basel Committee on banking Supervision, as amended, and that is subject to such standards, or a subsidiary thereof; or

(E) The United States or a foreign sovereign.

(10) *Qualifying covered bonds*—(i) Scope. An entity owning or holding a dynamic or fixed pool of loans or other assets as provided in paragraph (c)(8) of this section for the benefit of the holders of covered bonds, provided that the assets in the pool are ~~comprised~~ composed solely of assets that meet the conditions in paragraph (c)(8)(i) of this section.

(ii) *Covered bond.* For purposes of this paragraph (c)(10), a covered bond means:

(A) A debt obligation issued by an entity that meets the definition of foreign banking organization, the payment obligations of which are fully and unconditionally guaranteed by an entity that meets the conditions set forth in paragraph (c)(10)(i) of this section; or

(B) A debt obligation of an entity that meets the conditions set forth in paragraph (c)(10)(i) of this section, provided that the payment obligations are fully and unconditionally guaranteed by an entity that meets the definition of foreign banking organization and the entity is a wholly-owned subsidiary, as defined in paragraph (c)(2) of this section, of such foreign banking organization.

(11) *SBICs and public welfare investment funds*. An issuer:

(i) That is a small business investment company, as defined in section 103(3) of the Small Business Investment Act of 1958 (15 U.S.C. 662), or that has received from the Small Business Administration notice to proceed to qualify for a license as a small business investment company, which notice or license has not been revoked, or that has voluntarily surrendered its license to operate as a small business investment company in accordance with 13 CFR 107.1900 and does not make any new investments (other than investments in cash equivalents, which, for the purposes of this paragraph, means high quality, highly liquid investments whose maturity corresponds to the issuer's expected or potential need for funds and whose currency corresponds to the issuer's assets) after such voluntary surrender; or

(ii) The business of which is to make investments that are:

(A) Designed primarily to promote the public welfare, of the type permitted under paragraph (11) of section 5136 of the Revised Statutes of the United States (12 U.S.C. 24), including the welfare of low- and moderate-income communities or families (such as providing housing, services, or jobs); or

(B) Qualified rehabilitation expenditures with respect to a qualified rehabilitated building or certified historic structure, as such terms are defined in section 47 of the Internal Revenue Code of 1986 or a similar State historic tax credit program.

(12) Registered investment companies and excluded entities. An issuer:

(i) That is registered as an investment company under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a–8), or that is formed and operated pursuant to a written plan to become a registered investment company as described in § 248.20(e)(3) of subpart D and that complies with the requirements of section 18 of the Investment Company Act of 1940 (15 U.S.C. 80a–18);

(ii) That may rely on an exclusion or exemption from the definition of "investment company" under the Investment Company Act of 1940 (15 U.S.C. 80a–1 *et seq.*) other than the exclusions contained in section 3(c)(1) and 3(c)(7) of that Act; or

(iii) That has elected to be regulated as a business development company pursuant to section 54(a) of that Act (15 U.S.C. 80a–53) and has not withdrawn its election, or that is formed and operated pursuant to a written plan to become a business development company as described in § 248.20(e)(3) of subpart D and that complies with the requirements of section 61 of the Investment Company Act of 1940 (15 U.S.C. 80a–60).

(13) *Issuers in conjunction with the FDIC's receivership or conservatorship operations.* An issuer that is an entity formed by or on behalf of the FDIC for the purpose of facilitating the disposal of assets acquired in the FDIC's capacity as conservator or receiver under the Federal Deposit Insurance Act or Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

(14) *Other excluded issuers.* (i) Any issuer that the appropriate Federal banking agencies, the SEC, and the CFTC jointly determine the exclusion of which is consistent with the purposes of section 13 of the BHC Act.

(ii) A determination made under paragraph (c)(14)(i) of this section will be promptly made public.

(15) *Credit funds*. Subject to paragraphs (c)(15)(iii), (iv), and (v) of this section, an issuer that satisfies the asset and activity requirements of paragraphs (c)(15)(i) and (ii) of this section.

(i) *Asset requirements*. The issuer's assets must be composed solely of:

(A) Loans as defined in section 248.2(t) of subpart A;

(B) Debt instruments, subject to paragraph (c)(15)(iv) of this section;

(C) Rights and other assets that are related or incidental to acquiring, holding, servicing, or selling such loans or debt instruments, provided that:

(*1*) each right or asset that is a security is either:

(*i*) a cash equivalent (which, for the purposes of this paragraph, means high quality, highly liquid investments whose maturity corresponds to the issuer's expected or potential need for funds and whose currency corresponds to either the underlying loans or the debt instruments);

(*ii*) a security received in lieu of debts previously contracted with respect to such loans or debt instruments; or

(*iii*) an equity security (or right to acquire an equity security) received on customary terms in connection with such loans or debt instruments; and

(*2*) Rights or other assets held under this paragraph (c)(15)(i)(C) may not include commodity forward contracts; and

(D) Interest rate or foreign exchange derivatives, if:

(*1*) The written terms of the derivative directly relate to the loans, debt instruments, or other rights or assets described in paragraph (c)(15)(i)(C) of this section; and

(*2*) The derivative reduces the interest rate and/or foreign exchange risks related to the loans, debt instruments, or other rights or assets described in paragraph (c)(15)(i)(C) of this section.

(ii) *Activity requirements*. To be eligible for the exclusion of paragraph (c)(15) of this section, an issuer must:

(A) Not engage in any activity that would constitute proprietary trading under § 248.3(b)(l)(i) of subpart A, as if the issuer were a banking entity; and

(B) Not issue asset-backed securities.

(iii) *Requirements for a sponsor, investment adviser, or commodity trading advisor*. A banking entity that acts as a sponsor, investment adviser, or commodity trading advisor to an issuer that meets the conditions in paragraphs (c)(15)(i) and (ii) of this section may not rely on this exclusion unless the banking entity:

(A) Provides in writing to any prospective and actual investor in the issuer the disclosures required under § 248.11(a)(8) of this subpart, as if the issuer were a covered fund; and

(B) Ensures that the activities of the issuer are consistent with safety and soundness standards that are substantially similar to those that would apply if the banking entity engaged in the activities directly.

(iv) A banking entity may not rely on this exclusion with respect to an issuer that meets the conditions in paragraphs (c)(15)(i) and (ii) of this section unless:

(A) The banking entity does not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of the issuer or of any entity to which such issuer extends credit or in which such issuer invests; and

(B) Any assets the issuer holds pursuant to paragraphs (c)(15)(i)(B) or (i)(C)(*1*)(*iii*) of this section would be permissible for the banking entity to acquire and hold directly.

(v) A banking entity's investment in, and relationship with, the issuer must:

(A) Comply with the limitations imposed in §§ 248.14 (except the banking entity may acquire and retain any ownership interest in the issuer) and 248.15 of this subpart, as if the issuer were a covered fund; and

(B) Be conducted in compliance with, and subject to, applicable banking laws and regulations, including applicable safety and soundness standards.

(16) *Qualifying venture capital funds*.

(i) Subject to paragraphs (c)(16)(ii) through (iv) of this section, an issuer that:

(A) Is a venture capital fund as defined in 17 CFR § 275.203(l)-1; and

(B) Does not engage in any activity that would constitute proprietary trading under section 248.3(b)(1)(i), as if the issuer were a banking entity.

(ii) A banking entity that acts as a sponsor, investment adviser, or commodity trading advisor to an issuer that meets the conditions in paragraph (c)(16)(i) of this section may not rely on this exclusion unless the banking entity:

(A) Provides in writing to any prospective and actual investor in the issuer the disclosures required under section _.11 (a)(8) of this subpart, as if the issuer were a covered fund; and

(B) Ensures that the activities of the issuer are consistent with safety and soundness standards that are substantially similar to those that would apply if the banking entity engaged in the activities directly.(iii) [*sic*] The banking entity must not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of the issuer.

(iv) A banking entity’s ownership interest in or relationship with the issuer must:

(A) Comply with the limitations imposed in §§ 248.14 (except the banking entity may acquire and retain any ownership interest in the issuer) and 248.15 of this subpart, as if the issuer were a covered fund; and

(B) Be conducted in compliance with, and subject to, applicable banking laws and regulations, including applicable safety and soundness standards.

(17) *Family wealth management vehicles*.

(i) Subject to paragraph (c)(17)(ii) of this section, any entity that is not, and does not hold itself out as being, an entity or arrangement that raises money from investors primarily for the purpose of investing in securities for resale or other disposition or otherwise trading in securities, and:

(A) If the entity is a trust, the grantor(s) of the entity are all family customers; and

(B) If the entity is not a trust:

(1) A majority of the voting interests in the entity are owned (directly or indirectly) by family customers; and

(2) The entity is owned only by family customers and up to 3 closely related persons of the family customers.

(ii) A banking entity may rely on the exclusion in paragraph (c)(17)(i) of this section with respect to an entity provided that the banking entity (or an affiliate):

(A) Provides bona fide trust, fiduciary, investment advisory, or commodity trading advisory services to the entity;

(B) Does not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of such entity;

(C) Complies with the disclosure obligations under § 248.11(a)(8), as if such entity were a covered fund;

(D) Does not acquire or retain, as principal, an ownership interest in the entity, other than up to 0.5 percent of the entity's outstanding ownership interests that may be held by the banking entity and its affiliates for the purpose of and to the extent necessary for establishing corporate separateness or addressing bankruptcy, insolvency, or similar concerns;

(E) Complies with the requirements of §§ 248.14(b) and 248.15, as if such entity were a covered fund; and

(F) Complies with the requirements of 12 CFR 223.15(a), as if such banking entity and its affiliates were a member bank and the issuer were an affiliate thereof.

(iii) For purposes of paragraph (c)(17) of this section, the following definitions apply:

(A) "Closely related person" means a natural person (including the estate and estate planning vehicles of such person) who has longstanding business or personal relationships with any family customer.

(B) "Family customer" means:

(1) A family client, as defined in Rule 202(a)(11)(G)-1(d)(4) of the Investment Advisers Act of 1940 (17 CFR 275.202(a)(11)(G)-1(d)(4)); or

(2) Any natural person who is a father-in-law, mother-in-law, brother-in-law, sister-in-law, son-in-law or daughter-in-law of a family client, or a spouse or a spousal equivalent of any of the foregoing.

(18) *Customer facilitation vehicles*.

(i) Subject to paragraph (c)(18)(ii) of this section, an issuer that is formed by or at the request of a customer of the banking entity for the purpose of providing such customer (which may include one or more affiliates of such customer) with exposure to a transaction, investment strategy, or other service provided by the banking entity.

(ii) A banking entity may rely on the exclusion in paragraph (c)(18)(i) of this section with respect to an issuer provided that:

(A) All of the ownership interests of the issuer are owned by the customer (which may include one or more of its affiliates) for whom the issuer was created, subject to paragraph (c)(18)(ii)(B)(*4*) of this section; and

(B) The banking entity and its affiliates:

(*1*) Maintain documentation outlining how the banking entity intends to facilitate the customer's exposure to such transaction, investment strategy, or service;

(*2*) Do not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of such issuer;

(*3*) Comply with the disclosure obligations under § 248.11(a)(8), as if such issuer were a covered fund;

(*4*) Do not acquire or retain, as principal, an ownership interest in the issuer, other than up to 0.5 percent of the issuer's outstanding ownership interests that may be held by the banking entity and its affiliates for the purpose of and to the extent necessary for establishing corporate separateness or addressing bankruptcy, insolvency, or similar concerns;

(*5*) Comply with the requirements of § 248.14(b) and 248.15, as if such issuer were a covered fund; and

(*6*) Comply with the requirements of 12 CFR 223.15(a), as if such banking entity and its affiliates were a member bank and the issuer were an affiliate thereof.

(d) Definition of other terms related to covered funds. For purposes of this subpart:

(1) *Applicable accounting standards* means U.S. generally accepted accounting principles, or such other accounting standards applicable to a banking entity that the Board determines are appropriate and that the banking entity uses in the ordinary course of its business in preparing its consolidated financial statements.

(2) *Asset-backed security* has the meaning specified in Section 3(a)(79) of the Exchange Act (15 U.S.C. 78c(a)(79)).

(3) *Director* has the same meaning as provided in section 215.2(d)(1) of the Board's Regulation O (12 CFR 215.2(d)(1)).

(4) *Issuer* has the same meaning as in section 2(a)(22) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(22)).

(5) *Issuing entity* means with respect to asset-backed securities the special purpose vehicle that owns or holds the pool assets underlying asset-backed securities and in whose name the asset- backed securities supported or serviced by the pool assets are issued.

(6) *Ownership interest*—(i) Ownership interest means any equity, partnership, or other similar interest. An "other similar interest" means an interest that:

(A) Has the right to participate in the selection or removal of a general partner, managing member, member of the board of directors or trustees, investment manager, investment adviser, or commodity trading advisor of the covered fund (excluding the rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event, which includes the right to participate in the removal of an investment manager for cause or to nominate or vote on a nominated replacement manager upon an investment manager's resignation or removal);

(B) Has the right under the terms of the interest to receive a share of the income, gains or profits of the covered fund;

(C) Has the right to receive the underlying assets of the covered fund after all other interests have been redeemed and/or paid in full (excluding the rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event);

(D) Has the right to receive all or a portion of excess spread (the positive difference, if any, between the aggregate interest payments received from the underlying assets of the covered fund and the aggregate interest paid to the holders of other outstanding interests);

(E) Provides under the terms of the interest that the amounts payable by the covered fund with respect to the interest could be reduced based on losses arising from the underlying assets of the covered fund, such as allocation of losses, write-downs or charge-offs of the outstanding principal balance, or reductions in the amount of interest due and payable on the interest;

(F) Receives income on a pass-through basis from the covered fund, or has a rate of return that is determined by reference to the performance of the underlying assets of the covered fund; or

(G) Any synthetic right to have, receive, or be allocated any of the rights in paragraphs (d)(6)(i)(A) through (F) of this section.

(ii) Ownership interest does not include:

(A) *Restricted profit interest*. An interest held by an entity (or an employee or former employee thereof) in a covered fund for which the entity (or employee thereof) serves as investment manager, investment adviser, commodity trading advisor, or other service provider so long as:

(~~A~~*1*) The sole purpose and effect of the interest is to allow the entity (or employee or former employee thereof) to share in the profits of the

covered fund as performance compensation for the investment management, investment advisory, commodity trading advisory, or other services provided to the covered fund by the entity (or employee or former employee thereof), provided that the entity (or employee or former employee thereof) may be obligated under the terms of such interest to return profits previously received;

(~~B~~*2*) All such profit, once allocated, is distributed to the entity (or employee or former employee thereof) promptly after being earned or, if not so distributed, is retained by the covered fund for the sole purpose of establishing a reserve amount to satisfy contractual obligations with respect to subsequent losses of the covered fund and such undistributed profit of the entity (or employee or former employee thereof) does not share in the subsequent investment gains of the covered fund;

(*3*) Any amounts invested in the covered fund, including any amounts paid by the entity in connection with obtaining the restricted profit interest, are within the limits of § 248.12 of this subpart; and

(*4*) The interest is not transferable by the entity (or employee or former employee thereof) except to an affiliate thereof (or an employee of the banking entity or affiliate), to immediate family members, or through the intestacy, of the employee or former employee, or in connection with a sale of the business that gave rise to the restricted profit interest by the entity (or employee or former employee thereof) to an unaffiliated party that provides investment management, investment advisory, commodity trading advisory, or other services to the fund.

(B) Any senior loan or senior debt interest that has the following characteristics:

(*1*) Under the terms of the interest the holders of such interest do not have the rights to receive a share of the income, gains, or profits of the covered fund, but are entitled to receive only:

(*i*) Interest at a stated interest rate, as well as commitment fees or other fees, which are not determined by reference to the performance of the underlying assets of the covered fund; and

(*ii*) Fixed principal payments on or before a maturity date (which may include prepayment premiums intended solely to reflect, and compensate holders of the interest for, foregone income resulting from an early prepayment);

(*2*) The entitlement to payments under the terms of the interest are absolute and could not be reduced based on losses arising from the underlying assets of the covered fund, such as allocation of losses, write-downs or charge-offs of the outstanding principal balance, or reductions in the amount of interest due and payable on the interest; and

(*3*) The holders of the interest are not entitled to receive the underlying assets of the covered fund after all other interests have been redeemed or paid in full (excluding the rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event).

(7) *Prime brokerage transaction* means any transaction that would be a covered transaction, as defined in section 23A(b)(7) of the Federal Reserve Act (12 U.S.C. 371c(b)(7)), that is provided in connection with custody, clearance and settlement, securities borrowing or

lending services, trade execution, financing, or data, operational, and administrative support.

(8) *Resident of the United States* means a person that is a "U.S. person" as defined in rule 902(k) of the SEC's Regulation S (17 CFR 230.902(k)).

(9) *Sponsor* means, with respect to a covered fund:

(i) To serve as a general partner, managing member, or trustee of a covered fund, or to serve as a commodity pool operator with respect to a covered fund as defined in (b)(1)(ii) of this section;

(ii) In any manner to select or to control (or to have employees, officers, or directors, or agents who constitute) a majority of the directors, trustees, or management of a covered fund; or

(iii) To share with a covered fund, for corporate, marketing, promotional, or other purposes, the same name or a variation of the same name, except as permitted under § 248.11(a)(6).

(10) *Trustee.* (i) For purposes of paragraph (d)(9) of this section and § 248.11 of subpart C, a trustee does not include:

(A) A trustee that does not exercise investment discretion with respect to a covered fund, including a trustee that is subject to the direction of an unaffiliated named fiduciary who is not a trustee pursuant to section 403(a)(1) of the Employee's Retirement Income Security Act (29 U.S.C. 1103(a)(1)); or

(B) A trustee that is subject to fiduciary standards imposed under foreign law that are substantially equivalent to those described in paragraph (d)(10)(i)(A) of this section;

(ii) Any entity that directs a person described in paragraph (d)(10)(i) of this section, or that possesses authority and discretion to manage and control the investment decisions of a covered fund for which such person serves as trustee, shall be considered to be a trustee of such covered fund.

§ 248.11 Permitted organizing and offering, underwriting, and market making with respect to a covered fund.

(a) *Organizing and offering a covered fund in general.* Notwithstanding § 248.10(a) of this subpart, a banking entity is not prohibited from acquiring or retaining an ownership interest in, or acting as sponsor to, a covered fund in connection with, directly or indirectly, organizing and offering a covered fund, including serving as a general partner, managing member, trustee, or commodity pool operator of the covered fund and in any manner selecting or controlling (or having employees, officers, directors, or agents who constitute) a majority of the directors, trustees, or management of the covered fund, including any necessary expenses for the foregoing, only if:

(1) The banking entity (or an affiliate thereof) provides *bona fide* trust, fiduciary, investment advisory, or commodity trading advisory services;

(2) The covered fund is organized and offered only in connection with the provision of *bona fide* trust, fiduciary, investment advisory, or commodity trading advisory services and only to persons that are customers of such services of the banking entity (or an affiliate thereof), pursuant to a written plan or similar documentation outlining how the banking entity or such affiliate intends to provide advisory or similar services to its customers through organizing and offering such fund;

(3) The banking entity and its affiliates do not acquire or retain an ownership interest in the covered fund except as permitted under § 248.12 of this subpart;

(4) The banking entity and its affiliates comply with the requirements of § 248.14 of this subpart;

(5) The banking entity and its affiliates do not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of the covered fund or of any covered fund in which such covered fund invests;

(6) The covered fund, for corporate, marketing, promotional, or other purposes:

(i) Does not share the same name or a variation of the same name with the banking entity (or an affiliate thereof) except that a covered fund may share the same name or a variation of the same name with a banking entity that is an investment adviser to the covered fund if:

(A) The investment adviser is not an insured depository institution, a company that controls an insured depository institution, or a company that is treated as a bank holding company for purposes of section 8 of the International Banking Act of 1978 (12 U.S.C. 3106); and

(B) The investment adviser does not share the same name or a variation of the same name as an insured depository institution, a company that controls an insured depository institution, or a company that is treated as a bank holding company for purposes of section 8 of the International Banking Act of 1978 (12 U.S.C. 3106); and

(ii) Does not use the word “bank” in its name;

(7) No director or employee of the banking entity (or an affiliate thereof) takes or retains an ownership interest in the covered fund, except for any director or employee of the banking entity or such affiliate who is directly engaged in providing investment advisory, commodity trading advisory, or other services to the covered fund at the time the director or employee takes the ownership interest; and

(8) The banking entity:

(i) Clearly and conspicuously discloses, in writing, to any prospective and actual investor in the covered fund (such as through disclosure in the covered fund’s offering documents):

(A) That “any losses in [such covered fund] will be borne solely by investors in [the covered fund] and not by [the banking entity] or its affiliates; therefore, [the banking entity’s] losses in [such covered fund] will be limited to losses attributable to the ownership interests in the covered fund held by [the banking entity] and any affiliate in its capacity as investor in the [covered fund] or as beneficiary of a restricted profit interest held by [the banking entity] or any affiliate”;

(B) That such investor should read the fund offering documents before investing in the covered fund;

(C) That the “ownership interests in the covered fund are not insured by the FDIC, and are not deposits, obligations of, or endorsed or guaranteed in any way, by any banking entity” (unless that happens to be the case); and

(D) The role of the banking entity and its affiliates and employees in sponsoring or providing any services to the covered fund; and

(ii) Complies with any additional rules of the appropriate Federal banking agencies, the SEC, or the CFTC, as provided in section 13(b)(2) of the BHC Act, designed to ensure that losses in such covered fund are borne solely by investors in the covered fund and not by the covered banking entity and its affiliates.

(b) *Organizing and offering an issuing entity of asset-backed securities.* (1) Notwithstanding § 248.10(a) of this subpart, a banking entity is not prohibited from acquiring or retaining an ownership interest in, or acting as sponsor to, a covered fund that is an issuing entity of asset-backed securities in connection with, directly or indirectly, organizing and offering that issuing entity, so long as the banking entity and its affiliates comply with all of the requirements of paragraph (a)(3) through (8) of this section.

(2) For purposes of this paragraph (b), organizing and offering a covered fund that is an issuing entity of asset-backed securities means acting as the securitizer, as that term is used in section 15G(a)(3) of the Exchange Act (15 U.S.C. 78*o*–11(a)(3)) of the issuing entity, or acquiring or retaining an ownership interest in the issuing entity as required by section 15G of that Act (15 U.S.C. 78*o*–11) and the implementing regulations issued thereunder.

(c) *Underwriting and market making in ownership interests of a covered fund.* The prohibition contained in § 248.10(a) does not apply to a banking entity's underwriting activities or market making-related activities involving a covered fund so long as:

(1) Those activities are conducted in accordance with the requirements of § 248.4(a) or (b), respectively; and

(2) With respect to any banking entity (or any affiliate thereof) that: Acts as a sponsor, investment adviser or commodity trading advisor to a particular covered fund or otherwise acquires and retains an ownership interest in such covered fund in reliance on paragraph (a) of this section; or acquires and retains an ownership interest in such covered fund and is either a securitizer, as that term is used in section 15G(a)(3) of the Exchange Act (15 U.S.C. 78o–11(a)(3)), or is acquiring and retaining an ownership interest in such covered fund in compliance with section 15G of that Act (15 U.S.C. 78o–11) and the implementing regulations issued thereunder each as permitted by paragraph (b) of this section, then in each such case any ownership interests acquired or retained by the banking entity and its affiliates in connection with underwriting and market making related activities for that particular covered fund are included in the calculation of ownership interests permitted to be held by the banking entity and its affiliates under the limitations of § 248.12(a)(2)(ii) and (iii) and (d).

§ 248.12 Permitted investment in a covered fund.

(a) Authority and limitations on permitted investments in covered funds.

(1) Notwithstanding the prohibition contained in § 248.10(a) of this subpart, a banking entity may acquire and retain an ownership interest in a covered fund that the banking entity or an affiliate thereof organizes and offers pursuant to § 248.11, for the purposes of:

(i) *Establishment.* Establishing the fund and providing the fund with sufficient initial equity for investment to permit the fund to attract unaffiliated investors, subject to the limits contained in paragraphs (a)(2)(i) and (iii) of this section; or

(ii) *De minimis investment.* Making and retaining an investment in the covered fund subject to the limits contained in paragraphs (a)(2)(ii) and (iii) of this section.

(2) *Investment limits*—(i) *Seeding period.* With respect to an investment in any covered fund made or held pursuant to paragraph (a)(1)(i) of this section, the banking entity and its affiliates:

(A) Must actively seek unaffiliated investors to reduce, through redemption, sale, dilution, or other methods, the aggregate amount of all ownership interests of the banking entity in the covered fund to the amount permitted in paragraph (a)(2)(i)(B) of this section; and

(B) Must, no later than 1 year after the date of establishment of the fund (or such longer period as may be provided by the Board pursuant to paragraph (e) of this section), conform its ownership interest in the covered fund to the limits in paragraph (a)(2)(ii) of this section;

(ii) *Per-fund limits.* (A) Except as provided in paragraph (a)(2)(ii)(B) of this section, an investment by a banking entity and its affiliates in any covered fund made or held pursuant to paragraph (a)(1)(ii) of this section may not exceed 3 percent of the total number or value of the outstanding ownership interests of the fund.

(B) An investment by a banking entity and its affiliates in a covered fund that is an issuing entity of asset-backed securities may not exceed 3 percent of the total fair market value of the ownership interests of the fund measured in accordance with paragraph (b)(3) of this section, unless a greater percentage is retained by the banking entity and its affiliates in compliance with the requirements of section 15G of the Exchange Act (15 U.S.C. 78*o*–11) and the implementing regulations issued thereunder, in which case the investment by the banking entity and its affiliates in the covered fund may not exceed the amount, number, or value of ownership interests of the fund required under section 15G of the Exchange Act and the implementing regulations issued thereunder.

(iii) *Aggregate limit.* The aggregate value of all ownership interests of the banking entity and its affiliates in all covered funds acquired or retained under this section may not exceed 3 percent of the tier 1 capital of the banking entity, as provided under paragraph (c) of this section, and shall be calculated as of the last day of each calendar quarter.

(iv) *Date of establishment.* For purposes of this section, the date of establishment of a covered fund shall be:

(A) *In general.* The date on which the investment adviser or similar entity to the covered fund begins making investments pursuant to the written investment strategy for the fund;

(B) *Issuing entities of asset-backed securities.* In the case of an issuing entity of asset-backed securities, the date on which the assets are initially transferred into the issuing entity of asset-backed securities.

(b) *Rules of construction*—(1) *Attribution of ownership interests to a covered banking entity.* (i) For purposes of paragraph (a)(2) of this section, the amount and value of a banking entity's permitted investment in any single covered fund shall include any ownership interest held under § 248.12 directly by the banking entity, including any affiliate of the banking entity.

(ii) *Treatment of registered investment companies, SEC-regulated business development companies, and foreign public funds.* For purposes of paragraph (b)(1)(i) of this section, a registered investment company, SEC-regulated business development companies or foreign public fund as described in §

248.10(c)(1) of this subpart will not be considered to be an affiliate of the banking entity so long as the banking entity:

(A) Does not own, control, or hold with the power to vote 25 percent or more of the voting shares of the company or fund; and

(B) Provides investment advisory, commodity trading advisory, administrative, and other services to the company or fund in compliance with the limitations under applicable regulation, order, or other authority.

(iii) *Covered funds.* For purposes of paragraph (b)(1)(i) of this section, a covered fund will not be considered to be an affiliate of a banking entity so long as the covered fund is held in compliance with the requirements of this subpart.

(iv) *Treatment of employee and director investments financed by the banking entity.* For purposes of paragraph (b)(1)(i) of this section, an investment by a director or employee of a banking entity who acquires an ownership interest in his or her personal capacity in a covered fund sponsored by the banking entity will be attributed to the banking entity if the banking entity, directly or indirectly, extends financing for the purpose of enabling the director or employee to acquire the ownership interest in the fund and the financing is used to acquire such ownership interest in the covered fund.

(2) *Calculation of permitted ownership interests in a single covered fund.* Except as provided in paragraph (b)(3) or (4), for purposes of determining whether an investment in a single covered fund complies with the restrictions on ownership interests under paragraphs (a)(2)(i)(B) and (a)(2)(ii)(A) of this section:

(i) The aggregate number of the outstanding ownership interests held by the banking entity shall be the total number of ownership interests held under this section by the banking entity in a covered fund divided by the total number of ownership interests held by all entities in that covered fund, as of the last day of each calendar quarter (both measured without regard to committed funds not yet called for investment);

(ii) The aggregate value of the outstanding ownership interests held by the banking entity shall be the aggregate fair market value of all investments in and capital contributions made to the covered fund by the banking entity, divided by the value of all investments in and capital contributions made to that covered fund by all entities, as of the last day of each calendar quarter (all measured without regard to committed funds not yet called for investment). If fair market value cannot be determined, then the value shall be the historical cost basis of all investments in and contributions made by the banking entity to the covered fund;

(iii) For purposes of the calculation under paragraph (b)(2)(ii) of this section, once a valuation methodology is chosen, the banking entity must calculate the value of its investment and the investments of all others in the covered fund in the same manner and according to the same standards.

(3) *Issuing entities of asset-backed securities.* In the case of an ownership interest in an issuing entity of asset- backed securities, for purposes of determining whether an investment in a single covered fund complies with the restrictions on ownership interests under paragraphs (a)(2)(i)(B) and (a)(2)(ii)(B) of this section:

(i) For securitizations subject to the requirements of section 15G of the Exchange Act (15 U.S.C. 78o–11), the calculations shall be made as of the date and according to the valuation methodology applicable pursuant to the requirements

of section 15G of the Exchange Act (15 U.S.C. 78o–11) and the implementing regulations issued thereunder; or

(ii) For securitization transactions completed prior to the compliance date of such implementing regulations (or as to which such implementing regulations do not apply), the calculations shall be made as of the date of establishment as defined in paragraph (a)(2)(iv)(B) of this section or such earlier date on which the transferred assets have been valued for purposes of transfer to the covered fund, and thereafter only upon the date on which additional securities of the issuing entity of asset-backed securities are priced for purposes of the sales of ownership interests to unaffiliated investors.

(iii) For securitization transactions completed prior to the compliance date of such implementing regulations (or as to which such implementing regulations do not apply), the aggregate value of the outstanding ownership interests in the covered fund shall be the fair market value of the assets transferred to the issuing entity of the securitization and any other assets otherwise held by the issuing entity at such time, determined in a manner that is consistent with its determination of the fair market value of those assets for financial statement purposes.

(iv) For purposes of the calculation under paragraph (b)(3)(iii) of this section, the valuation methodology used to calculate the fair market value of the ownership interests must be the same for both the ownership interests held by a banking entity and the ownership interests held by all others in the covered fund in the same manner and according to the same standards.

(4) *Multi-tier fund investments*—(i) *Master-feeder fund investments*. If the principal investment strategy of a covered fund (the "feeder fund") is to invest substantially all of its assets in another single covered fund (the "master fund"), then for purposes of the investment limitations in paragraphs (a)(2)(i)(B) and (a)(2)(ii) of this section, the banking entity's permitted investment in such funds shall be measured only by reference to the value of the master fund. The banking entity's permitted investment in the master fund shall include any investment by the banking entity in the master fund, as well as the banking entity's pro-rata share of any ownership interest ~~of~~in the master fund that is held through the feeder fund; and

(ii) *Fund-of-funds investments*. If a banking entity organizes and offers a covered fund pursuant to § 248.11 of this subpart for the purpose of investing in other covered funds (a "fund of funds") and that fund of funds itself invests in another covered fund that the banking entity is permitted to own, then the banking entity's permitted investment in that other fund shall include any investment by the banking entity in that other fund, as well as the banking entity's pro-rata share of any ownership interest ~~of~~in the fund that is held through the fund of funds. The investment of the banking entity may not represent more than 3 percent of the amount or value of any single covered fund.

(5) *Parallel Investments and Co-Investments*—(i) A banking entity shall not be required to include in the calculation of the investment limits under paragraph (a)(2) of this section any investment the banking entity makes alongside a covered fund as long as the investment is made in compliance with applicable laws and regulations, including applicable safety and soundness standards.

(ii) A banking entity shall not be restricted under this section in the amount of any investment the banking entity makes alongside a covered fund as long as the investment is made in compliance with applicable laws and regulations, including applicable safety and soundness standards.

(c) *Aggregate permitted investments in all covered funds.* (1)(i) For purposes of paragraph (a)(2)(iii) of this section, the aggregate value of all ownership interests held by a banking entity shall be the sum of all amounts paid or contributed by the banking entity in connection with acquiring or retaining an ownership interest in covered funds (together with any amounts paid by the entity ~~(or employee thereof)~~ in connection with obtaining a restricted profit interest under § 248.10(d)(6)(ii) of this subpart), on a historical cost basis~~.~~:

(ii) Treatment of employee and director restricted profit interests financed by the banking entity. For purposes of paragraph (c)(1)(i) of this section, an investment by a director or employee of a banking entity who acquires a restricted profit interest in their personal capacity in a covered fund sponsored by the banking entity will be attributed to the banking entity if the banking entity, directly or indirectly, extends financing for the purpose of enabling the director or employee to acquire the restricted profit interest in the fund and the financing is used to acquire such ownership interest in the covered fund.

(2) *Calculation of tier 1 capital.* For purposes of paragraph (a)(2)(iii) of this section:

(i) *Entities that are required to hold and report tier 1 capital.* If a banking entity is required to calculate and report tier 1 capital, the banking entity's tier 1 capital shall be equal to the amount of tier 1 capital of the banking entity as of the last day of the most recent calendar quarter, as reported to its primary financial regulatory agency; and

(ii) If a banking entity is not required to calculate and report tier 1 capital, the banking entity's tier 1 capital shall be determined to be equal to:

(A) In the case of a banking entity that is controlled, directly or indirectly, by a depository institution that calculates and reports tier 1 capital, be equal to the amount of tier 1 capital reported by such controlling depository institution in the manner described in paragraph (c)(2)(i) of this section;

(B) In the case of a banking entity that is not controlled, directly or indirectly, by a depository institution that calculates and reports tier 1 capital:

(*1*) *Bank holding company subsidiaries.* If the banking entity is a subsidiary of a bank holding company or company that is treated as a bank holding company, be equal to the amount of tier 1 capital reported by the top-tier affiliate of such covered banking entity that calculates and reports tier 1 capital in the manner described in paragraph (c)(2)(i) of this section; and

(*2*) *Other holding companies and any subsidiary or affiliate thereof.* If the banking entity is not a subsidiary of a bank holding company or a company that is treated as a bank holding company, be equal to the total amount of shareholders' equity of the top-tier affiliate within such organization as of the last day of the most recent calendar quarter that has ended, as determined under applicable accounting standards.

(iii) *Treatment of foreign banking entities*—(A) *Foreign banking entities.* Except as provided in paragraph (c)(2)(iii)(B) of this section, with respect to a banking entity that is not itself, and is not controlled directly or indirectly by, a banking entity that is located or organized under the laws of the United States or of any State, the tier 1 capital of the banking entity shall be the consolidated tier 1 capital of the entity as calculated under applicable home country standards.

(B) *U.S. affiliates of foreign banking entities.* With respect to a banking entity that is located or organized under the laws of the United States or of any State and is controlled by a foreign banking entity identified under paragraph (c)(2)(iii)(A) of this section, the banking entity's tier 1 capital shall be as calculated under paragraphs (c)(2)(i) or (ii) of this section.

(d) *Capital treatment for a permitted investment in a covered fund*. For purposes of calculating compliance with the applicable regulatory capital requirements, a banking entity shall deduct from the banking entity's tier 1 capital (as determined under paragraph (c)(2) of this section) the greater of:

(1) (i) The sum of all amounts paid or contributed by the banking entity in connection with acquiring or retaining an ownership interest (together with any amounts paid by the entity ~~(or employee thereof)~~ in connection with obtaining a restricted profit interest under § 248.10(d)(6)(ii) of subpart C), on a historical cost basis, plus any earnings received; and

(~~2~~ii) The fair market value of the banking entity's ownership interests in the covered fund as determined under paragraph (b)(2)(ii) or (b)(3) of this section (together with any amounts paid by the entity ~~(or employee thereof)~~ in connection with obtaining a restricted profit interest under § 248.10(d)(6)(ii) of subpart C), if the banking entity accounts for the profits (or losses) of the fund investment in its financial statements.

(2) Treatment of employee and director restricted profit interests financed by the banking entity. For purposes of paragraph (d)(1) of this section, an investment by a director or employee of a banking entity who acquires a restricted profit interest in his or her personal capacity in a covered fund sponsored by the banking entity will be attributed to the banking entity if the banking entity, directly or indirectly, extends financing for the purpose of enabling the director or employee to acquire the restricted profit interest in the fund and the financing is used to acquire such ownership interest in the covered fund.

(e) *Extension of time to divest an ownership interest*. (1) Upon application by a banking entity, the Board may extend the period under paragraph (a)(2)(i) of this section for up to 2 additional years if the Board finds that an extension would be consistent with safety and soundness and not detrimental to the public interest. ~~An application for extension must:~~

(2) An application for extension must:

(i) Be submitted to the Board at least 90 days prior to the expiration of the applicable time period;

(ii) Provide the reasons for application, including information that addresses the factors in paragraph (e)(~~2~~3) of this section; and

(iii) Explain the banking entity's plan for reducing the permitted investment in a covered fund through redemption, sale, dilution or other methods as required in paragraph (a)(2) of this section.

(~~2~~3) *Factors governing the Board determinations*. In reviewing any application under paragraph (e)(1) of this section, the Board may consider all the facts and circumstances related to the permitted investment in a covered fund, including:

(i) Whether the investment would result, directly or indirectly, in a material exposure by the banking entity to high-risk assets or high-risk trading strategies;

(ii) The contractual terms governing the banking entity's interest in the covered fund;

(iii) The date on which the covered fund is expected to have attracted sufficient investments from investors unaffiliated with the banking entity to enable the banking entity to comply with the limitations in paragraph (a)(2)(i) of this section;

(iv) The total exposure of the covered banking entity to the investment and the risks that disposing of, or maintaining, the investment in the covered fund may pose to the banking entity and the financial stability of the United States;

(v) The cost to the banking entity of divesting or disposing of the investment within the applicable period;

(vi) Whether the investment or the divestiture or conformance of the investment would involve or result in a material conflict of interest between the banking entity and unaffiliated parties, including clients, customers, or counterparties to which it owes a duty;

(vii) The banking entity's prior efforts to reduce through redemption, sale, dilution, or other methods its ownership interests in the covered fund, including activities related to the marketing of interests in such covered fund;

(viii) Market conditions; and

(ix) Any other factor that the Board believes appropriate.

(3) [*sic*] Authority to impose restrictions on activities or investment during any extension period. The Board may impose such conditions on any extension approved under paragraph (e)(1) of this section as the Board determines are necessary or appropriate to protect the safety and soundness of the banking entity or the financial stability of the United States, address material conflicts of interest or other unsound banking practices, or otherwise further the purposes of section 13 of the BHC Act and this part.

(4) [*sic*] Consultation. In the case of a banking entity that is primarily regulated by another Federal banking agency, the SEC, or the CFTC, the Board will consult with such agency prior to acting on an application by the banking entity for an extension under paragraph (e)(1) of this section.

§ 248.13 Other permitted covered fund activities and investments.

(a) *Permitted risk-mitigating hedging activities.* (1) The prohibition contained in § 248.10(a) does not apply with respect to an ownership interest in a covered fund acquired or retained by a banking entity that is designed to reduce or otherwise significantly mitigate the specific, identifiable risks to the banking entity in connection with:

(i) A compensation arrangement with an employee of the banking entity or an affiliate thereof that directly provides investment advisory, commodity trading advisory or other services to the covered fund; or

(ii) A position taken by the banking entity when acting as intermediary on behalf of a customer that is not itself a banking entity to facilitate the exposure by the customer to the profits and losses of the covered fund.

(2) *Requirements.* The risk-mitigating hedging activities of a banking entity are permitted under this paragraph (a) only if:

(i) The banking entity has established and implements, maintains and enforces an internal compliance program in accordance with subpart D of this part that is reasonably designed to ensure the banking entity's compliance with the requirements of this section, including:

(A) Reasonably designed written policies and procedures; and

(B) Internal controls and ongoing monitoring, management, and authorization procedures, including relevant escalation procedures; and

(ii) The acquisition or retention of the ownership interest:

(A) Is made in accordance with the written policies, procedures, and internal controls required under this section;

(B) At the inception of the hedge, is designed to reduce or otherwise significantly mitigate one or more specific, identifiable risks arising:

(*1*) Out of a transaction conducted solely to accommodate a specific customer request with respect to the covered fund; or

(*2*) In connection with the compensation arrangement with the employee that directly provides investment advisory, commodity trading advisory, or other services to the covered fund;

(C) Does not give rise, at the inception of the hedge, to any significant new or additional risk that is not itself hedged contemporaneously in accordance with this section; and

(D) Is subject to continuing review, monitoring and management by the banking entity.

(iii) With respect to risk-mitigating hedging activity conducted pursuant to paragraph (a)(1)(i), the compensation arrangement relates solely to the covered fund in which the banking entity or any affiliate has acquired an ownership interest pursuant to paragraph (a)(1)(i) and such compensation arrangement provides that any losses incurred by the banking entity on such ownership interest will be offset by corresponding decreases in amounts payable under such compensation arrangement.

(b) *Certain permitted covered fund activities and investments outside of the United States.* (1) The prohibition contained in § 248.10(a) of this subpart does not apply to the acquisition or retention of any ownership interest in, or the sponsorship of, a covered fund by a banking entity only if:

(i) The banking entity is not organized or directly or indirectly controlled by a banking entity that is organized under the laws of the United States or of one or more States;

(ii) The activity or investment by the banking entity is pursuant to paragraph (9) or (13) of section 4(c) of the BHC Act;

(iii) No ownership interest in the covered fund is offered for sale or sold to a resident of the United States; and

(iv) The activity or investment occurs solely outside of the United States.

(2) An activity or investment by the banking entity is pursuant to paragraph (9) or (13) of section 4(c) of the BHC Act for purposes of paragraph (b)(1)(ii) of this section only if:

(i) The activity or investment is conducted in accordance with the requirements of this section; and

(ii) (A) With respect to a banking entity that is a foreign banking organization, the banking entity meets the qualifying foreign banking organization requirements

of section 211.23(a), (c) or (e) of the Board's Regulation K (12 CFR 211.23(a), (c) or (e)), as applicable; or

(B) With respect to a banking entity that is not a foreign banking organization, the banking entity is not organized under the laws of the United States or of one or more States and the banking entity, on a fully-consolidated basis, meets at least two of the following requirements:

(*1*) Total assets of the banking entity held outside of the United States exceed total assets of the banking entity held in the United States;

(*2*) Total revenues derived from the business of the banking entity outside of the United States exceed total revenues derived from the business of the banking entity in the United States; or

(*3*) Total net income derived from the business of the banking entity outside of the United States exceeds total net income derived from the business of the banking entity in the United States.

(3) An ownership interest in a covered fund is not offered for sale or sold to a resident of the United States for purposes of paragraph (b)(1)(iii) of this section only if it is not sold and has not been sold pursuant to an offering that targets residents of the United States in which the banking entity or any affiliate of the banking entity participates. If the banking entity or an affiliate sponsors or serves, directly or indirectly, as the investment manager, investment adviser, commodity pool operator or commodity trading advisor to a covered fund, then the banking entity or affiliate will be deemed for purposes of this paragraph (b)(3) to participate in any offer or sale by the covered fund of ownership interests in the covered fund.

(4) An activity or investment occurs solely outside of the United States for purposes of paragraph (b)(1)(iv) of this section only if:

(i) The banking entity acting as sponsor, or engaging as principal in the acquisition or retention of an ownership interest in the covered fund, is not itself, and is not controlled directly or indirectly by, a banking entity that is located in the United States or organized under the laws of the United States or of any State;

(ii) The banking entity (including relevant personnel) that makes the decision to acquire or retain the ownership interest or act as sponsor to the covered fund is not located in the United States or organized under the laws of the United States or of any State; and

(iii) The investment or sponsorship, including any transaction arising from risk-mitigating hedging related to an ownership interest, is not accounted for as principal directly or indirectly on a consolidated basis by any branch or affiliate that is located in the United States or organized under the laws of the United States or of any State.

(5) For purposes of this section, a U.S. branch, agency, or subsidiary of a foreign bank, or any subsidiary thereof, is located in the United States; however, a foreign bank of which that branch, agency, or subsidiary is a part is not considered to be located in the United States solely by virtue of operation of the U.S. branch, agency, or subsidiary.

(c) *Permitted covered fund interests and activities by a regulated insurance company.* The prohibition contained in § 248.10(a) of this subpart does not apply to the acquisition or retention by an insurance company, or an affiliate thereof, of any ownership interest in, or the sponsorship of, a covered fund only if:

(1) The insurance company or its affiliate acquires and retains the ownership interest solely for the general account of the insurance company or for one or more separate accounts established by the insurance company;

(2) The acquisition and retention of the ownership interest is conducted in compliance with, and subject to, the insurance company investment laws and regulations of the State or jurisdiction in which such insurance company is domiciled; and

(3) The appropriate Federal banking agencies, after consultation with the Financial Stability Oversight Council and the relevant insurance commissioners of the States and foreign jurisdictions, as appropriate, have not jointly determined, after notice and comment, that a particular law or regulation described in paragraph (c)(2) of this section is insufficient to protect the safety and soundness of the banking entity, or the financial stability of the United States.

(d) *Permitted covered fund activities and investments of qualifying foreign excluded funds.*

(1) The prohibition contained in § 248.10(a) does not apply to a qualifying foreign excluded fund.

(2) For purposes of this paragraph (d), a qualifying foreign excluded fund means a banking entity that:

(i) Is organized or established outside the United States, and the ownership interests of which are offered and sold solely outside the United States;

(ii) (A) Would be a covered fund if the entity were organized or established in the United States, or

(B) Is, or holds itself out as being, an entity or arrangement that raises money from investors primarily for the purpose of investing in financial instruments for resale or other disposition or otherwise trading in financial instruments;

(iii) Would not otherwise be a banking entity except by virtue of the acquisition or retention of an ownership interest in, sponsorship of, or relationship with the entity, by another banking entity that meets the following:

(A) The banking entity is not organized, or directly or indirectly controlled by a banking entity that is organized, under the laws of the United States or of any State; and

(B) The banking entity's acquisition of an ownership interest in or sponsorship of the fund by the foreign banking entity meets the requirements for permitted covered fund activities and investments solely outside the United States, as provided in section 248.13(b)

(iv) Is established and operated as part of a bona fide asset management business; and

(v) Is not operated in a manner that enables any other banking entity to evade the requirements of section 13 of the BHC Act or this part.

§ 248.14 Limitations on relationships with a covered fund.

(a) *Relationships with a covered fund*.

(1) Except as provided for in paragraph (a)(2) of this section, no banking entity that serves, directly or indirectly, as the investment manager, investment adviser, commodity trading

advisor, or sponsor to a covered fund, that organizes and offers a covered fund pursuant to § 248.11 of this subpart, or that continues to hold an ownership interest in accordance with § 248.11(b) of this subpart, and no affiliate of such entity, may enter into a transaction with the covered fund, or with any other covered fund that is controlled by such covered fund, that would be a covered transaction as defined in section 23A of the Federal Reserve Act (12 U.S.C. 371c(b)(7)), as if such banking entity and the affiliate thereof were a member bank and the covered fund were an affiliate thereof.

(2) Notwithstanding paragraph (a)(1) of this section, a banking entity may:

(i) Acquire and retain any ownership interest in a covered fund in accordance with the requirements of § 248.11, § 248.12, or § 248.13 of this subpart; ~~and~~

(ii) Enter into any prime brokerage transaction with any covered fund in which a covered fund managed, sponsored, or advised by such banking entity (or an affiliate thereof) has taken an ownership interest, if:

(A) The banking entity is in compliance with each of the limitations set forth in § 248.11 of this subpart with respect to a covered fund organized and offered by such banking entity (or an affiliate thereof);

(B) The chief executive officer (or equivalent officer) of the banking entity certifies in writing annually no later than March 31 to the Board (with a duty to update the certification if the information in the certification materially changes) that the banking entity does not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of the covered fund or of any covered fund in which such covered fund invests; and

(C) The Board has not determined that such transaction is inconsistent with the safe and sound operation and condition of the banking entity; and

(iii) Enter into a transaction with a covered fund that would be an exempt covered transaction under 12 U.S.C. §371c(d) or section 223.42 of the Board's Regulation W (12 CFR 223.42); and

(iv) Extend credit to or purchase assets from a covered fund, provided:

(A) Each extension of credit or purchase of assets is in the ordinary course of business in connection with payment transactions; settlement services; or futures, derivatives, and securities clearing;

(B) Each extension of credit is repaid, sold, or terminated by the end of five business days; and

(C) The banking entity making each extension of credit meets the requirements of section 223.42(l)(1)(i) and (ii) of the Board's Regulation W (12 CFR 223.42(l)(1)(i) and(ii)), as if the extension of credit was an intraday extension of credit, regardless of the duration of the extension of credit.

(3) Any transaction or activity permitted under paragraphs (a)(2)(iii) or (iv) must comply with the limitations in § 248.15 of this section. ~~The Board has not determined that such transaction is inconsistent with the safe and sound operation and condition of the banking entity.~~

(b) *Restrictions on transactions with covered funds.* A banking entity that serves, directly or indirectly, as the investment manager, investment adviser, commodity trading advisor, or sponsor to a covered fund, or that organizes and offers a covered fund pursuant to § 248.11 of this subpart, or

that continues to hold an ownership interest in accordance with § 248.11(b) of this subpart, shall be subject to section 23B of the Federal Reserve Act (12 U.S.C. 371c–1), as if such banking entity were a member bank and such covered fund were an affiliate thereof.

(c) *Restrictions on ~~prime brokerage~~ other permitted transactions*. ~~A prime brokerage~~Any transaction permitted under ~~paragraph~~paragraphs (a)(2)(ii), (a)(2)(iii), or (a)(2)(iv) of this section shall be subject to section 23B of the Federal Reserve Act (12 U.S.C. 371c–1) as if the counterparty were an affiliate of the banking entity.

§ 248.15 Other limitations on permitted covered fund activities.

(a) No transaction, class of transactions, or activity may be deemed permissible under §§ 248.11 through 248.13 of this subpart if the transaction, class of transactions, or activity would:

(1) Involve or result in a material conflict of interest between the banking entity and its clients, customers, or counterparties;

(2) Result, directly or indirectly, in a material exposure by the banking entity to a high-risk asset or a high-risk trading strategy; or

(3) Pose a threat to the safety and soundness of the banking entity or to the financial stability of the United States.

(b) *Definition of material conflict of interest.* (1) For purposes of this section, a material conflict of interest between a banking entity and its clients, customers, or counterparties exists if the banking entity engages in any transaction, class of transactions, or activity that would involve or result in the banking entity's interests being materially adverse to the interests of its client, customer, or counterparty with respect to such transaction, class of transactions, or activity, and the banking entity has not taken at least one of the actions in paragraph (b)(2) of this section.

(2) Prior to effecting the specific transaction or class or type of transactions, or engaging in the specific activity, the banking entity:

(i) *Timely and effective disclosure.* (A) Has made clear, timely, and effective disclosure of the conflict of interest, together with other necessary information, in reasonable detail and in a manner sufficient to permit a reasonable client, customer, or counterparty to meaningfully understand the conflict of interest; and (B) Such disclosure is made in a manner that provides the client, customer, or counterparty the opportunity to negate, or substantially mitigate, any materially adverse effect on the client, customer, or counterparty created by the conflict of interest; or

(ii) *Information barriers.* Has established, maintained, and enforced information barriers that are memorialized in written policies and procedures, such as physical separation of personnel, or functions, or limitations on types of activity, that are reasonably designed, taking into consideration the nature of the banking entity's business, to prevent the conflict of interest from involving or resulting in a materially adverse effect on a client, customer, or counterparty. A banking entity may not rely on such information barriers if, in the case of any specific transaction, class or type of transactions or activity, the banking entity knows or should reasonably know that, notwithstanding the banking entity's establishment of information barriers, the conflict of interest may involve or result in a materially adverse effect on a client, customer, or counterparty.

(c) Definition of high-risk asset and high-risk trading strategy. For purposes of this section:

(1) *High-risk asset* means an asset or group of related assets that would, if held by a banking entity, significantly increase the likelihood that the banking entity would incur a substantial financial loss or would pose a threat to the financial stability of the United States.

(2) *High-risk trading strategy* means a trading strategy that would, if engaged in by a banking entity, significantly increase the likelihood that the banking entity would incur a substantial financial loss or would pose a threat to the financial stability of the United States.

§ 248.16 Ownership of interests in and sponsorship of issuers of certain collateralized debt obligations backed by trust-preferred securities.

(a) The prohibition contained in § 248.10(a)(1) does not apply to the ownership by a banking entity of an interest in, or sponsorship of, any issuer if:

(1) The issuer was established, and the interest was issued, before May 19, 2010;

(2) The banking entity reasonably believes that the offering proceeds received by the issuer were invested primarily in Qualifying TruPS Collateral; and

(3) The banking entity acquired such interest on or before December 10, 2013 (or acquired such interest in connection with a merger with or acquisition of a banking entity that acquired the interest on or before December 10, 2013).

(b) For purposes of this § 248.16, *Qualifying TruPS Collateral* shall mean any trust preferred security or subordinated debt instrument issued prior to May 19, 2010 by a depository institution holding company that, as of the end of any reporting period within 12 months immediately preceding the issuance of such trust preferred security or subordinated debt instrument, had total consolidated assets of less than $15,000,000,000 or issued prior to May 19, 2010 by a mutual holding company.

(c) Notwithstanding paragraph (a)(3) of this section, a banking entity may act as a market maker with respect to the interests of an issuer described in paragraph (a) of this section in accordance with the applicable provisions of §§ 248.4 and 248.11.

(d) Without limiting the applicability of paragraph (a) of this section, the Board, the FDIC and the OCC will make public a non-exclusive list of issuers that meet the requirements of paragraph (a). A banking entity may rely on the list published by the Board, the FDIC and the OCC.