August 22, 2019

Volcker Rule

Office of the Comptroller of the Currency and Federal Deposit Insurance Corporation Finalize Amendments to Implementing Regulations, with Approval by Other Agencies Expected to Follow; Additional Covered Funds-Related Amendments to be Addressed in Future Rulemaking

EXECUTIVE SUMMARY

On August 20, 2019, the Office of the Comptroller of the Currency (the "OCC") and the Federal Deposit Insurance Corporation (the "FDIC") approved a final rule (the "Final Rule") amending the regulations implementing Section 13 of the Bank Holding Company Act of 1956 (the "BHC Act"),[1] known as the "Volcker Rule." The Board of Governors of the Federal Reserve System (the "Federal Reserve"), the Securities and Exchange Commission (the "SEC") and the Commodity Futures Trading Commission (the "CFTC" and, collectively with the OCC, FDIC, Federal Reserve and SEC, the "Agencies") are expected to approve in the near term substantially similar amendments to their Volcker Rule regulations. The Final Rule follows a notice of proposed rulemaking issued by the Agencies in 2018 that proposed a series of amendments (collectively, the "Proposed Rule") to the existing regulations implementing the Volcker Rule that were adopted on December 10, 2013 (the "2013 Rule").[2]

The Final Rule's impact on particular banking organizations will differ significantly depending on the size, scope and nature of their businesses and operations, which is consistent with the federal banking agencies' broad-gauged focus on regulatory "tailoring." Institutions with $20 billion or more in gross trading assets and liabilities will continue to be subject to the six-pillar compliance program requirement that is currently in effect. By contrast, an institution with less than $20 billion in gross trading assets and liabilities will be subject to a substantially simpler compliance program requirement, and an institution with less than $1 billion in gross trading assets and liabilities will benefit from a "presumption of compliance"

with all aspects of the Final Rule (and is excluded from the Volcker Rule and Final Rule entirely if it has total consolidated assets not exceeding $10 billion and trading assets and liabilities equal to 5 percent or less of its total consolidated assets).[3]

Consistent with the federal banking agencies' overall approach to bank regulation, the Final Rule does not constitute a "roll-back" of the enhanced regulatory regime that evolved in the aftermath of the 2008 financial crisis and in response to the Dodd-Frank Act.[4] Rather, it represents an effort, which we believe to be largely successful, to provide clarification, simplification and tailoring, and thereby reduce unnecessary compliance burden, without compromising the fundamental strengths and objectives of the post-crisis regulatory framework. It reflects the Agencies' experience in administering, and banking entities' experience in seeking to comply with, a highly complex and lengthy rule.

The Final Rule also reflects a thoughtful consideration of the comments received on the Proposed Rule, in particular with respect to the proprietary trading and compliance program provisions that are the focus of the amendments. The Final Rule adopts, without change, the limited amendments to the covered funds provisions for which specific rule text was included in the Proposed Rule. The supplementary information accompanying the Final Rule (the "Preamble") states that the Agencies intend to propose additional changes relating to the restrictions on covered fund investments and activities.

The Final Rule will become effective on January 1, 2020. On that date, banking entities may begin voluntarily to comply, in whole or in part, with the Final Rule, although they will not be required to do so until the compliance date of January 1, 2021. Voluntary compliance with the Final Rule before the required compliance date will be advantageous for many banking entities, as the amendments generally do not create new obligations or add conditions to which banking entities are not already subject (other than in the case of certain modifications to the quantitative trading metrics reporting regime).

The remainder of this Memorandum discusses the amendments adopted under the Final Rule and related discussion in the Preamble. **Figure 1** below provides a high-level overview of key amendments contained in the Final Rule, including notable departures from the Proposed Rule. **Appendix A** and **Appendix B** to this Memorandum provide comparisons of the text of the Final Rule against the text of the currently effective regulations and the Proposed Rule, respectively.

Figure 1: Overview of Selected Final Rule Amendments and Differences from 2013 Rule and Proposed Rule

	Differences from 2013 Rule	Differences from Proposed Rule
"Trading account" definition	• For banking entities that are subject to the market risk capital rule[5] (and their consolidated affiliates), the "trading account" definition will consist of the Market Risk Capital Prong and Dealer Prong. Both of these prongs remain in substantially similar form as in the 2013 Rule. The Market Risk Capital Prong continues to include a test based on short-term intent that is functionally similar to the Short-Term Intent Prong. • For all other banking entities, the "trading account" definition will consist of the Dealer Prong and either the Short-Term Intent Prong or, at the banking entity's election, the Market Risk Capital Prong (provided that such election applies to the banking entity and all its wholly owned subsidiaries). The 60-day rebuttable presumption under the Short-Term Intent Prong is reversed—*i.e.*, any position held for 60 days or longer is presumed not to be captured by this prong.	• Accounting Prong was not adopted. • Short-Term Intent Prong is restored, but applies only to banking entities that are not subject to the market risk capital rule (unless the banking entity elects to be subject instead to the Market Risk Capital Prong, as described at left).
"Trading desk" definition	• Trading desks need not be the "smallest discrete" units of organization, but must be defined and structured based on criteria used to establish trading desks for other operational, management, and compliance purposes (either meeting enumerated criteria or established for purposes of the market risk capital rule).	• Proposed Rule did not expressly propose a revised definition of "trading desk," but requested comment on a multi-factor definition similar to the one adopted.
Liquidity management exclusion	• Financial instruments that a banking entity may purchase and sell under this exclusion will be expanded to include foreign exchange forwards, foreign exchange swaps and physically settled cross-currency swaps (in addition to transactions involving securities).	• Expanded to include non-deliverable cross-currency swaps.
Other proprietary trading exclusions	• Definition of "proprietary trading" will exclude the following: ○ Error trades and subsequent correcting transactions; ○ A customer-driven swap (or security-based swap) and a matched swap (or security-based swap), provided that (i) the swaps are entered into contemporaneously; (ii) the banking entity retains no more than minimal price risk; and (iii) the banking entity is not a registered dealer, swap dealer or security-based swap dealer; ○ Purchase or sale of a financial instrument that does not meet the definition of "trading asset" or "trading liability" under the banking entity's applicable reporting form; and ○ Purchase or sale of a financial instrument used to hedge mortgage servicing rights or mortgage servicing assets in accordance with a documented hedging strategy.	• Proposed Rule did not expressly propose these exclusions (other than the error trade exclusion), but requested comment on whether such exclusions could be appropriate.
Underwriting and market making exemptions	• Banking entities that establish and enforce certain internal risk limits for each trading desk will be presumed to satisfy the so-called reasonably expected near term demand ("RENTD") requirement, subject to rebuttal by the relevant Agency. • Compliance program requirement is limited to banking entities with	• Removed requirement that limit breaches and increases be promptly reported to the relevant Agency.

	Differences from 2013 Rule	Differences from Proposed Rule
	significant trading assets and liabilities.	
Risk-mitigating hedging exemption	• Banking entities will no longer be required to conduct a correlation analysis that demonstrates that the hedging activity demonstrably reduces or mitigates the specific risks being hedged. For banking entities that do not have significant trading assets and liabilities, the conditions of this exemption are further simplified.	• Adopted substantially as proposed.
"Trading outside the United States" exemption	• Eliminates the requirement that no U.S. personnel of the banking entity are involved in the arrangement, negotiation or execution of trades. However, the decision to purchase or sell as principal must still be made outside the U.S. by non-U.S. personnel. • Eliminates the requirements that (i) no financing for the purchase or sale is provided by a U.S. branch or affiliate of the banking entity; and (ii) the purchase or sale is not conducted "with or through" a U.S. entity.	• Adopted as proposed.
Market making and underwriting with respect to covered fund interests	• Aggregate investment limitation and regulatory capital deduction do not include market making or underwriting positions in third-party covered funds (*i.e.*, funds that are not sponsored or advised by the banking entity or held in reliance on the organizing and offering exemption). Similar treatment applies to covered funds the obligations or performance of which a banking entity guarantees, assumes or otherwise insures.	• Adopted as proposed.
Covered fund activities "solely outside the United States"	• Formally adopts prior FAQ guidance that non-U.S. banking entities may rely on the "SOTUS" exemption to invest in covered funds that were offered or sold in the United States so long as the banking entity does not itself participate in the marketing activity. • Eliminates the requirement that no financing for the non-U.S. banking entity's investment in, or sponsorship of, the covered fund is provided by a U.S. branch or affiliate of the banking entity.	• Adopted as proposed.
Prime brokerage exemption	• Formally adopts prior FAQ guidance indicating that the required annual CEO certification is due no later than March 31.	• Adopted as proposed.
Compliance program; tailoring based on trading assets and liabilities	• Eliminates Appendix B, including its enhanced minimum standards and standalone compliance program requirement. • Three-tier categorization depending on the banking entity's gross trading assets and liabilities, measured over the prior consecutive four quarters as of the last day of each quarter (as discussed in Section 1 below): ○ "Significant trading assets and liabilities" (*i.e.*, $20 billion or more) – Subject to six-pillar compliance program, metrics reporting, covered fund documentation and CEO attestation requirements. ○ "Moderate trading assets and liabilities" (*i.e.*, less than $20 billion but equal to or greater than $1 billion) – Permitted to maintain a simplified compliance program. ○ "Limited trading assets and liabilities" (*i.e.*, less than $1 billion)	Largely adopted as proposed, except that: • threshold for "significant" trading assets and liabilities was raised to $20 billion from $10 billion;[6] • CEO attestation requirement applies only to firms with significant trading assets and liabilities; • trading assets and liabilities of foreign banking organizations are, across

	Differences from 2013 Rule	Differences from Proposed Rule
	– Presumed to comply with the Final Rule and will have no obligation to demonstrate compliance on an ongoing basis. In addition, an institution that has total consolidated assets not exceeding $10 billion and trading assets and liabilities equal to 5 percent or less of its total consolidated assets is exempted from the Volcker Rule and Final Rule entirely. • Trading assets and liabilities of a foreign banking organization for purposes of this categorization are calculated based on the firm's U.S. operations.	all tiers, calculated based on combined U.S. operations; • excludes from the trading assets and liabilities calculation any obligations of an agency of the United States or of a government-sponsored enterprise (in addition to U.S. government obligations) in which banking entities are permitted to trade.
Quantitative Trading Metrics	• The following metrics are no longer required to be reported: (i) Customer-Facing Trade Ratio (replaced with the new Transaction Volumes metric), (ii) Stressed Value-at-Risk, (iii) Risk Factor Sensitivities (including the related daily reporting requirement for each trading desk), (iv) Inventory Aging and (v) Inventory Turnover (replaced with the new Positions metric). • Metrics must be filed on a quarterly basis within 30 days of each quarter-end (rather than within 10 days of each calendar month-end). • Additional quantitative and qualitative information must be reported, including (i) Positions metric (*i.e.*, value of securities and derivatives positions managed by the trading desk), (ii) Transaction Volumes metric (*i.e.*, value of securities and derivatives transactions conducted by the trading desk with customers, non-customers and other trading desks booking the transactions into the same banking entity or an affiliated banking entity), (iii) trading desk-level descriptive information, and (iv) Internal Limits Information Schedule and Risk Factor Attribution Information Schedule. • The Positions and Transaction Volumes metrics are applicable only to those trading desks relying on the underwriting exemption or market making exemption.	• Key changes largely adopted as proposed. Agencies did not adopt the narrative statement requirement (leaving in place an option for a voluntary statement, as provided in the 2013 Rule's reporting instructions).

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I. TAILORING OF THE FINAL RULE'S REQUIREMENTS

The Final Rule divides banking entities into three categories, each of which will be subject to a distinct set of compliance program requirements and other substantive requirements. This categorization represents a significant change from the 2013 Rule. Under the 2013 Rule, a banking entity's total consolidated assets and its trading assets and liabilities (together with those of its affiliates and subsidiaries) determined the compliance program requirements that are applicable to the banking entity.[7] Under the Final Rule, a banking entity's categorization will be based on the amount of the banking entity's trading assets and liabilities as calculated in the following manner (referred to as "TALs" in this Section I):

- In the case of a banking entity that is not and is not controlled by a foreign banking organization ("FBO"), the banking entity's TALs equal the average gross sum of the banking entity's and its affiliates' and subsidiaries' trading assets and liabilities over the previous consecutive four quarters, as measured as of the last day of each of the four previous calendar quarters, on a worldwide consolidated basis, but excluding trading assets and liabilities involving obligations of, or guaranteed by, the United States, any agency of the United States or any government-sponsored enterprise permitted under Section _.6(a)(1)–(2) of the Final Rule.

- In the case of a banking entity that is an FBO or is controlled by an FBO, the calculation of TALs is based on the combined U.S. operations of the top-tier FBO (including all subsidiaries, affiliates, branches and agencies of the FBO operating, located or organized in the United States) and also excludes trading assets and liabilities involving obligations of, or guaranteed by, the United States, any agency of the United States or any government-sponsored enterprise permitted under Section _.6(a)(1)–(2) of the Final Rule.[8] The Agencies departed from Proposed Rule in limiting this calculation to the trading assets and liabilities of combined U.S. operations, which they believe is appropriate because the "trading activities of foreign banking entities that occur outside of the United States and are booked into such foreign banking entities (or into their foreign affiliates), pose substantially less risk to the U.S. financial system than trading activities booked into a U.S. banking entity."[9]

In addition to the relief the Final Rule provides for banking entities with "limited trading assets and liabilities"—*i.e.*, banking entities with TALs of less than $1 billion, calculated on a worldwide consolidated basis—the Agencies recently finalized amendments to implement Section 203 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (the "EGRRCPA"), which excludes from the Volcker Rule certain institutions that (i) have less than $10 billion in total consolidated assets and also (ii) have total trading assets and trading liabilities representing less than 5% of total consolidated assets.[10]

Figure 2 below summarizes the categorization of banking entities under the Final Rule based on whether they have "significant trading assets and liabilities," "moderate trading assets and liabilities" or "limited trading assets and liabilities" (in each case, as defined in the Final Rule), or are excluded entirely from the definition of "banking entity." The Final Rule increases to $20 billion (from $10 billion in the Proposed Rule) the TALs threshold that triggers treatment as a banking entity with "significant trading assets and liabilities" and includes certain changes to the calculation methodology described above, but otherwise sets forth a categorization that is substantially similar to the Proposed Rule.

The Final Rule includes a reservation of authority allowing an Agency, under certain circumstances, to require a banking entity with "limited" or "moderate" trading assets and liabilities to comply with the more extensive requirements associated with a higher tier of trading assets and liabilities.[11] Unlike the Proposed Rule, however, the Final Rule prescribes a notice and response procedure that an Agency must follow in exercising such authority.[12] Specifically, an Agency must provide the subject banking entity with a written notice explaining the Agency's determination of the need for more extensive compliance requirements and allow the banking entity to respond to the notice within 30 days (or such other time period as may be specified by the Agency) of receipt.[13]

Figure 2: Categorization of Banking Entities under the Final Rule

Categorization of Banking Entity	Criteria for This Categorization	Compliance Program Requirements	Metrics Reporting	CEO Attestation	Additional Permitted Activity Requirements
Significant trading assets and liabilities	TALs equal or exceed $20 billion. Calculation of TALs is based on (i) in the case of U.S. banking entities, all affiliates and subsidiaries on a worldwide basis and (ii) in the case of FBOs and their subsidiaries, combined U.S. operations only.	Six pillars required under the 2013 Rule (*i.e.*, written policies and procedures, internal controls, management framework, independent testing, training and records). Subject to the same additional covered fund documentation requirements as under the 2013 Rule.[14]	Yes. Metrics must be reported on a quarterly basis within 30 days after each quarter-end.	Yes.	Subject to specific compliance requirements in order to rely on exemptions for underwriting, market making and risk-mitigating hedging.
Moderate trading assets and liabilities	TALs are less than $10 billion, but greater than or equal to the $1 billon threshold for banking entities with "limited" TALs (see below). TALs are calculated in the manner described immediately above.	Simplified compliance program requirement, which allows the banking entity to comply with the applicable requirements by "incorporat[ing] their simplified compliance program into existing compliance policies and procedures and tailor[ing] their compliance programs to the size and nature of their activities."[15] Subject to the Agencies' reservation of authority to require the banking entity to apply any requirement that is applicable to banking entities having "significant" TALs.	No, subject to the Agencies' reservation of authority (described at left).		--

Categorization of Banking Entity	Criteria for This Categorization	Compliance Program Requirements	Metrics Reporting	CEO Attestation	Additional Permitted Activity Requirements
Limited trading assets and liabilities	TALs are less than $1 billon (as calculated in the manner described above), and the banking entity is not otherwise excluded by the EGRRCPA (see below).	No compliance program requirement, subject to the Agencies' reservation of authority (described above). Presumed to be in compliance with substantive provisions (subject to rebuttal by an Agency pursuant to notice and response procedures).[16]	No, subject to the Agencies' reservation of authority (described above).		--
Not engaged in covered activities	Does not engage in proprietary trading or covered fund activities, other than permitted trading in U.S. government obligations, and the banking entity is not otherwise excluded by the EGRRCPA (see below).	None, unless and until the banking entity becomes engaged in covered proprietary trading or covered fund activities.	No, subject to the Agencies' reservation of authority (described above).		--
Excluded by EGRRCPA	Institutions that have (i) total consolidated assets equal to $10 billion or less *and* (ii) total trading assets and liabilities equal to 5% or less of total consolidated assets are excluded from the definition of "insured depository institution," and therefore generally are excluded from the scope of "banking entities" that are subject to the Volcker Rule and Final Rule.[17]				

II. PROPRIETARY TRADING

A. DEFINITION OF "TRADING ACCOUNT"

The Volcker Rule defines proprietary trading to mean engaging, as principal, in any purchase or sale of one or more financial instruments "for the 'trading account' of the banking entity."[18] Accordingly, the definition of "trading account" is the principal determinant of the scope of the prohibition on proprietary trading. The Final Rule's amendments to the "trading account" definition, taken together with the other changes to the exemptions and exclusions from the proprietary trading prohibition described in the remainder of this Section II, may simplify for banking entities the challenge of determining whether a purchase or sale is prohibited proprietary trading and help to reduce the associated compliance burden.

In a notable departure from the Proposed Rule, the Final Rule maintains the Short-Term Intent Prong and does not adopt the so-called "accounting prong" that the Agencies had proposed as a replacement for the Short-Term Intent Prong. The accounting prong would have included any account used to purchase or sell financial instruments that the banking entity records at fair value on a recurring basis under applicable accounting standards, including, among other financial instruments, derivatives, trading securities and available-for-sale securities.[19] As the Agencies note in the Preamble, the accounting prong was criticized in a number of comment letters, including by commenters who pointed out that it would have

inappropriately brought within the proprietary trading prohibition many financial instruments and activities that the Volcker Rule was not intended to capture, such as long-term investments, seeding activity that would otherwise be permitted under the covered funds provisions, and other types of financial instruments held without short-term trading intent.[20]

Under the Final Rule, a banking entity's "trading account" will consist of the Dealer Prong and either (but not both) the Market Risk Capital Prong or the Short-Term Intent Prong. The remainder of this Section II.A summarizes the tests that comprise the "trading account" definition under the Final Rule.

II.A.1. SHORT-TERM INTENT PRONG

Under the 2013 Rule as well as the Final Rule, the "Short-Term Intent Prong" generally includes a purchase or sale of a financial instrument principally for the purpose of (i) short-term resale; (ii) benefiting from actual or expected short-term price movements; (iii) realizing short-term arbitrage profits; or (iv) hedging one or more positions resulting from the purchases or sales of financial instruments described in clauses (i)–(iii).[21]

The Final Rule modifies in two significant respects the Short-Term Intent Prong as established under the 2013 Rule. First, the Final Rule's Short-Term Intent Prong does not apply to any banking entity that calculates risk-based capital ratios under the market risk capital rule (or any affiliate with which the banking entity is consolidated for regulatory reporting purposes). Those banking entities are subject to the Market Risk Capital Prong, as discussed below, which also includes a test based on short-term intent that is functionally similar to the Short-Term Intent Prong and, according to the Agencies, captures a "scope of activities . . . substantially similar to the scope of activities captured by" the Short-Term Intent Prong.[22] The Final Rule permits a banking entity that is not subject to the Market Risk Capital Prong to elect to apply the Market Risk Capital Prong in place of the Short-Term Intent Prong, as described further below.[23]

Second, the Final Rule eliminates the rebuttable presumption that any purchase or sale of a financial instrument that is held for fewer than 60 days (or an instrument of which the banking entity substantially transfers the risk within 60 days) meets the Short-Term Intent Prong and therefore is within the banking entity's "trading account."[24] Instead, the Final Rule establishes a "reverse presumption" that positions held for 60 days or more do not meet the Short-Term Intent Prong, absent rebuttal by the relevant Agency.[25]

II.A.2. MARKET RISK CAPITAL PRONG

Consistent with the 2013 Rule and the Proposed Rule, the Final Rule's definition of "trading account" under the "Market Risk Capital Prong" includes any purchase or sale of financial instruments that is both (i) a market risk capital rule covered position and (ii) a trading position (or a hedge of another market risk capital rule covered position).[26]

Under the Final Rule, a banking entity's "trading account" includes the Market Risk Capital Prong if the banking entity, or any affiliate with which the banking entity is consolidated for regulatory reporting purposes, calculates risk-based capital ratios under the market risk capital rule.[27] All other banking entities will be subject to the Short-Term Intent Prong, but may elect instead to be subject to the Market Risk Capital Prong. Any such election must also apply to all wholly owned subsidiaries of the electing banking entity.[28]

The Final Rule includes a one-year transition period for banking entities that are subject to the Short-Term Intent Prong but subsequently become subject to the Market Risk Capital Prong (for example, by virtue of becoming affiliated with another banking entity that calculates risk-based capital ratios under the market risk capital rule). During the transition period, a banking entity may continue to apply the Short-Term Intent Prong instead of the Market Risk Capital Prong.[29]

In addition, the Final Rule amends the definition of "market risk capital rule covered position and trading position" to clarify that this definition includes any position that meets the criteria to be a covered position and a trading position, without regard to whether the financial instrument is reported as a covered position or trading position on any applicable regulatory reporting forms.[30] The Final Rule does not adopt the proposal to include within the Market Risk Capital Prong any account used by the banking entity to purchase or sell one or more financial instruments that are subject to risk-based capital requirements under a market risk framework established by the home-country supervisor.[31]

II.A.3. DEALER PRONG

The Final Rule retains the Dealer Prong as established under the 2013 Rule without substantive change, both in terms of the elements comprising this test and the banking entities to which it applies. For all banking entities, the Dealer Prong remains a part of the definition of "trading account." The "Dealer Prong" includes any account that is used by a banking entity to purchase or sell one or more financial instruments, if the banking entity (A) is licensed or registered, or is required to be licensed or registered, to engage in the business of a dealer, swap dealer or security-based swap dealer, to the extent the instrument is purchased or sold in connection with the activities that require the banking entity to be licensed or registered as such; or (B) is engaged in the business of a dealer, swap dealer or security-based swap dealer outside of the United States, to the extent the instrument is purchased or sold in connection with the activities of such business.[32]

In response to commenters, the Agencies reaffirmed that the Dealer Prong does not necessarily apply to all transactions conducted by a banking entity that is licensed or registered as a dealer—rather, the Dealer Prong captures "only the types of activities that require [the banking entity] to be so licensed or registered."[33] The Agencies acknowledged commenters' concerns that the Dealer Prong under the 2013 Rule "may require dealers to conduct a position-by-position analysis of their trading activities to determine

whether a position is captured by the [D]ealer [P]rong," but stated that they believe the Final Rule's amendments—and in particular, the new exclusion for financial instruments that are not trading assets or liabilities—"should help alleviate those concerns by narrowing the range of transactions covered by the [Final Rule]".[34]

B. DEFINITION OF "TRADING DESK"

The Final Rule adopts a modified definition of "trading desk" that is intended to align the criteria used to designate trading desks for Volcker Rule purposes with the criteria used to establish trading desks for other operational, management and compliance purposes.[35] It will continue to be the case under the Final Rule that many of the substantive and compliance-related requirements for permitted proprietary trading are determined in relation to a banking entity's trading desks.

However, unlike the 2013 Rule, the Final Rule does not require that a trading desk be the "smallest discrete unit of organization" of a banking entity.[36] The Final Rule provides two approaches for designating a "trading desk", the second of which applies with respect to a banking entity that calculates risk-based capital ratios under the market risk capital rule (or a consolidated affiliate thereof for regulatory reporting purposes).

Multi-factor approach to "trading desk" designation. Under the first approach, a "trading desk" may be any unit of organization of a banking entity that purchases or sells financial instruments for the trading account of the banking entity or an affiliate thereof that meets each of the following criteria:

(1) The trading desk "is structured by the banking entity to implement a well-defined business strategy." The Agencies indicate that, in general, a "well-defined business strategy" for this purpose typically includes a written description of a desk's objectives, including the economics behind its trading and hedging strategies as well as the instruments and activities the desk will use to accomplish its objectives, and may also include an annual budget and staffing plan and management reports.[37]

(2) The trading desk is organized to ensure appropriate setting, monitoring, and management review of the desk's trading and hedging limits, current and potential future loss exposures, and strategies.

(3) The trading desk is characterized by a clearly defined unit that (i) engages in coordinated trading activity with a unified approach to its key elements; (ii) operates subject to a common and calibrated set of risk metrics, risk levels and joint trading limits; (iii) submits compliance reports and other information as a unit for monitoring by management; and (iv) books its trades together.

"Trading desk" designation for banking entities subject to the market risk capital rule. Under the second approach, which will apply to a banking entity that calculates risk-based capital ratios under the market risk capital rule, or a consolidated affiliate of a banking entity that calculates risk-based ratios under the market risk capital rule, "trading desk" means a unit of organization that purchases or sells financial instruments for the trading account of the banking entity or an affiliate thereof that is established by the banking entity or its affiliate for purposes of capital requirements under the market risk capital rule. The Agencies clarify that, "for a banking entity that is subject to the market risk capital prong, the trading desk established for purposes of the market risk capital rule must be the same unit of organization that is established as a trading desk under the [Final Rule]."[38]

The Agencies state that this second approach is expected to simplify the supervisory activities of the Agencies that also oversee compliance with the market risk capital rule because the same unit of organization can be assessed for purposes of both the market risk capital rule and the Volcker Rule.[39] The current market risk capital rule does not include a definition of "trading desk." The federal banking agencies expect that their revised market risk capital rule will include a definition of "trading desk" that is consistent with the trading desk concept described in the Basel Committee's revised market risk capital standards and the multi-factor "trading desk" definition in the Final Rule.[40]

C. PERMITTED UNDERWRITING ACTIVITIES

The Final Rule modifies certain of the conditions to the exemption for underwriting activities (referred to herein as the "underwriting exemption"), reflecting the Agencies' effort to "tailor, streamline, and clarify the requirements that a banking entity must satisfy to avail itself of [the exemption]"[41] and to respond to concerns that the "significant and costly compliance requirements in the [2013 Rule's] existing exemptions may unnecessarily constrain underwriting and market making without a corresponding reduction in the type of trading activities that the [Volcker Rule] was designed to prohibit."[42] The Final Rule's changes to the underwriting exemption, which are summarized below, are substantially consistent with those contained in the Proposed Rule, with certain targeted modifications to respond to commenters' concerns.

Presumption of compliance with reasonably expected near-term demand ("RENTD") requirement. Under the Final Rule, a banking entity's purchase or sale of a financial instrument is presumed to meet the underwriting RENTD requirement if the banking entity has established, implements, maintains and enforces limits that are designed not to exceed RENTD, based on the nature and amount of the trading desk's underwriting activities, on: (i) the amount, types and risk of its underwriting position; (ii) the level of exposures to relevant risk factors arising from its underwriting position; and (iii) the period of time a security may be held.[43]

Consistent with the Proposed Rule, the limits used to satisfy the presumption of compliance under the Final Rule will be subject to supervisory review and oversight by the applicable Agency on an ongoing basis.[44] The Agencies state that this approach will "allow[] supervisors and examiners to look to the articulation and use of limits to distinguish between permissible and impermissible proprietary trading."[45] The Final Rule provides that the presumption of compliance may be rebutted by the applicable Agency based on its determination, "taking into account the liquidity, maturity, and depth of the market for the relevant types of financial instruments and based on all relevant facts and circumstances, that a trading desk is engaging in activity that is not designed not to exceed RENTD."[46] Any such rebuttal of the presumption must be made in accordance with the notice and response procedures in subpart D of the Final Rule.[47]

The Final Rule does not adopt the Proposed Rule's requirement that a banking entity promptly report to the appropriate Agency when a trading desk exceeds or increases its internal limits it sets to avail itself of the RENTD presumption. Instead, the Final Rule requires that banking entities maintain and make available to the applicable Agency, upon request, records regarding limit breaches and temporary or permanent limit increases. When a limit is breached or increased, the presumption of compliance with RENTD will continue to be available so long as the banking entity: (i) takes action as promptly as possible after a breach to bring the trading desk into compliance; and (ii) follows established written authorization procedures, including escalation procedures that require review and approval of any trade that exceeds a trading desk's limit(s), demonstrable analysis of the basis for any temporary or permanent increase to a trading desk's limit(s), and independent review of such demonstrable analysis and approval.[48]

Compliance program requirement for banking entities with significant trading assets and liabilities. Substantially consistent with the Proposed Rule, the Final Rule modifies the compliance program requirement associated with the exemption for permitted underwriting activities (which, under the currently effective regulations, applies to all banking entities relying on the exemption) by making that requirement applicable only to banking entities with "significant trading assets and liabilities."[49] The Agencies clarify that the removal of these compliance program requirements for banking entities that do not have significant trading assets and liabilities would not relieve those banking entities of the obligation to comply with the other requirements of the exemption for underwriting activities under the Final Rule, including RENTD requirements.[50]

D. PERMITTED MARKET MAKING-RELATED ACTIVITIES

Consistent with the Proposed Rule, the Final Rule amends the exemption for market making-related activities (referred to herein as the "market making exemption") in a manner that parallels the amendments to the underwriting exemption discussed above. Specifically, the Final Rule adopts the Proposed Rule's presumption that a banking entity's purchase or sale of a financial instrument meets the

RENTD requirement of the market making exemption if the banking entity has established, implements, maintains and enforces risk and position limits that are designed not to exceed RENTD, based on the nature and amount of the trading desk's market making-related activities, that address: (i) the amount, types and risks of the trading desk's market-maker positions; (ii) the amount, types and risks of the products, instruments and exposures the trading desk may use for risk management purposes; (iii) the level of exposures to relevant risk factors arising from its financial exposure; and (iv) the period of time a financial instrument may be held.[51]

In the Preamble, the Agencies address two additional topics that are not directly reflected in the Final Rule text:

- ***Derivatives.*** The Agencies acknowledge that, for some derivatives, the RENTD-related factors enumerated in clauses (i) through (iv) above "may not be effective for designing market making-related activities not to exceed RENTD." It may be appropriate, therefore, for banking entities to establish limits with respect to their market making in derivatives "based on specific conditions that would need to be satisfied in order to utilize the presumption of compliance, rather than a fixed number of market-maker positions."[52] For example, for a desk that engages in market making-related activities only with respect to derivatives (or derivatives and non-financial instruments), the requirement to establish, implement, maintain and enforce limits designed not to exceed RENTD could be satisfied "to the extent the banking entity establishes limits on the market making desk's level of exposures to relevant risk factors arising from its financial exposure and such limits are designed not to exceed RENTD (including derivatives positions related to a request from a client, customer, or counterparty), based on the nature and amount of the trading desk's market making-related activities."[53]

- ***Market making hedging for affiliated trading desks.*** The Agencies expressly declined to permit banking entities to treat affiliated trading desks as "clients, customers, or counterparties" for purposes of establishing a trading desk's RENTD under the market making exemption, notwithstanding recommendations in favor of this change from a number of commenters.[54] Permitting banking entities to treat affiliated trading desks as "clients, customers, or counterparties" could, in the Agencies' view, impede monitoring of market making-related activity and detection of impermissible proprietary trading, because a banking entity could aggregate in a single trading desk the RENTD of trading desks that engage in multiple different trading strategies.[55]

  The Agencies clarify that transactions between affiliated trading desks may be permitted under the market making exemption in certain circumstances that do not require the expansion of a trading desk's market making limits based on internal transactions. Each trading desk, however,

must be able to "independently tie its activities to the RENTD of [the desk's] *external* customers."[56]

By way of example, the Agencies state that if a banking entity's trading desk makes a market in interest rate swaps and then transfers the foreign exchange ("FX") risk of the interest rate swaps to the banking entity's affiliated FX swaps desk, the interest rate swaps desk and the FX swaps desk would not be permitted to treat one another as "clients, customers, or counterparties" for purposes of establishing their respective RENTD. The FX swaps desk may be able to rely on the market making exemption for its transactions with the interest rate swaps desk in either of two scenarios:

- First, if the FX swaps desk is itself a market maker in FX swaps, then it could rely on the market making exemption to transact with the interest rate swaps desk so long as the transactions are consistent with the requirements of the market making exemption, including the FX swaps desk's RENTD.
- Second, for a banking entity that has significant trading assets and liabilities, if the FX swaps desk does not independently satisfy the requirements of the market making exemption with respect to the transaction, it would be permitted to rely on the market making exemption available to the interest rate swaps desk if (i) the resulting risk mitigating position is attributed to the interest rate swaps desk's financial exposure (and not the FX swaps desk's financial exposure) and is included in the interest rate swaps desk's daily profit and loss calculation and (ii) the FX swaps desk acts in accordance with the interest rate swaps desk's risk management policies and procedures established in accordance with the market making exemption.[57]

As with the underwriting exemption, the presumption of compliance with the market making exemption's RENTD requirement is subject to (i) a requirement to maintain and make available reports on limit breaches or increases of the limits to the relevant Agency,[58] (ii) review and oversight by the relevant Agency,[59] (iii) the possibility of a rebuttal of the presumption by the relevant Agency,[60] and (iv) a compliance program requirement for banking entities with significant trading assets and liabilities.[61]

E. PERMITTED RISK-MITIGATING HEDGING ACTIVITIES

The Final Rule follows the approach taken by the Proposed Rule and maintains most of the requirements of the 2013 Rule for the risk-mitigating hedging exemption for banking entities with significant trading assets and liabilities, with the following modifications:

- ***Correlation analysis.*** The Final Rule eliminates the correlation analysis requirement of the exemption, as proposed, although the banking entity must still conduct "analysis and independent

testing designed to ensure that the positions, techniques and strategies that may be used for hedging may reasonably be expected to reduce or otherwise significantly mitigate the specific, identifiable risk(s) being hedged."[62] The Agencies state that the requisite analysis need not be—but could be—a correlation analysis, and anticipate that the flexibility to apply the type of analysis that is appropriate to assess the particular hedging activity at issue will facilitate the appropriate use of risk-mitigating hedging under this exemption.[63]

- ***"Demonstrably reduces" or otherwise "significantly mitigates" specific, identifiable risks.*** The Final Rule eliminates the requirement that the hedging activity "demonstrably reduces" or otherwise "significantly mitigates" risk, in line with the Proposed Rule.[64] The Agencies note that this requirement was not directly required by the statute,[65] which requires only that the hedge "be designed" to reduce or otherwise significantly mitigate specific risks.[66] The Agencies further acknowledge that, in practice, the requirement of a "demonstrable" reduction or mitigation of a specific, identifiable risk can be complex and could potentially reduce bona fide risk-mitigating hedging activity. In particular, the Agencies note that unforeseeable changes in market conditions, event risk, sovereign risk and other factors that cannot be known in advance could reduce or eliminate the otherwise intended hedging benefits.[67]

- ***Exception to documentation requirements for certain inter-desk hedging transactions.*** The Final Rule retains the enhanced documentation requirements for the risk-mitigating hedging exemption, with a new exception for certain commonly used, pre-approved hedging instruments that are used by one trading desk to hedge positions at another affiliated trading desk.[68] Financial instruments that would qualify for this exception must be identified on a written list of pre-approved financial instruments that are commonly used by the trading desk for the specific types of hedging activity for which the financial instrument is being purchased or sold. The limits must be appropriately tailored for: (i) the size, types and risks of the hedging activities commonly undertaken by the trading desk; (ii) the financial instruments purchased and sold by the trading desk for hedging activities; and (iii) the levels and duration of the risk exposures being hedged.[69]

The Final Rule streamlines the conditions of the risk-mitigating hedging exemption for banking entities with moderate or limited trading assets and liabilities. With respect to those banking entities, risk-mitigating hedging activities must (i) at the inception of the hedging activity (including any adjustments), be designed to reduce or otherwise significantly mitigate one or more specific, identifiable risks; and (ii) be subject to ongoing recalibration, as appropriate, to ensure that the hedge remains designed to reduce or otherwise significantly mitigate one or more specific, identifiable risks.[70] The Agencies explain that the conditions which have been eliminated with respect to banking entities with moderate or limited trading assets and liabilities—*e.g.*, internal compliance program requirements related to risk-mitigating hedging; limits on compensation arrangements for relevant personnel; and certain documentation

requirements—were overly burdensome and complex for banking entities that do not have significant trading assets and liabilities, which are generally less likely to engage in the types of trading activities and hedging strategies that would necessitate these additional compliance requirements.[71]

F. EXCLUSION FOR LIQUIDITY MANAGEMENT ACTIVITIES

Consistent with the Proposed Rule, the Final Rule broadens the liquidity management exclusion to allow banking entities to use foreign exchange forwards and foreign exchange swaps[72] and cross-currency swaps[73] as part of their liquidity management activities.[74] The Final Rule includes a further modification to the Proposed Rule to permit the use of non-deliverable cross-currency swaps (as opposed to only physically settled cross-currency swaps as under the Proposed Rule).[75] The Agencies state that the intent of this change is to permit banking entities to purchase and sell financial instruments generally as part of their liquidity management activities to the same extent they may purchase or sell securities under the existing exclusion, subject to the same conditions that currently apply with respect to securities transactions.[76]

The Agencies expressly declined to modify the requirement that liquidity management activities under this exclusion be conducted in accordance with a documented liquidity management plan with certain enumerated elements, notwithstanding concerns expressed by multiple commenters that such a requirement is unnecessarily prescriptive.[77] The Agencies emphasize that the documented liquidity management plan requirement, which is unchanged from the 2013 Rule, is a "key element in assuring that liquidity management is the purpose of the relevant transactions . . . . Under the plan, the purpose of the transactions must be liquidity management. The timing of purchases and sales, the types and duration of positions taken and the incentives provided to managers of these purchases and sales must all indicate that managing liquidity, and not taking short-term profits (or limiting short-term losses), is the purpose of these activities."[78]

G. EXCLUSION FOR ERROR TRADES

Consistent with the Proposed Rule, the Final Rule establishes a new exclusion for any purchase or sale of a financial instrument that was made in error by a banking entity in the course of conducting a permitted or excluded activity or is a subsequent transaction to correct such an error.[79] The Final Rule, however, does not adopt the Proposed Rule's requirement that the erroneously purchased (or sold) financial instrument must be promptly transferred to a separately managed trade error account for disposition, as the Agencies concurred with commenters' concerns that this requirement could have resulted in duplicative resolution systems and imposed undue regulatory costs.[80]

The Agencies explain that trading errors and subsequent correcting transactions are not proprietary trading because banking entities do not enter into these transactions principally for the purpose of selling

in the near-term (or otherwise with the intent to resell in order to profit from short-term price movements).[81] The Agencies intend to monitor use of this exclusion for evasion, noting that, for example, the magnitude or frequency of errors could indicate that the trading activity is inconsistent with this exclusion.[82]

H. EXCLUSION FOR CUSTOMER-DRIVEN MATCHED DERIVATIVE TRANSACTIONS

The Final Rule establishes a new exclusion for entering into a customer-driven swap or a customer-driven security-based swap and a matched swap or security-based swap if: (i) the transactions are entered into contemporaneously; (ii) the banking entity retains no more than minimal price risk; and (iii) the banking entity is not a registered dealer, swap dealer or security-based swap dealer.[83] The Agencies explain that a banking entity would retain "minimal price risk" if the economic terms of the two swaps (*e.g.,* index, amount, maturity and underlying reference asset or index) match.[84] Although the Proposed Rule did not include a specific amendment relating to loan-related swaps, the Final Rule's change was among the potential approaches discussed in the preamble to the Proposed Rule.[85]

The Agencies note that loan-related swaps in particular have presented a compliance challenge, especially for smaller non-dealer banking entities,[86] and intend that the new exclusion will reduce costs for non-dealer banking entities and avoid disrupting a common and traditional banking service provided to small and medium-sized businesses.[87] The Agencies emphasize, however, that the exclusion is not limited to loan-related swaps and could apply to swaps in connection with end-user activity that is not loan related.[88]

I. EXCLUSION FOR HEDGES OF MORTGAGE SERVICING RIGHTS OR ASSETS

The Final Rule establishes a new exclusion for any purchase or sale of one or more financial instruments that the banking entity uses to hedge mortgage servicing rights or mortgage servicing assets in accordance with a documented hedging strategy.[89] The Agencies state this exclusion is intended to clarify the scope of the prohibition on proprietary trading in this context and to provide parity between banking entities that are subject to the Market Risk Capital Prong and banking entities that are subject to the Short-Term Intent Prong.[90] This exclusion applies to all banking entities, including those subject to the Market Risk Capital Prong.

As the Agencies explain, financial instruments used to hedge mortgage servicing rights or assets generally would not be captured under the Market Risk Capital Prong. The market risk capital rule explicitly excludes intangibles, including servicing assets, from the definition of "covered position," and therefore financial instruments used to hedge servicing assets generally would not be captured under the Market Risk Capital Prong. Absent an explicit exclusion, banking entities that are subject to the Market Risk Capital Prong would have more certainty than banking entities that are subject to the Short-Term

Intent Prong that the purchase or sale of a financial instrument to hedge mortgage servicing rights or mortgage servicing assets is not proprietary trading.

J. EXCLUSION FOR FINANCIAL INSTRUMENTS THAT ARE NOT TRADING ASSETS OR TRADING LIABILITIES

The Final Rule establishes a new exclusion for any purchase or sale of a financial instrument that does not meet the definition of "trading asset" or "trading liability" under the banking entity's applicable reporting form as of January 1, 2020.[91] This exclusion applies to any purchase or sale of a financial instrument that does not meet the definition of "trading asset" or "trading liability" under the applicable reporting form of the banking entity as of the Final Rule's effective date of January 1, 2020. The exclusion applies to all banking entities, including those subject to the Market Risk Capital Prong.

Like the new exclusion for hedges of mortgage servicing rights or assets described above, the Agencies explain they are adopting this exclusion to provide parity between banking entities that are subject to the Market Risk Capital Prong (or that elect to apply the Market Risk Capital Prong) and banking entities that are subject to the Short-Term Intent Prong. Under the Market Risk Capital Prong, a purchase or sale of a financial instrument is within the trading account if it would be both a covered position and trading position under the market risk capital rule. In general, a position is a covered position under the Market Risk Capital Prong if it is a trading asset or trading liability (whether on- or off-balance sheet).[92] Thus, the exclusion for financial instruments that are not "trading assets and liabilities" extends the same certainty to banking entities subject to the Short-Term Intent Prong as is provided by operation of the Market Risk Capital Prong.[93]

K. TRADING BY FOREIGN BANKING ENTITIES OUTSIDE OF THE UNITED STATES

The Volcker Rule permits certain foreign banking entities to engage in proprietary trading that occurs solely outside of the United States. The Agencies' implementation of this exemption, referred to as the "TOTUS exemption," included five conditions under the 2013 Rule. The Final Rule, consistent with the Proposed Rule, simplifies one of these conditions and eliminates two others:[94]

- ***Involvement of U.S. personnel in arranging, negotiating or executing.*** The Final Rule continues to require that relevant personnel engaged in the decision to purchase or sell be located outside of the United States.[95] The Final Rule, however, permits U.S. personnel of the banking entity or its affiliate to be involved in arranging, negotiating or executing the trade. Under the 2013 Rule's implementation of the TOTUS exemption, these personnel were required to be located outside of the United States.

- ***Financing by U.S. branch or affiliate.*** The Final Rule removes the prohibition on financing for a banking entity's purchase or sale being provided by any branch, agency or affiliate that is located in the United States or organized under the laws of the United States or of any state.

- ***Conduct of trade "with or through any U.S. entity."*** The Final Rule also removes the condition to the TOTUS exemption that the purchase or sale not be "with or through" a U.S. entity (other than an unaffiliated market intermediary).

According to the Agencies, these modifications are intended in general to balance concerns regarding competitive impact while mitigating the concern that an overly narrow approach to the foreign trading exemption may cause market bifurcations, reduce the efficiency and liquidity of markets,[96] and impose requirements that foreign banking entities have found "overly difficult and costly . . . to monitor, track, and comply with in practice."[97]

Therefore, the TOTUS exemption under the Final Rule consists of three requirements: (i) the banking entity engaging as principal in the purchase or sale (including relevant personnel) is not located in the United States or organized under the laws of the United States or of any U.S. state; (ii) the banking entity (including relevant personnel) that makes the decision to purchase or sell as principal is not located in the United States or organized under the laws of the United States or of any U.S. state; and (iii) the purchase or sale, including any transaction arising from risk-mitigating hedging related to the instruments purchased or sold, is not accounted for as principal directly or 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 U.S. state.

Although the TOTUS exemption may be relied on only by foreign banking entities that are not owned, directly or indirectly, by a U.S. parent company, the Preamble includes two clarifications that are relevant to the U.S. counterparties of such foreign banking entities. First, the Agencies state that the conditions of the TOTUS exemption do not impose a duty on a U.S. banking entity to ensure that its foreign banking entity counterparty is conducting its activity in conformance with the Volcker Rule. Rather, a banking entity's compliance obligation under the Volcker Rule is to conduct its own activities in compliance with the relevant requirements.[98] Second, the Agencies confirm that the TOTUS exemption does not preclude a foreign banking entity from engaging a non-affiliated U.S. investment adviser to provide advisory services in connection with a transaction as long as the actions and decisions of the banking entity as principal occur outside of the United States.[99]

III. COVERED FUND ACTIVITIES AND INVESTMENTS

The Final Rule adopts, without change, the proposed revisions to the covered fund provisions for which specific rule text was included in the Proposed Rule.[100] The adopted revisions are relatively narrow in scope and do not cover any aspects of the covered fund provisions for which specific rule text was not proposed, nor does the Preamble include specific proposals with respect to further amendments to these provisions. As discussed in Section III.E below, the Agencies state in the Preamble that they continue to consider other aspects of the covered fund provisions on which they sought comment in connection with the Proposed Rule, including consideration of certain specific comments received thereon, and intend to issue a separate proposed rulemaking that specifically addresses those areas.[101]

A. PERMITTED UNDERWRITING AND MARKET MAKING-RELATED ACTIVITIES

Under the 2013 Rule, a banking entity was generally permitted to rely on the exemptions for underwriting and market making-related activities involving covered fund ownership interests, subject to certain quantitative limitations and a deduction from regulatory capital.[102] Specifically, if a banking entity acquired or retained any ownership interest in a covered fund in reliance on the exemptions for underwriting or market making-related activities, then that ownership interest was (i) included in the so-called "aggregate funds limitation" on a banking entity's total permitted investments in all covered funds and (ii) deducted from Tier 1 capital.[103] Further, if the banking entity had certain other relationships with the covered fund (*e.g.,* if the banking entity sponsored or advised the covered fund or guaranteed, assumed or otherwise insured the obligations or performance of the covered fund or of any other covered fund in which the first covered fund invested), then that ownership interest was also included in the so-called "per-fund limitation" on a banking entity's permitted investment in any single covered fund.[104]

Consistent with the Proposed Rule, the Final Rule removes the requirement to include in the calculation of the aggregate funds limitation and Tier 1 capital deduction the value of any ownership interests in a third-party covered fund (*i.e.*, funds that are not sponsored or advised by the banking entity or held in reliance on the organizing and offering exemption) that the banking entity acquires or retains in accordance with the exemptions for underwriting or market making-related activities.[105] This requirement is also eliminated for underwriting and market making activities involving covered funds with respect to which the banking entity directly or indirectly, guarantees, assumes or otherwise insures the obligations or performance of the covered fund or of any covered fund in which such fund invests.[106]

The Agencies note that banking entities have encountered practical difficulties in determining whether an issuer is a covered fund and whether the security issued is an ownership interest for the purpose of ensuring compliance with the aggregate fund limit and capital deduction requirement for the period of time that the banking entity holds the ownership interest as part of its permissible underwriting and market

making activities.[107] The Agencies believe these challenges are reduced in the case of funds that are advised or organized and offered by the banking entity, but nevertheless are continuing to consider whether the Final Rule's approach may be extended to "other issuers, such as funds advised by the banking entity[.]"[108]

B. PERMITTED RISK-MITIGATING HEDGING ACTIVITIES

Consistent with the Proposed Rule, the Final Rule permits a banking entity to acquire or retain an ownership interest in a covered fund as a risk-mitigating hedge when acting as an 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 (*e.g.*, in the context of fund-linked products).[109] A banking entity that seeks to rely on the exemption for customer facilitation activities must comply with all the requirements of Section _.13(a) of the Final Rule, which generally track the requirements of the risk-mitigating hedging exemption from the proprietary trading restriction set forth in Section _.5 of the Final Rule (as discussed in Section II.E above).[110] The Agencies emphasize that such customer facilitation activities must be "solely to accommodate a specific customer request with respect to the covered fund" and that a "banking entity cannot rely on this exemption to solicit customer transactions in order to facilitate the banking entity's own exposure to a covered fund."[111]

The Agencies' commentary accompanying the 2013 Rule indicated that the risk-mitigating hedging exemption generally could not be relied upon for this type of activity, which they believed to be a "high risk strategy that could threaten the safety and soundness of the banking entity."[112] In explaining the rationale for permitting this activity under the Final Rule's risk-mitigating hedging exemption, the Agencies state that they "do not believe that a banking entity's customer facilitation activities and related hedging activities involving ownership interests in covered funds necessarily constitute high-risk trading strategies that could threaten the safety and soundness of the banking entity."[113] The Agencies also note that, "properly monitored and managed, these activities can be conducted without creating a greater degree of risk to the banking entity than the other customer facilitation activities permitted by the [Final Rule]."[114] As the Agencies observe, such activities remain subject to the "prudential backstop" provisions of Section _.15 of the Final Rule.[115]

Paralleling a change to the risk-mitigating hedging exemption from the proprietary trading restriction, the Final Rule modifies the requirement under the 2013 Rule's risk-mitigating hedging exemption that the acquisition or retention of ownership interests in a covered fund "demonstrably reduce[ ]" or otherwise "significantly mitigate[ ]" specific, identifiable risks to the banking entity.[116] Consistent with the Proposed Rule, the Final Rule requires only that the hedge be "designed" to "reduce or otherwise significantly mitigate" specific, identifiable risks to the banking entity.[117]

C. INVESTMENT OR SPONSORSHIP "SOLELY OUTSIDE OF THE UNITED STATES"

The Final Rule modifies two conditions in the 2013 Rule's implementation of the Volcker Rule's so-called "SOTUS" exemption, which permits certain foreign banking entities to acquire or retain an ownership interest in, or act as sponsor to, a covered fund, so long as those activities and investments occur solely outside the United States and certain other conditions are satisfied.[118] The 2013 Rule required, among other conditions, that (i) no ownership interest in the covered fund is "offered for sale or sold" to a "resident of the United States" (defined to mean a "U.S. person" as defined in the SEC's Regulation S) (the "U.S. Marketing Restriction")[119] and (ii) no financing for the banking entity's ownership or sponsorship is provided, directly or indirectly, by any branch or affiliate located in the United States or organized under the laws of the United States or of any U.S. state (the "U.S. Financing Restriction").[120]

Consistent with the Proposed Rule, the Final Rule modifies these two conditions as follows:[121]

- ***Codification of guidance on U.S. Marketing Restriction.*** The Final Rule codifies the Agencies' previously issued guidance (provided in FAQ #13) regarding the U.S. Marketing Restriction.[122] Specifically, the Final Rule provides that an ownership interest in a covered fund satisfies the U.S. Marketing Restriction "only if [the ownership interest] 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 is deemed to participate in any offer or sale by the covered fund of ownership interests in the covered fund.[123] In other words, a foreign banking entity's ability to rely on the SOTUS exemption would not be lost as a result of third parties' marketing or selling activities to residents of the United States, provided that the foreign banking entity has not itself offered for sale or sold an ownership interest in the fund to a resident of the United States or participated in such an offer or sale.

- ***Elimination of U.S. Financing Restriction.*** Consistent with the change to the parallel restriction in the TOTUS exemption, the Final Rule eliminates the U.S. Financing Restriction from the SOTUS exemption.[124] The Agencies explain that this modification is intended to streamline the requirements of the SOTUS exemption, which are designed to require that the principal risks of covered fund investments and sponsorship by foreign banking entities occur and remain solely outside of the United States.[125]

Finally, the Agencies confirm that the SOTUS exemption "does not preclude a foreign banking entity from engaging a non-affiliated U.S. investment adviser as long as the actions and decisions of the banking entity as principal occur outside of the United States."[126]

D. PRIME BROKERAGE EXEMPTION

The Volcker Rule's so-called "Super 23A" prohibition is subject to an exemption for prime brokerage transactions[127] with a "second-tier" covered fund—*i.e.*, a third-party covered fund in which a covered fund that is managed, sponsored, or advised by a banking entity has taken an ownership interest.[128] The conditions to qualify for the prime brokerage exemption include, among others, that the CEO (or equivalent officer) of the banking entity must certify in writing annually 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.[129] The Final Rule, consistent with the Agencies' previously issued guidance in FAQ #18[130] and the Proposed Rule,[131] provides that the officer's annual certification is due no later than March 31 of the relevant year.[132] The Agencies reiterate in the Preamble that the officer has a duty to update the certification if the information in the certification materially changes at any time during the year when he or she becomes aware of the material change.[133]

As discussed further below, the Agencies indicate in the Preamble that other aspects of Super 23A and the prime brokerage exemption remain under consideration and may be addressed in future rulemaking.

E. AREAS IDENTIFIED FOR POTENTIAL RE-PROPOSAL

The Agencies state in the Preamble that, although they are not adopting any changes to the covered fund provisions other than those for which specific rule text was proposed in the Proposed Rule, that approach "does not reflect any final determination with respect to the comments received on other aspects of the covered fund provisions."[134] Outlined below are the topics, together with certain related comments received in response to the Proposed Rule, that the Agencies specifically note are under consideration and are intended to be addressed in a subsequent proposed rulemaking:

Final Rule Provision	Issues and Comments Identified in Preamble as Topics for Re-Proposal
Definition of "Banking Entity"	• Comments expressing concern that "certain funds that are excluded from the definition of 'covered fund' in the [regulations], including registered investment companies (RICs), foreign public funds (FPFs), and, with respect to a foreign banking entity, certain foreign funds offered and sold outside of the United States (foreign excluded funds)" could meet the definition of "banking entity" due to "the interaction between the [BHC Act's and the regulation's] definitions of the terms 'banking entity' and 'covered fund.'"[135] • "[W]ays in which the regulations may be amended in a manner consistent with the statutory definition of 'banking entity,' or other appropriate actions that may be taken . . . that specifically addresses the fund structures under the rule, including the treatment of foreign excluded funds."[136]
Definition of "Covered Fund"	• "[G]eneral approach to defining the term 'covered fund,' as well as the existing "exclusions from the covered fund definition and potential new exclusions from this definition."[137]

Final Rule Provision	Issues and Comments Identified in Preamble as Topics for Re-Proposal
Permitted Underwriting and Market Making	• Comments supporting "additional revisions to § _.11 by eliminating the aggregate fund limit and capital deduction for other funds, such as affiliated funds or sponsored funds and advised funds."[138]
Per-fund and Aggregate Funds Limitations	• Comment recommending that "the aggregate fund limit should apply only at the global consolidated level for all firms."[139] • Comment recommending that "the [Agencies] should expand the per-fund limit to allow bank-affiliated securitization investment managers to rely on applicable foreign risk retention regulations as a basis for exceeding the three percent per-fund limitation, provided that those foreign regulations are generally comparable to U.S. requirements."[140] • Comment requesting that the Agencies "clarify that the [regulations] do[ ] not prohibit banking entities from making direct investments alongside covered funds, regardless of whether the fund is sponsored or the investments are coordinated, so long as such investments are otherwise authorized for such banking entities (*e.g.*, under merchant banking authority)."[141]
Super 23A and Prime Brokerage Exemption	• Generally, prohibitions on covered transactions with a covered fund for which a banking entity serves, directly or indirectly, as the investment manager, investment adviser or sponsor to a hedge fund or private equity fund, or that the banking entity organizes and offers.[142] • Comments regarding the scope of the term "prime brokerage transaction" and requested expansions or limitations to that list of transactions.[143] • Comment recommending that the Agencies "expressly state that the CEO certification for purposes of the prime brokerage exemption is based on a reasonable review by the CEO and is made based on the knowledge and reasonable belief of the CEO."[144] • Comment suggesting that "any prime brokerage transaction with a second-tier covered fund should be presumed to comply with section _.14 of the rule and the prime brokerage exemption as long as it is executed in compliance with the requirements of Section 23B of the Federal Reserve Act."[145]

IV. COMPLIANCE PROGRAM AND METRICS

A. COMPLIANCE PROGRAM

The 2013 Rule established compliance program requirements for all banking entities (with simplified requirements for smaller banking entities).[146] As described in Section I above, the Final Rule establishes three categories of banking entities based on trading assets and liabilities, each with different tiers of compliance programs and other requirements.

The Final Rule also removes the "enhanced" compliance program requirements, set forth in Appendix B to the 2013 Rule. The Agencies state that this change "will afford a banking entity considerable flexibility to satisfy the [Volcker Rule's compliance requirements] in a manner that it determines to be most

appropriate given its existing compliance regimes, organizational structure, and activities" and will "eliminate[ ] duplicative governance and oversight structures arising from the Appendix B requirement for a stand-alone compliance program."[147] Although the Final Rule eliminates Appendix B, many of the other aspects of the 2013 Rule's compliance program requirements apply in unchanged form for banking entities with significant trading assets and liabilities—namely, the six-pillar compliance program,[148] CEO attestation and covered fund documentation requirements.[149]

B. QUANTITATIVE TRADING METRICS

The Final Rule includes amendments intended to streamline and reduce compliance-related inefficiencies associated with the Quantitative Metrics Reporting and Recordkeeping Requirements, included as Appendix A to the 2013 Rule. Only banking entities with significant trading assets and liabilities are required to report quantitative trading metrics under the Final Rule and must do so on a quarterly basis within 30 days of each quarter-end (as opposed to within 10 days of each calendar month-end as required by Appendix A to the 2013 Rule).[150] Banking entities will not be required to comply with the Final Rule, including the modified metrics reporting requirements, until the Final Rule's compliance date of January 1, 2021, although they may voluntarily do so prior to the compliance date "subject to the agencies' completion of necessary technical changes."[151]

Summarized below are key aspects of the Final Rule's changes to the quantitative metrics regime. The Agencies estimate that the revised metrics reporting requirements in the Final Rule will result in a 67 percent reduction in the number of data items and a 94 percent reduction in the total volume of data relative to the 2013 Rule's reporting requirements.[152]

Changes to calculation of certain metrics.

- ***Removal of Inventory Turnover metric.*** The 2013 Rule requires banking entities to calculate and report inventory turnover, or the turnover of a trading desk's inventory, over a 30-, 60- and 90-day reporting period.[153] The Final Rule eliminates this metric and includes the new "Positions" metric, which requires that subject banking entities report the daily positions data underlying the Inventory Turnover metric without the need for aggregating or limiting the data according to specific calculation periods.[154] Accordingly, the Agencies believe the Positions metric will allow for better analysis of trading activity over different time horizons and will not require firms to generate additional data not currently produced internally because the 2013 Rule's Inventory Turnover data relied on the same underlying positions data the Positions metric requires.[155]
- ***Replacement of Customer-Facing Trade Ratio with Transactions Volume metric.*** The Final Rule replaces the 2013 Rule's Customer-Facing Trade Ratio, which compares transactions involving a counterparty that is a customer of the trading desk (*i.e.*, a "client, customer, and

counterparty" as defined for purposes of the Final Rule) to those where the trading desk's counterparty is a non-customer, with the "Transactions Volume" metric. Rather than reporting such transactions data over a specified reporting period, the Transactions Volume metric requires a daily reporting of the value and number of security and derivative transactions conducted by the trading desk with three categories of counterparties: (i) customers (excluding desk-to-desk transactions within the same legal entity and transactions between, collectively referred to as "Internal Transactions"); (ii) non-customers (excluding Internal Transactions); and (iii) trading desks or other organizational units booking the transaction within the same banking entity or in an affiliated banking entity.[156] The Agencies state that this new metric will allow supervisors to more readily distinguish "Internal Transactions from transactions with external non-affiliated counterparties because, based on supervisory experience under the 2013 [R]ule, firms report these transactions inconsistently depending on a desk's purpose and business model."[157]

- ***Removal of Inventory Aging metric.*** The 2013 Rule requires all trading desks engaged in covered trading activities to report Inventory Aging metrics for their securities and derivative positions.[158] The Proposed Rule would have renamed this metric the "Securities Inventory Aging" metric and only applied it to securities (and not also to derivatives).[159] In light of the comments received and the Agencies' "general desire to reduce reporting burden," the Final Rule does not contain any type of Inventory Aging requirement as "[such] metric may be overly prescriptive as an indicator of compliance with the [Volcker Rule]."[160]

- ***Removal of Stressed Value-at-Risk ("VaR") and Risk Factor Sensitivities metrics.*** In an effort to further reduce the reporting burden on banking entities without compromising the ability of the Agencies to monitor for impermissible proprietary trading, the Final Rule includes neither the Proposed Rule's Stressed VaR metric, which would have required each trading desk to measure VaR daily based on market conditions during a period of significant stress, nor the 2013 Rule's Risk Factor Sensitivities metric, which generally requires each trading desk to report changes impacting its profitability and risk on a daily basis.[161]

Trading Desk Information. The Final Rule retains a modified version of the Proposed Rule's requirement that banking entities begin to report descriptive information regarding each trading desk engaged in covered trading activities, referred to as "Trading Desk Information."[162] Under the Final Rule, the Trading Desk Information must include the following elements: (i) the trading desk name and trading desk identifier; (ii) the type of covered trading activity; (iii) brief description of trading desk's strategy; (iv) a list of each Agency receiving the submission of the Trading Desk Information; (v) the trading day indicator; and (vii) the currency used by the trading desk and, if applicable, the conversion rate of such currency to U.S. dollars.[163] The Final Rule does not include the Proposed Rule's requirements that a

banking entity report the types of financial instruments and other products traded by the desk and the legal entities that serve as booking entities for each trading desk.

Quantitative Measurements Identifying Information. The Final Rule requires banking entities to submit, collectively for all relevant trading desks, the following schedules, which collectively comprise the Quantitative Measurements Identifying Information: (i) a Risk Factor Attribution Information Schedule that provides certain identifying and descriptive information for each risk factor attribution reported pursuant to the Comprehensive Profit and Loss Attribution metric; and (ii) a Risk and Position Limits Information Schedule that includes identification of the corresponding risk factor attribution for each limit reported pursuant to the Internal Limits and Usage metric.[164] The Proposed Rule had included three other schedules that the Agencies determined not to include in the Final Rule on the basis that they "could significantly increase firms' reporting burden in a way not commensurate with the potential benefits": (i) the Risk Factor Sensitivities Information (consistent with the Agencies' removal of this metric in its entirety); (ii) Limit/Sensitivity Cross-References; and (iii) Risk Factor Sensitivity/Attribution Cross-References.[165]

Narrative Statement. The Final Rule omits the Proposed Rule's affirmative obligation that banking entities periodically submit a Narrative Statement describing, among other things, any changes in calculation methods used for quantitative trading metrics or in trading desk structure or strategies. Rather, the Final Rule retains a provision from the 2013 Rule's reporting instructions that allow, but do not require, banking entities to submit a narrative statement containing any information viewed as helpful for the Agencies to consider in connection with their assessment of the firms' reported information.[166] The Agencies observe that these optional narrative statements "may permit the [A]gencies to understand aspects of the metrics without going back to the banking entities to ask questions."[167]

* * *

ENDNOTES

[1] 12 U.S.C. § 1851.

[2] OCC, Federal Reserve, FDIC and SEC, *Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds*, 79 Fed. Reg. 5535 (Jan. 31, 2014); CFTC, *Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds*, 79 Fed. Reg. 5807 (Jan. 31, 2014). Each Agency adopted the 2013 Rule and codified it separately in its respective regulations. *See* 12 C.F.R. §§ 248 (Federal Reserve); 44 (OCC); 351 (FDIC); and 17 C.F.R. §§ 255 (SEC); 75 (CFTC). References and citations herein to the 2013 Rule are to the currently effective common rule text. For a discussion of the requirements of the 2013 Rule, please see our Client Memorandum, *Volcker Rule: U.S. Agencies Approve Final Volcker Rule, Detailing Prohibitions and Compliance Regimes Applicable to Banking Entities Worldwide*, dated January 27, 2014, *available at* https://www.sullcrom.com/Volcker-Rule-01-27-2014.

[3] On July 9, 2019, the Agencies adopted amendments to modify the Volcker Rule implementing regulations in a manner consistent with Sections 203 and 204 of the EGRRCPA. Pursuant to the amendments implementing Section 203, institutions that have (i) total consolidated assets equal to $10 billion or less *and* (ii) total trading assets and liabilities equal to 5% or less of total consolidated assets are excluded from the definition of "insured depository institution," and therefore generally are excluded from the scope of "banking entities" that are subject to the Volcker Rule. For further discussion of these amendments, please see our Client Memorandum, *Volcker Rule: Federal Banking Agencies, SEC and CFTC Approve Final Rule to Exclude Certain Smaller Institutions from Banking Entity Status and Modify Fund Name-Sharing Restrictions, Conforming to the Economic Growth, Regulatory Relief, and Consumer Protection Act*, dated July 10, 2019, *available at* https://www.sullcrom.com/agencies-adopt-amendments-to-volcker-rule-regulations.

[4] Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, 12 U.S.C. §5301 *et seq*; *see also, e.g.*, 12 C.F.R. Part 1022 (*Bureau of Consumer Financial Protection's Regulation V (Fair Credit Reporting*)); 12 C.F.R. Part 1310 (*Financial Stability Oversight Council's Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies*)

[5] Under the federal banking agencies' capital rules, the market risk capital rule generally applies if the banking organization has aggregate trading assets and trading liabilities equal to (i) 10% or more of quarter-end total assets; or (ii) $1 billion or more. *See* 12 C.F.R. §§ 3.201(b) (OCC), 217.201(b) (Federal Reserve) and 324.201(b) (FDIC).

[6] The Agencies estimate that 93 percent of trading assets and liabilities in the U.S. banking system are held by banking entities with over $20 billion in trading assets and liabilities and that, under the Final Rule, firms with significant or moderate trading assets and liabilities collectively hold approximately 99 percent of the total trading assets and liabilities in the U.S. Preamble at 30. The Agencies note that increasing the relevant threshold to $20 billion for designating banking entities as having "significant trading assets and liabilities" would provide greater certainty to firms that are near or approaching the $10 billion threshold and might exceed it (permanently or on a short-term basis) due to market events or unusual customer demands. Preamble at 29–30.

[7] A banking entity could be subject under the 2013 Rule to any of five different tiers of compliance program requirements, each of which entails a different set of required policies and procedures, recordkeeping, internal controls and other compliance program elements, as well as, potentially, quantitative metrics reporting and attestation requirements. For further detail regarding the specific requirements associated with the compliance program tiers under the 2013 Rule, please see Section 10 of our Client Memorandum, *Volcker Rule: U.S. Agencies Approve Final Volcker Rule, Detailing Prohibitions and Compliance Regimes Applicable to Banking Entities Worldwide*, dated January 27, 2014, *available at* https://www.sullcrom.com/Volcker-Rule-01-27-2014/.

ENDNOTES (CONTINUED)

8 Final Rule §§ ._2(ee)(2)–(3).

9 Preamble at 32.

10 *See supra* note 3.

11 Final Rule § ._20(h).

12 Final Rule § ._20(i).

13 *Id.*

14 The additional documentation requirements for covered funds under § _.20(e) of the 2013 Rule continue to apply to banking entities with significant trading assets and liabilities under the Final Rule, including documentation of the exclusions or exemptions relied on by each fund sponsored by the banking entity, written seeding plans for certain types of seeding vehicles and, for certain U.S. banking entities, documentation of the value of the banking entity's ownership interests in foreign public funds.

15 Preamble at 198.

16 Banking entities with limited trading assets and liabilities have no affirmative obligation to demonstrate compliance with the Proposed Rule on an ongoing basis. However, if upon examination or audit, the relevant Agency determines that the banking entity has engaged in covered activities, such Agency may rebut the presumption of compliance and require the banking entity to demonstrate compliance with the requirements of the rule applicable to a banking entity with moderate trading assets and liabilities pursuant to the same notice and response procedures applicable to an Agency's determination to subject a banking entity without significant trading assets and liabilities to compliance requirements applicable to firms in that category. Final Rule § _.20(g), (i). *See also* Preamble at 201–02.

17 12 U.S.C. § 1851(h)(1)(B).

18 12 U.S.C. § 1851(h)(6).

19 Proposed Rule § _.3(b)(3).

20 Preamble at 41–42.

21 Final Rule § _.3(b)(1)(i). Pages 7–8 of Appendix A of this Memorandum contain the changes made to § _.3(b) as between the 2013 Rule and the Final Rule. Pages 7–9 of Appendix B of this Memorandum contain the changes made to § _.3(b) as between the Proposed Rule and the Final Rule.

22 Preamble at 50.

23 Final Rule § _.3(b)(2)(ii).

24 Proposed Rule § _.3(b)(1).

25 Final Rule § _.3(b)(4).

26 Final Rule § _.3(b)(1)(ii). *See also* 12 CFR 3.202(b); 12 CFR 217.202(b); 12 CFR 324.202(b).

27 Final Rule § _.3(b)(1)(ii). *See also* 12 CFR 3.202(b); 12 CFR 217.202(b); 12 CFR 324.202(b).

28 Final Rule § _.3(b)(3)(i).

29 Final Rule § _.3(b)(3)(ii).

30 Preamble at 59.

31 Proposed Rule § _.3(b)(1)(ii); Preamble at 56.

32 Final Rule § _.3(b)(1)(iii).

33 Preamble at 61.

34 Preamble at 61.

35 Preamble at 92.

36 Final Rule § _.3(e)(13).

37 Preamble at 93–94.

38 Preamble at 92–93.

39 Preamble at 92.

40 Preamble at 92 n. 346.

41 Preamble at 101.

42 *Id*.

43 Final Rule § _.4(c)(1)(ii)(A); Pages 13–18 of Appendix A of this Memorandum contain the changes made to § _.4 as between the 2013 Rule and the Final Rule. Pages 15–21 of Appendix B of this Memorandum contain the changes made to § _.4 as between the Proposed Rule and the Final Rule.

44 Final Rule § _.4(c)(2).

45 Preamble at 116.

46 Final Rule § _.4(c)(4); Preamble at 120.

47 *See* Final Rule § _.20(i)).

48 Final Rule § _.4(c)(3)(i).

49 Final Rule § _.4(a)(2)(iii).

50 Preamble 127-28

51 Final Rule § _.4(c)(1)(ii)(B).

52 Preamble at 119.

53 *Id*.

54 Preamble at 138.

55 *I'd.*

56 Preamble at 138–39 (emphasis added).

57 Preamble at 139–40.

58 Final Rule § _.4(c)(3).

59 Final Rule § _.4(c)(3).

60 Final Rule § _.4(c)(4).

61 Final Rule § _.4(b)(2)(iii).

62 Final Rule § _.5(b)(1)(i)(C). Pages 18–21 of Appendix A of this Memorandum contain the changes made to § _.5 as between the 2013 Rule and the Final Rule. Pages 21–24 of Appendix B of this Memorandum contain the changes made to § _.5 as between the Proposed Rule and the Final Rule.

63 Preamble at 149.

64 Final Rule §§ _.5(b)(1)(i)(C); _.5(b)(1)(ii)(B); _.5(b)(1)(ii)(D)(2).

ENDNOTES (CONTINUED)

65 Preamble at 150.

66 12 U.S.C. § 1851(d)(1)(C).

67 Preamble at 150.

68 Final Rule § _.5(c)(4).

69 Final Rule § _.5(c)(4)(ii).

70 Final Rule §§ _.5(b)(2); _.5(c).

71 Preamble at 145.

72 The Final Rule's definitions of "foreign exchange forward" and "foreign exchange swap" reference the corresponding definitions of such terms in the Commodity Exchange Act. Final Rule § _.3(d)(3). *See also* 7 U.S.C. §§ 1a(24) and 1a(25). Pages 8–10 of Appendix A of this Memorandum contain the changes made to § _.3(d) as between the 2013 Rule and the Final Rule. Pages 10–12 of Appendix B of this Memorandum contain the changes made to § _.3(d) as between the Proposed Rule and the Final Rule.

73 The Final Rule defines a "cross-currency swap" as a swap in which one party exchanges with another party principal and interest rate payments in one currency for principal and interest rate payments in another currency, and the exchange of principal occurs on the date the swap is entered into, with a reversal of the exchange of principal at a later date that is agreed upon when the swap is entered into. Final Rule § _.3(e)(5).

74 Final Rule § _.3(d)(3).

75 Final Rule § _.3(e)(5).

76 Final Rule §§ _.3(d)(3)(i)–(vi).

77 Preamble at 70.

78 Preamble at 69–70.

79 Final Rule § _.3(d)(10).

80 Preamble 75.

81 *Id.*

82 *Id.*

83 Final Rule § _.3(d)(11).

84 Preamble at 84, n. 323.

85 *See* 83 Fed. Reg. 33432, 33463–44 (July 17, 2018).

86 Preamble at 77.

87 Preamble at 82.

88 Preamble at 82–83.

89 Final Rule § _.3(d)(12).

90 Preamble at 86–87.

91 Final Rule § _.3(d)(13).

92 *See* Preamble at 88 n.330; *see also* 12 CFR 3.202(b); 12 CFR 217.202(b); 12 CFR 324.202(b). In addition, the market risk capital rule's "covered position" definition expressly includes and excludes additional classes of instruments.

ENDNOTES (CONTINUED)

93 Preamble at 88.

94 BHC Act § 13(d)(1)(H).

95 Preamble at 158.

96 Preamble at 164.

97 Preamble at 161.

98 Preamble at 162.

99 Preamble at 165.

100 Preamble at 166.

101 Preamble at 166.

102 2013 Rule § _.11. Pages 35–37 of Appendix A of this Memorandum contain the changes made to § _.11 as between the 2013 Rule and the Final Rule. Pages 38–41 of Appendix B of this Memorandum contain the changes made to § _.11 as between the Proposed Rule and the Final Rule.

103 2013 Rule § _.11(c)(3).

104 2013 Rule § _.11(c)(2).

105 Final Rule § _.11(c).

106 *See* Preamble at 170 n. 571; Final Rule § _.11(c)(2).

107 Preamble at 170–71.

108 Preamble at 171.

109 Final Rule § _.13(a)(1)(ii). Pages 42–45 of Appendix A of this Memorandum contain the changes made to § _.13 as between the 2013 Rule and the Final Rule. Pages 47–50 of Appendix B of this Memorandum contain the changes made to § _.13 as between the Proposed Rule and the Final Rule.

110 Preamble at 174–176.

111 Preamble at 176.

112 *See* 79 Fed. Reg. at 5737.

113 Preamble at 176–77.

114 Preamble at 177.

115 Preamble at 177.

116 Final Rule § _.13(a)(2)(ii)(B). *See also* 2013 Rule § _.13(a)(2)(ii)(B).

117 Final Rule § _.13(a)(1).

118 Final Rule § _.13(b). Other than the U.S. Marketing Restriction, the remaining conditions to the Final Rule's SOTUS exemption are that: (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 U.S. 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) 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 (iv) 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.

119 2013 Rule §§ _.13(b)(1)(iii); _.10(d)(8).

120 2013 Rule §§ _.13(b)(1)(iv); _.13(b)(4)(iv).

121 Final Rule § _.13(b).

122 Final Rule § _.13(b)(3). Following the issuance of the 2013 Rule, the U.S. Marketing Restriction became the subject of uncertainty and industry comment, as it was unclear whether foreign banking entities would be able to rely on the SOTUS exemption with respect to investments in third-party covered funds, such as offshore feeder funds with U.S. tax-exempt investors or other covered funds, where the fund sponsor or investors other than the foreign banking entity had engaged in U.S. marketing activities. The staffs of the Agencies issued guidance through a response to FAQ #13 clarifying that the U.S. Marketing Restriction applies *only* to the activities of the foreign banking entity (including its affiliates) that is seeking to rely on the SOTUS exemption and not to the activities of third parties, including the sponsor of the covered fund, other investors and the covered fund itself. Thus, a foreign banking entity's ability to rely on the exemption would not be lost as a result of third parties' marketing or selling activities to residents of the United States, provided that the foreign banking entity has not itself offered for sale or sold an ownership interest in the fund to a resident of the United States or participated in such an offer or sale. Client Memorandum, *Agencies Release New Volcker Rule FAQ with Critical Guidance for Foreign Banking Entities and Fund Sponsors; Clarify That U.S. Marketing Restriction Under "SOTUS" Covered Fund Exemption Does Not Apply to Third Parties*, dated February 27 2015, *available at* https://www.sullcrom.com/volcker-rule-agencies-release-new-volcker-rule-faq-with-critical-guidance-for-foreign-banking-entities-and-fund-sponsors.

123 Final Rule § _.13(b)(3). The Agencies also reaffirm that the SOTUS exemption "permits the U.S. personnel and operations of a foreign banking entity to act as investment adviser to a covered fund in certain circumstances," noting that "[f]or example, the U.S. personnel of a foreign banking entity may provide investment advice and recommend investment selections to the manager or general partner of a covered fund so long as the investment advisory activity in the United States does not result in U.S. personnel participating in the control of the covered fund or offering or selling an ownership interest to a resident of the United States." Preamble at 183.

124 *See* Final Rule § _.13(b)(4).

125 Preamble at 179, 182.

126 Preamble at 183–84.

127 For this purpose, a "prime brokerage transaction" is defined to mean 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. Final Rule § _.10(d)(7). The Agencies specifically note that they are considering and intend to address comments received on the scope of the term "prime brokerage transaction," including a request that the Agencies clarify that the term includes "(1) lending and borrowing of financial assets, (2) provision of secured financing collateralized by financial assets, (3) repurchase and reverse repurchase of financial assets, (4) derivatives, (5) clearance and settlement of transactions, (6) 'give-up' agreements, and (7) purchase and sale of financial assets from inventory." Preamble at 186–87.

128 Final Rule § _.14(a)(2)(ii). Pages 45–46 of Appendix A of this Memorandum contain the changes made to § _.14 as between the 2013 Rule and the Final Rule. Pages 50–51 of Appendix B of this

Memorandum contains the changes made to § _.14 as between the Proposed Rule and the Final Rule.

129 Final Rule § _.14(a)(2)(ii)(B).

130 FAQ # 18, *available at* https://www.federalreserve.gov/supervisionreg/faq.htm#18.

131 Proposed Rule § _.14(a)(2)(ii)(B).

132 Final Rule § _.14(a)(2)(ii)(B).

133 Preamble at 186.

134 Preamble at 166.

135 Preamble at 18–19.

136 Preamble at 20.

137 Preamble at 165.

138 Preamble at 169 (internal citations omitted).

139 Preamble at 172.

140 Preamble at 173.

141 Preamble at 173.

142 Preamble at 184.

143 Preamble at 186–87. In addition to the comment requesting inclusion of the seven enumerated transactions referenced in note 127, *supra*, in the term "prime brokerage transaction," the Agencies specifically note that they are also considering and intend to address comments (1) requesting clarification that the term "applies to any transaction provided in connection with custody, clearance and settlement, securities borrowing or lending services, trade execution, financing, or data, operational, and administrative support regardless of which business line within the banking entity conducts the business" and (2) recommending "limiting the prime brokerage exemption by, for instance, excluding financing and securities lending and borrowing from the prime brokerage exemption." Preamble at 187.

144 Preamble at 186.

145 Preamble at 187.

146 2013 Rule § _.20. Pages 48–52 of Appendix A of this Memorandum contains the changes made to § _.20 as between the 2013 Rule and the Final Rule. Pages 52–56 of Appendix B of this Memorandum contain the changes made to § _.20 as between the Proposed Rule and the Final Rule.

147 Preamble at 194.

148 The Agencies noted that, based on several years' experience with the six-pillar compliance program, they believe "such requirements are appropriate and effective for firms with significant trading assets and liabilities [and] impose certain minimum standards, but permit the banking entity flexibility to reasonably design the program in light of the banking entity's activities." Preamble at 193. Another stated reason for retaining the six-pillar compliance program is that the Agencies consider its requirements to be "consistent with the standards banking entities use in their traditional risk management and compliance processes." *Id.*

149 Preamble at 193–197.

150 Final Rule § _.20(d)(2).

ENDNOTES (CONTINUED)

151 Preamble at 13.

152 Preamble at 206.

153 2013 Rule Appendix A at para IV.c.1.iii.

154 Final Rule Appendix at para IV.c.1. Pages 52–62 of Appendix A of this Memorandum contain the changes made to the appendix as between the 2013 Rule and the Final Rule. Pages 57–66 of Appendix B of this Memorandum contain the changes made to the appendix as between the Proposed Rule and the Final Rule.

155 Preamble at 227–28. The Final Rule also removes the requirement to report the notional value of derivatives to avoid complexities arising from banking entities using different calculation methods for ascertaining the notional value of different derivatives. *Id.* at 228.

156 Final Rule Appendix at para IV.c.2.i.

157 Preamble at 231. Note that the Positions and Transaction Volumes metrics are applicable only to trading desks that rely upon the exemptions for underwriting or market making-related activities. Final Rule Appendix at para IV.c.1–2.

158 2013 Rule Appendix A at para IV.c.2.

159 Preamble at 232.

160 Preamble at 232–33.

161 Preamble at 222–24.

162 Preamble at 213.

163 Final Rule Appendix at para. III.b.

164 Final Rule Appendix at para. III.c.

165 Preamble at 215.

166 Final Rule Appendix at para. III.d.

167 Preamble at 217.

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APPENDIX A

Volcker Rule Implementing Regulations

(Textual Comparison of the 2013 Rule against the 2019 Rule)[1]

Subpart A—Authority and Definitions

§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

[1] **[N.B.: The base text that was used to generate this comparison is drawn from the Federal Reserve's Regulation VV (12 C.F.R. § 248.1), including the amendments thereto adopted on July 9, 2019 implementing Sections 203 and 204 of the Economic Growth, Regulatory Relief, and Consumer Protection Act.]**

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 paragraphs (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 paragraphs (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, ~~guidance,~~ 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*~~, unless otherwise indicated,~~ 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.*

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

(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 § ___.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 [Agency] has not determined pursuant to § __.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 (3), 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 § ___.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 § ___.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.

(~~s~~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.

(~~t~~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)).

(~~u~~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.

(~~v~~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)).

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

(~~x~~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.

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

(~~z~~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)).

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

(~~bb~~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.*

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

(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 [Agency] has determined pursuant to § ___.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 (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 § ___.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 § ___.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.

(~~cc~~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.

(~~dd~~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)).

(~~ee~~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.

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

Subpart B—Proprietary Trading

§248.3 Prohibition on proprietary trading.

(a) *Prohibition.* Except as otherwise provided in this subpart, a banking entity may not engage in proprietary trading. *Proprietary trading* means engaging as principal for the trading account of the banking entity in any purchase or sale of one or more financial instruments.

(b) *Definition of trading account.* (1) *Trading account* means:

(i) any account that is used by a banking entity to ~~:(i) P~~ purchase or sell one or more financial instruments principally for the purpose of ~~:(A) S~~short-term resale ~~;(B) B~~benefitting from actual or expected short-term price movements ~~;(C) R~~realizing short-term arbitrage profits ~~;~~ or ~~(D) H~~hedging one or more of the positions resulting from the purchases or sales of financial instruments described in ~~paragraphs (b)(1)(i)(A), (B), or (C) of this section~~this paragraph;

(ii) Any account that is used by a banking entity to ~~P~~purchase or sell one or more financial instruments that are both market risk capital rule covered positions and trading positions (or hedges of other market risk capital rule covered positions), if the banking entity, or any affiliate ~~of~~ with which the banking entity ~~,~~ is ~~an insured depository institution, bank holding company, or savings and loan holding company, and~~ consolidated for regulatory reporting purposes, calculates risk-based capital ratios under the market risk capital rule; or

(iii) Any account that is used by a banking entity to ~~P~~purchase or sell one or more financial instruments ~~for any purpose~~, if the banking entity:

(A) Is licensed or registered, or is required to be licensed or registered, to engage in the business of a dealer, swap dealer, or security-based swap dealer, to the extent the instrument is purchased or sold in connection with the activities that require the banking entity to be licensed or registered as such; or

(B) Is engaged in the business of a dealer, swap dealer, or security-based swap dealer outside of the United States, to the extent the instrument is purchased or sold in connection with the activities of such business.

(2)(i) A banking entity that is subject to paragraph (b)(1)(ii) in determining the scope of its trading account is not subject to paragraph (b)(1)(i).

(ii) A banking entity that does not calculate risk-based capital ratios under the market risk capital rule and is not a consolidated affiliate for regulatory reporting purposes of a banking entity that calculates risk based capital ratios under the market risk capital rule may elect to apply paragraph (b)(1)(ii) of this section in determining the scope of its trading account as if it were subject to that paragraph. A banking entity that elects under this subsection to apply paragraph (b)(1)(ii) of this section in determining the scope of its trading account as if it were subject to that paragraph is not required to apply paragraph (b)(1)(i) of this section.

(3) *Consistency of account election for certain banking entities*.

(i) Any election or change to an election under paragraph (b)(2)(ii) of this section must apply to the electing banking entity and all of its wholly owned subsidiaries. The primary financial regulatory agency of a banking entity that is affiliated with but is not a wholly owned subsidiary of such electing banking entity may require that the banking entity be subject to this uniform application requirement if the primary financial regulatory agency determines that it is necessary to prevent evasion of the requirements of this part after notice and opportunity for response as provided in Subpart D.

(ii) Transition. A banking entity that does not elect under paragraph (b)(2)(ii) of this section to be subject to the trading account definition in (b)(1)(ii) may continue to apply the trading account definition in paragraph (b)(1)(i) of this section for one year from the date on which it becomes, or becomes a consolidated affiliate for regulatory reporting purposes with, a banking entity that calculates risk-based capital ratios under the market risk capital rule.

(~~2~~4) *Rebuttable presumption for certain purchases and sales.* The purchase (or sale) of a financial instrument by a banking entity shall be presumed not to be for the trading account of the banking entity under paragraph (b)(1)(i) of this section if the banking entity holds the financial instrument for ~~fewer than~~ sixty days or longer and does not transfer substantially ~~transfers~~ all of the risk of the financial instrument within sixty days of the purchase (or sale)~~, unless the banking entity can demonstrate, based on all relevant facts and circumstances, that the banking entity did not purchase (or sell) the financial instrument principally for any of the purposes described in paragraph (b)(1)(i) of this section~~.

(c) *Financial instrument.* (1) *Financial instrument* means:

(i) A security, including an option on a security;

(ii) A derivative, including an option on a derivative; or

(iii) A contract of sale of a commodity for future delivery, or option on a contract of sale of a commodity for future delivery.

(2) A financial instrument does not include:

(i) A loan;

(ii) A commodity that is not:

(A) An excluded commodity (other than foreign exchange or currency);

(B) A derivative;

(C) A contract of sale of a commodity for future delivery; or

(D) An option on a contract of sale of a commodity for future delivery; or

(iii) Foreign exchange or currency.

(d) *Proprietary trading.* Proprietary trading does not include:

(1) Any purchase or sale of one or more financial instruments by a banking entity that arises under a repurchase or reverse repurchase agreement pursuant to which the banking entity has simultaneously agreed, in writing, to both purchase and sell a stated asset, at stated prices, and on stated dates or on demand with the same counterparty;

(2) Any purchase or sale of one or more financial instruments by a banking entity that arises under a transaction in which the banking entity lends or borrows a security temporarily to or from another party pursuant to a written securities lending agreement under which the lender retains the

economic interests of an owner of such security, and has the right to terminate the transaction and to recall the loaned security on terms agreed by the parties;

(3) Any purchase or sale of a security, foreign exchange forward (as that term is defined in section 1a(24) of the Commodity Exchange Act (7 U.S.C. 1a(24)), foreign exchange swap (as that term is defined in section 1a(25) of the Commodity Exchange Act (7 U.S.C. 1a(25)), or cross-currency swap by a banking entity for the purpose of liquidity management in accordance with a documented liquidity management plan of the banking entity that:

(i) Specifically contemplates and authorizes the particular ~~securities to be used for liquidity management purposes, the amount, types, and risks of these securities that~~ financial instruments to be used for liquidity management purposes, the amount, types, and risks of these financial instruments that are consistent with liquidity management, and the liquidity circumstances in which the particular ~~securities~~ financial instruments may or must be used;

(ii) Requires that any purchase or sale of ~~securities~~ financial instruments contemplated and authorized by the plan be principally for the purpose of managing the liquidity of the banking entity, and not for the purpose of short-term resale, benefitting from actual or expected short-term price movements, realizing short-term arbitrage profits, or hedging a position taken for such short-term purposes;

(iii) Requires that any ~~securities~~ financial instruments purchased or sold for liquidity management purposes be highly liquid and limited to ~~securities~~ financial instruments the market, credit, and other risks of which the banking entity does not reasonably expect to give rise to appreciable profits or losses as a result of short-term price movements;

(iv) Limits any ~~securities~~ financial instruments purchased or sold for liquidity management purposes, together with any other financial instruments purchased or sold for such purposes, to an amount that is consistent with the banking entity's near-term funding needs, including deviations from normal operations of the banking entity or any affiliate thereof, as estimated and documented pursuant to methods specified in the plan;

(v) Includes written policies and procedures, internal controls, analysis, and independent testing to ensure that the purchase and sale of ~~securities~~ financial instruments that are not permitted under §§~~248~~___.6(a) or (b) of this subpart are for the purpose of liquidity management and in accordance with the liquidity management plan described in paragraph (d)(3) of this section; and

(vi) Is consistent with ~~The Board's~~ [Agency]'s [supervisory/regulatory] requirements~~, guidance, and expectations~~ regarding liquidity management;

(4) Any purchase or sale of one or more financial instruments by a banking entity that is a derivatives clearing organization or a clearing agency in connection with clearing financial instruments;

(5) Any excluded clearing activities by a banking entity that is a member of a clearing agency, a member of a derivatives clearing organization, or a member of a designated financial market utility;

(6) Any purchase or sale of one or more financial instruments by a banking entity, so long as:

(i) The purchase (or sale) satisfies an existing delivery obligation of the banking entity or its customers, including to prevent or close out a failure to deliver, in connection with delivery, clearing, or settlement activity; or

(ii) The purchase (or sale) satisfies an obligation of the banking entity in connection with a judicial, administrative, self-regulatory organization, or arbitration proceeding;

(7) Any purchase or sale of one or more financial instruments by a banking entity that is acting solely as agent, broker, or custodian;

(8) Any purchase or sale of one or more financial instruments by a banking entity through a deferred compensation, stock-bonus, profit-sharing, or pension plan of the banking entity that is established and administered in accordance with the law of the United States or a foreign sovereign, if the purchase or sale is made directly or indirectly by the banking entity as trustee for the benefit of persons who are or were employees of the banking entity; or

(9) Any purchase or sale of one or more financial instruments by a banking entity in the ordinary course of collecting a debt previously contracted in good faith, provided that the banking entity divests the financial instrument as soon as practicable, and in no event may the banking entity retain such instrument for longer than such period permitted by the Board.

(10) Any purchase or sale of one or more financial instruments that was made in error by a banking entity in the course of conducting a permitted or excluded activity or is a subsequent transaction to correct such an error;

(11) Contemporaneously entering into a customer-driven swap or customer-driven security-based swap and a matched swap or security-based swap if:

(i) The banking entity retains no more than minimal price risk; and

(ii) The banking entity is not a registered dealer, swap dealer, or security-based swap dealer;

(12) Any purchase or sale of one or more financial instruments that the banking entity uses to hedge mortgage servicing rights or mortgage servicing assets in accordance with a documented hedging strategy;

(13) Any purchase or sale of a financial instrument that does not meet the definition of trading asset or trading liability under the applicable reporting form for a banking entity as of January 1, 2020.

(e) *Definition of other terms related to proprietary trading.* For purposes of this subpart:

(1) *Anonymous* means that each party to a purchase or sale is unaware of the identity of the other party(ies) to the purchase or sale.

(2) *Clearing agency* has the same meaning as in section 3(a)(23) of the Exchange Act (15 U.S.C. 78c(a)(23)).

(3) *Commodity* has the same meaning as in section 1a(9) of the Commodity Exchange Act (7 U.S.C. 1a(9)), except that a commodity does not include any security;

(4) *Contract of sale of a commodity for future delivery* means a contract of sale (as that term is defined in section 1a(13) of the Commodity Exchange Act (7 U.S.C. 1a(13)) for future delivery (as that term is defined in section 1a(27) of the Commodity Exchange Act (7 U.S.C. 1a(27))).

(5) *Cross-currency swap* means a swap in which one party exchanges with another party principal and interest rate payments in one currency for principal and interest rate payments in another currency, and the exchange of principal occurs on the date the swap is entered into, with a reversal of the exchange of principal at a later date that is agreed upon when the swap is entered into.

(~~5~~6) *Derivatives clearing organization* means:

(i) A derivatives clearing organization registered under section 5b of the Commodity Exchange Act (7 U.S.C. 7a-1);

(ii) A derivatives clearing organization that, pursuant to CFTC regulation, is exempt from the registration requirements under section 5b of the Commodity Exchange Act (7 U.S.C. 7a-1); or

(iii) A foreign derivatives clearing organization that, pursuant to CFTC regulation, is permitted to clear for a foreign board of trade that is registered with the CFTC.

(~~6~~7) *Exchange,* unless the context otherwise requires, means any designated contract market, swap execution facility, or foreign board of trade registered with the CFTC, or, for purposes of securities or security-based swaps, an exchange, as defined under section 3(a)(1) of the Exchange Act (15 U.S.C. 78c(a)(1)), or security-based swap execution facility, as defined under section 3(a)(77) of the Exchange Act (15 U.S.C. 78c(a)(77)).

(~~7~~8) *Excluded clearing activities* means:

(i) With respect to customer transactions cleared on a derivatives clearing organization, a clearing agency, or a designated financial market utility, any purchase or sale necessary to correct trading errors made by or on behalf of a customer provided that such purchase or sale is conducted in accordance with, for transactions cleared on a derivatives clearing organization, the Commodity Exchange Act, CFTC regulations, and the rules or procedures of the derivatives clearing organization, or, for transactions cleared on a clearing agency, the rules or procedures of the clearing agency, or, for transactions cleared on a designated financial market utility that is neither a derivatives clearing organization nor a clearing agency, the rules or procedures of the designated financial market utility;

(ii) Any purchase or sale in connection with and related to the management of a default or threatened imminent default of a customer provided that such purchase or sale is conducted in accordance with, for transactions cleared on a derivatives clearing organization, the Commodity Exchange Act, CFTC regulations, and the rules or procedures of the derivatives clearing organization, or, for transactions cleared on a clearing agency, the rules or procedures of the clearing agency, or, for transactions cleared on a designated financial market utility that is neither a derivatives clearing organization nor a clearing agency, the rules or procedures of the designated financial market utility;

(iii) Any purchase or sale in connection with and related to the management of a default or threatened imminent default of a member of a clearing agency, a member of a derivatives clearing organization, or a member of a designated financial market utility;

(iv) Any purchase or sale in connection with and related to the management of the default or threatened default of a clearing agency, a derivatives clearing organization, or a designated financial market utility; and

(v) Any purchase or sale that is required by the rules or procedures of a clearing agency, a derivatives clearing organization, or a designated financial market utility to mitigate the risk to the clearing agency, derivatives clearing organization, or designated financial market utility that would result from the clearing by a member of security-based swaps that reference the member or an affiliate of the member.

(~~8~~9) *Designated financial market utility* has the same meaning as in section 803(4) of the Dodd-Frank Act (12 U.S.C. 5462(4)).

(~~9~~10) *Issuer* has the same meaning as in section 2(a)(4) of the Securities Act of 1933 (15 U.S.C. 77b(a)(4)).

(~~10~~11) *Market risk capital rule covered position and trading position* means a financial instrument that ~~is both~~ meets the criteria to be a covered position and a trading position, as those terms are respectively defined, without regard to whether the financial instrument is reported as a covered position or trading position on any applicable regulatory reporting forms:

(i) In the case of a banking entity that is a bank holding company, savings and loan holding company, or insured depository institution, under the market risk capital rule that is applicable to the banking entity; and

(ii) In the case of a banking entity that is affiliated with a bank holding company or savings and loan holding company, other than a banking entity to which a market risk capital rule is applicable, under the market risk capital rule that is applicable to the affiliated bank holding company or savings and loan holding company.

(~~11~~12) *Market risk capital rule* means the market risk capital rule that is contained in subpart F of 12 CFR part 3 with respect to a banking entity for which the OCC is the primary financial regulatory agency, 12 CFR part~~s 208 and 225~~217 with respect to a banking entity for which the Board is the primary financial regulatory agency, or 12 CFR part 324 with respect to a banking entity for which the FDIC is the primary financial regulatory agency~~, as applicable~~.

(~~12~~13) *Municipal security* means a security that is a direct obligation of or issued by, or an obligation guaranteed as to principal or interest by, a State or any political subdivision thereof, or any agency or instrumentality of a State or any political subdivision thereof, or any municipal corporate instrumentality of one or more States or political subdivisions thereof.

(~~13~~14) *Trading desk* means ~~the smallest discrete~~ a unit of organization of a banking entity that purchases or sells financial instruments for the trading account of the banking entity or an affiliate thereof that is:~~.~~

(i)(A) Structured by the banking entity to implement a well-defined business strategy;

(B) Organized to ensure appropriate setting, monitoring, and management review of the desk's trading and hedging limits, current and potential future loss exposures, and strategies; and

(C) Characterized by a clearly defined unit that:

(1) Engages in coordinated trading activity with a unified approach to its key elements;

(2) Operates subject to a common and calibrated set of risk metrics, risk levels, and joint trading limits;

(3) Submits compliance reports and other information as a unit for monitoring by management; and

(4) Books its trades together; or

(ii) For a banking entity that calculates risk-based capital ratios under the market risk capital rule, or a consolidated affiliate for regulatory reporting purposes of a banking entity that calculates risk-based capital ratios under the market risk capital rule, established by the banking entity or its affiliate for purposes of market risk capital calculations under the market risk capital rule.

§248.4 Permitted underwriting and market making-related activities.

(a) *Underwriting activities*—(1) *Permitted underwriting activities.* The prohibition contained in §~~248~~___.3(a) does not apply to a banking entity's underwriting activities conducted in accordance with this paragraph (a).

(2) *Requirements.* The underwriting activities of a banking entity are permitted under paragraph (a)(1) of this section only if:

(i) The banking entity is acting as an underwriter for a distribution of securities and the trading desk's underwriting position is related to such distribution;

(ii) (A) The amount and type of the securities in the trading desk's underwriting position are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties, taking into account the liquidity, maturity, and depth of the market for the relevant types of securities; and (B) reasonable efforts are made to sell or otherwise reduce the underwriting position within a reasonable period, taking into account the liquidity, maturity, and depth of the market for the relevant types of securit~~y~~ies;

(iii) In ~~T~~the case of a banking entity with significant trading assets and liabilities, the banking entity has established and implements, maintains, and enforces an internal compliance program required by subpart D of this part that is reasonably designed to ensure the banking entity's compliance with the requirements of paragraph (a) of this section, including reasonably designed written policies and procedures, internal controls, analysis and independent testing identifying and addressing:

(A) The products, instruments or exposures each trading desk may purchase, sell, or manage as part of its underwriting activities;

(B) Limits for each trading desk, ~~based on the nature and amount of the trading desk's underwriting activities, including the reasonably expected near term demands of clients, customers, or counterparties, on the:~~in accordance with paragraph (a)(2)(ii)(A) of this section;

~~(1) Amount, types, and risk of its underwriting position;~~

~~(2) Level of exposures to relevant risk factors arising from its underwriting position; and~~

~~(3) Period of time a security may be held;~~

~~(C) Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits; and~~

(~~D~~C) Written ~~A~~authorization procedures, including escalation procedures that require review and approval of any trade that would exceed a trading desk's limit(s), demonstrable analysis of the basis for any temporary or permanent increase to a trading desk's limit(s), and independent review of such demonstrable analysis and approval; and

(D) Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits. A banking entity with significant trading assets and liabilities may satisfy the requirements in (B) and (C) by complying with the requirements set forth below in paragraph (c) of this section;

(iv) The compensation arrangements of persons performing the activities described in this paragraph (a) are designed not to reward or incentivize prohibited proprietary trading; and

(v) The banking entity is licensed or registered to engage in the activity described in this paragraph (a) in accordance with applicable law.

(3) *Definition of distribution.* For purposes of this paragraph (a), a *distribution* of securities means:

(i) An offering of securities, whether or not subject to registration under the Securities Act of 1933, that is distinguished from ordinary trading transactions by the presence of special selling efforts and selling methods; or

(ii) An offering of securities made pursuant to an effective registration statement under the Securities Act of 1933.

(4) *Definition of underwriter.* For purposes of this paragraph (a), *underwriter* means:

(i) A person who has agreed with an issuer or selling security holder to:

(A) Purchase securities from the issuer or selling security holder for distribution;

(B) Engage in a distribution of securities for or on behalf of the issuer or selling security holder; or

(C) Manage a distribution of securities for or on behalf of the issuer or selling security holder; or

(ii) A person who has agreed to participate or is participating in a distribution of such securities for or on behalf of the issuer or selling security holder.

(5) *Definition of selling security holder.* For purposes of this paragraph (a), *selling security holder* means any person, other than an issuer, on whose behalf a distribution is made.

(6) *Definition of underwriting position.* For purposes of this ~~paragraph (a)~~section, *underwriting position* means the long or short positions in one or more securities held by a banking entity or its

affiliate, and managed by a particular trading desk, in connection with a particular distribution of securities for which such banking entity or affiliate is acting as an underwriter.

(7) *Definition of client, customer, and counterparty.* For purposes of this paragraph (a), the terms *client, customer, and counterparty,* on a collective or individual basis, refer to market participants that may transact with the banking entity in connection with a particular distribution for which the banking entity is acting as underwriter.

(b) *Market making-related activities*—(1) *Permitted market making-related activities.* The prohibition contained in §~~248~~ ___.3(a) does not apply to a banking entity's market making-related activities conducted in accordance with this paragraph (b).

(2) *Requirements.* The market making-related activities of a banking entity are permitted under paragraph (b)(1) of this section only if:

(i) The trading desk that establishes and manages the financial exposure, routinely stands ready to purchase and sell one or more types of financial instruments related to its financial exposure, and is willing and available to quote, purchase and sell, or otherwise enter into long and short positions in those types of financial instruments for its own account, in commercially reasonable amounts and throughout market cycles on a basis appropriate for the liquidity, maturity, and depth of the market for the relevant types of financial instruments;

(ii) The ~~amount, types, and risks of the financial instruments in the~~ trading desk's market-mak~~er~~ing related activities ~~inventory~~ are designed not to exceed, on an ongoing basis, the reasonably expected near term demands of clients, customers, or counterparties, ~~based on:(A)~~ taking into account ~~T~~the liquidity, maturity, and depth of the market for the relevant types of financial instrument~~(s)~~; ~~and~~

~~(B) Demonstrable analysis of historical customer demand, current inventory of financial instruments, and market and other factors regarding the amount, types, and risks, of or associated with financial instruments in which the trading desk makes a market, including through block trades;~~

(iii) In the case of ~~The~~a banking entity with significant trading assets and liabilities, the banking entity has established and implements, maintains, and enforces an internal compliance program required by subpart D of this part that is reasonably designed to ensure the banking entity's compliance with the requirements of paragraph (b) of this section, including reasonably designed written policies and procedures, internal controls, analysis and independent testing identifying and addressing:

(A) The financial instruments each trading desk stands ready to purchase and sell in accordance with paragraph (b)(2)(i) of this section;

(B) The actions the trading desk will take to demonstrably reduce or otherwise significantly mitigate promptly the risks of its financial exposure consistent with the limits required under paragraph (b)(2)(iii)(C) of this section; the products, instruments, and exposures each trading desk may use for risk management purposes; the techniques and strategies each trading desk may use to manage the risks of its market making-related activities and ~~inventory~~positions; and the process, strategies, and personnel responsible for ensuring that the actions taken by the trading desk to mitigate these risks are and continue to be effective;

(C) Limits for each trading desk, ~~based on the nature and amount of the trading desk's market making-related activities, that address the factors prescribed by~~ in accordance with paragraph (b)(2)(ii) of this section~~, on:~~;

~~*(1)* The amount, types, and risks of its market-maker inventory;~~

~~*(2)* The amount, types, and risks of the products, instruments, and exposures the trading desk may use for risk management purposes;~~

~~*(3)* The level of exposures to relevant risk factors arising from its financial exposure; and~~

~~*(4)* The period of time a financial instrument may be held;~~

~~(D) Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits; and~~

(~~E~~D) Written ~~A~~authorization procedures, including escalation procedures that require review and approval of any trade that would exceed a trading desk's limit(s), demonstrable analysis ~~that~~ of the basis for any temporary or permanent increase to a trading desk's limit(s) ~~is consistent with the requirements of this paragraph (b)~~, and independent review of such demonstrable analysis and approval; and

(E) Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits. A banking entity with significant trading assets and liabilities may satisfy the requirements in (C) and (D) by complying with the requirements set forth below in paragraph (c) of this section;

~~(iv) To the extent that any limit identified pursuant to paragraph (b)(2)(iii)(C) of this section is exceeded, the trading desk takes action to bring the trading desk into compliance with the limits as promptly as possible after the limit is exceeded;~~

(iv) The compensation arrangements of persons performing the activities described in this paragraph (b) are designed not to reward or incentivize prohibited proprietary trading; and

(v~~i~~) The banking entity is licensed or registered to engage in activity described in this paragraph (b) in accordance with applicable law.

(3) *Definition of client, customer, and counterparty.* For purposes of paragraph (b) of this section, the terms *client, customer, and counterparty,* on a collective or individual basis refer to market participants that make use of the banking entity's market making-related services by obtaining such services, responding to quotations, or entering into a continuing relationship with respect to such services, provided that:

(i) A trading desk or other organizational unit of another banking entity is not a client, customer, or counterparty of the trading desk if that other entity has trading assets and liabilities of $50 billion or more as measured in accordance with ~~§248.20(d)(1) of subpart D~~the methodology described in § ___.2(ee) of this part, unless:

(A) The trading desk documents how and why a particular trading desk or other organizational unit of the entity should be treated as a client, customer, or counterparty of the trading desk for purposes of paragraph (b)(2) of this section; or

(B) The purchase or sale by the trading desk is conducted anonymously on an exchange or similar trading facility that permits trading on behalf of a broad range of market participants.

(4) *Definition of financial exposure.* For purposes of this ~~paragraph (b)~~section, *financial exposure* means the aggregate risks of one or more financial instruments and any associated loans, commodities, or foreign exchange or currency, held by a banking entity or its affiliate and managed by a particular trading desk as part of the trading desk's market making-related activities.

(5) *Definition of market-maker ~~inventory~~positions.* For the purposes of this ~~paragraph (b)~~section, *market-maker ~~inventory~~ positions* means all of the positions in the financial instruments for which the trading desk stands ready to make a market in accordance with paragraph (b)(2)(i) of this section, that are managed by the trading desk, including the trading desk's open positions or exposures arising from open transactions.

(c) *Rebuttable presumption of compliance.*

(1) *Internal Limits.*

(i) A banking entity shall be presumed to meet the requirement in paragraph (a)(2)(ii)(A) or (b)(2)(ii) of this section with respect to the purchase or sale of a financial instrument if the banking entity has established and implements, maintains, and enforces the internal limits for the relevant trading desk as described in paragraph (c)(1)(ii) of this section. (ii)(A) With respect to underwriting activities conducted pursuant to paragraph (a) of this section, the presumption described in paragraph (c)(1)(i) of this section shall be available to each trading desk that establishes, implements, maintains, and enforces internal limits that are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties, based on the nature and amount of the trading desk's underwriting activities, on the:

(1) Amount, types, and risk of its underwriting position;

(2) Level of exposures to relevant risk factors arising from its underwriting position; and

(3) Period of time a security may be held.

Such internal limits should take into account the liquidity, maturity, and depth of the market for the relevant types of securities.

(B) With respect to market making-related activities conducted pursuant to paragraph (b) of this section, the presumption described in paragraph (c)(1)(i) of this section shall be available to each trading desk that establishes, implements, maintains, and enforces internal limits that are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties, based on the nature and amount of the trading desk's market-making related activities, that address the:

(1) Amount, types, and risks of its market-maker positions;

(2) Amount, types, and risks of the products, instruments, and exposures the trading desk may use for risk management purposes;

(3) Level of exposures to relevant risk factors arising from its financial exposure; and

(4) Period of time a financial instrument may be held.

Such internal limits should take into account the liquidity, maturity, and depth of the market for the relevant types of financial instruments.

(2) *Supervisory review and oversight.* The limits described in paragraph (c)(1) of this section shall be subject to supervisory review and oversight by the [Agency] on an ongoing basis.

(3) *Limit Breaches and Increases.* (i) With respect to any limit set pursuant to paragraphs (c)(1)(ii)(A) or (c)(1)(ii)(B) of this section, a banking entity shall maintain and make available to the [Agency] upon request records regarding (1) any limit that is exceeded and (2) any temporary or permanent increase to any limit(s), in each case in the form and manner as directed by the [Agency].

(ii) In the event of a breach or increase of any limit set pursuant to paragraphs (c)(1)(ii)(A) or (c)(1)(ii)(B) of this section, the presumption described in paragraph (c)(1)(i) of this section shall continue to be available only if the banking entity:

(1) Takes action as promptly as possible after a breach to bring the trading desk into compliance; and

(2) Follows established written authorization procedures, including escalation procedures that require review and approval of any trade that exceeds a trading desk's limit(s), demonstrable analysis of the basis for any temporary or permanent increase to a trading desk's limit(s), and independent review of such demonstrable analysis and approval.

(4) *Rebutting the presumption.* The presumption in paragraph (c)(1)(i) of this section may be rebutted by the [Agency] if the [Agency] determines, taking into account the liquidity, maturity, and depth of the market for the relevant types of financial instruments and based on all relevant facts and circumstances, that a trading desk is engaging in activity that is not based on the reasonably expected near term demands of clients, customers, or counterparties. The [Agency]'s rebuttal of the presumption in paragraph (c)(1)(i) must be made in accordance with the notice and response procedures in Subpart D.

§248.5 Permitted risk-mitigating hedging activities.

(a) *Permitted risk-mitigating hedging activities.* The prohibition contained in §248.3(a) does not apply to the risk-mitigating hedging activities of a banking entity in connection with and related to individual or aggregated positions, contracts, or other holdings of the banking entity and designed to reduce the specific risks to the banking entity in connection with and related to such positions, contracts, or other holdings.

(b) *Requirements.*

(1) The risk-mitigating hedging activities of a banking entity that has significant trading assets and liabilities are permitted under paragraph (a) of this section only if:

(~~1~~i) The banking entity has established and implements, maintains and enforces an internal compliance program required by subpart D of this part that is reasonably designed to ensure the banking entity's compliance with the requirements of this section, including:

(~~i~~A) Reasonably designed written policies and procedures regarding the positions, techniques and strategies that may be used for hedging, including documentation indicating what positions, contracts or other holdings a particular trading desk may use in its risk-mitigating hedging activities, as well as position and aging limits with respect to such positions, contracts or other holdings;

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

(~~iii~~C) The conduct of analysis~~, including correlation analysis,~~ and independent testing designed to ensure that the positions, techniques and strategies that may be used for hedging may reasonably be expected to ~~demonstrably~~ reduce or otherwise significantly mitigate the specific, identifiable risk(s) being hedged~~, and such correlation analysis demonstrates that the hedging activity demonstrably reduces or otherwise significantly mitigates the specific, identifiable risk(s) being hedged~~;

(~~2~~ii) The risk-mitigating hedging activity:

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

(~~ii~~B) At the inception of the hedging activity, including, without limitation, any adjustments to the hedging activity, is designed to reduce or otherwise significantly mitigate ~~and demonstrably reduces or otherwise significantly mitigates~~ one or more specific, identifiable risks, including market risk, counterparty or other credit risk, currency or foreign exchange risk, interest rate risk, commodity price risk, basis risk, or similar risks, arising in connection with and related to identified positions, contracts, or other holdings of the banking entity, based upon the facts and circumstances of the identified underlying and hedging positions, contracts or other holdings and the risks and liquidity thereof;

(~~iii~~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;

(~~iv~~D) Is subject to continuing review, monitoring and management by the banking entity that:

(~~A~~1) Is consistent with the written hedging policies and procedures required under paragraph (b)(1)(i) of this section;

(~~B~~2) Is designed to reduce or otherwise significantly mitigate ~~and demonstrably reduces or otherwise significantly mitigates~~ the specific, identifiable risks that develop over time from the risk-mitigating hedging activities undertaken under this section and the underlying positions, contracts, and other holdings of the banking entity, based upon the facts and circumstances of the underlying and hedging positions, contracts and other holdings of the banking entity and the risks and liquidity thereof; and

(~~C~~3) Requires ongoing recalibration of the hedging activity by the banking entity to ensure that the hedging activity satisfies the requirements set out in paragraph (b)(~~2~~1)(ii) of this section and is not prohibited proprietary trading; and

(~~3~~iii) The compensation arrangements of persons performing risk-mitigating hedging activities are designed not to reward or incentivize prohibited proprietary trading.

(2) The risk-mitigating hedging activities of a banking entity that does not have significant trading assets and liabilities are permitted under paragraph (a) of this section only if the risk-mitigating hedging activity:

(i) At the inception of the hedging activity, including, without limitation, any adjustments to the hedging activity, is designed to reduce or otherwise significantly mitigate one or more specific, identifiable risks, including market risk, counterparty or other credit risk, currency or foreign exchange risk, interest rate risk, commodity price risk, basis risk, or similar risks, arising in connection with and related to identified positions, contracts, or other holdings of the banking entity, based upon the facts and circumstances of the identified underlying and hedging positions, contracts or other holdings and the risks and liquidity thereof; and

(ii) Is subject, as appropriate, to ongoing recalibration by the banking entity to ensure that the hedging activity satisfies the requirements set out in paragraph (b)(2) of this section and is not prohibited proprietary trading.

(c) *Documentation requirement.* (1) A banking entity that has significant trading assets and liabilities must comply with the requirements of paragraphs (c)(2) and (3) of this section, unless the requirements of paragraph (c)(4) of this section are met, with respect to any purchase or sale of financial instruments made in reliance on this section for risk-mitigating hedging purposes that is:

(i) Not established by the specific trading desk establishing or responsible for the underlying positions, contracts, or other holdings the risks of which the hedging activity is designed to reduce;

(ii) Established by the specific trading desk establishing or responsible for the underlying positions, contracts, or other holdings the risks of which the purchases or sales are designed to reduce, but that is effected through a financial instrument, exposure, technique, or strategy that is not specifically identified in the trading desk's written policies and procedures established under paragraph (b)(1) of this section or under §248.4(b)(2)(iii)(B) of this subpart as a product, instrument, exposure, technique, or strategy such trading desk may use for hedging; or

(iii) Established to hedge aggregated positions across two or more trading desks.

(2) In connection with any purchase or sale identified in paragraph (c)(1) of this section, a banking entity must, at a minimum, and contemporaneously with the purchase or sale, document:

(i) The specific, identifiable risk(s) of the identified positions, contracts, or other holdings of the banking entity that the purchase or sale is designed to reduce;

(ii) The specific risk-mitigating strategy that the purchase or sale is designed to fulfill; and

(iii) The trading desk or other business unit that is establishing and responsible for the hedge.

(3) A banking entity must create and retain records sufficient to demonstrate compliance with the requirements of this paragraph (c) for a period that is no less than five years in a form that allows the banking entity to promptly produce such records to the Board on request, or such longer period as required under other law or this part.

(4) The requirements of paragraphs (c)(2) and (3) of this section do not apply to the purchase or sale of a financial instrument described in paragraph (c)(1) of this section if:

(i) The financial instrument purchased or sold is identified on a written list of pre-approved financial instruments that are commonly used by the trading desk for the specific type of hedging activity for which the financial instrument is being purchased or sold; and

(ii) At the time the financial instrument is purchased or sold, the hedging activity (including the purchase or sale of the financial instrument) complies with written, pre-approved limits for the trading desk purchasing or selling the financial instrument for hedging activities undertaken for one or more other trading desks. The limits shall be appropriate for the:

(A) Size, types, and risks of the hedging activities commonly undertaken by the trading desk;

(B) Financial instruments purchased and sold for hedging activities by the trading desk; and

(C) Levels and duration of the risk exposures being hedged.

§248.6 Other permitted proprietary trading activities.

(a) *Permitted trading in domestic government obligations.* The prohibition contained in §248.3(a) does not apply to the purchase or sale by a banking entity of a financial instrument that is:

(1) An obligation of, or issued or guaranteed by, the United States;

(2) An obligation, participation, or other instrument of, or issued or guaranteed by, an agency of the United States, the Government National Mortgage Association, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, a Federal Home Loan Bank, the Federal Agricultural Mortgage Corporation or a Farm Credit System institution chartered under and subject to the provisions of the Farm Credit Act of 1971 (12 U.S.C. 2001 *et seq.*);

(3) An obligation of any State or any political subdivision thereof, including any municipal security; or

(4) An obligation of the FDIC, or any entity formed by or on behalf of the FDIC for purpose of facilitating the disposal of assets acquired or held by the FDIC 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.

(b) *Permitted trading in foreign government obligations*—(1) *Affiliates of foreign banking entities in the United States.* The prohibition contained in §248.3(a) does not apply to the purchase or sale of a financial instrument that is an obligation of, or issued or guaranteed by, a foreign sovereign (including any multinational central bank of which the foreign sovereign is a member), or any agency or political subdivision of such foreign sovereign, by a banking entity, so long as:

(i) The banking entity is organized under or is directly or indirectly controlled by a banking entity that is organized under the laws of a foreign sovereign and is not directly or indirectly controlled by a top-tier banking entity that is organized under the laws of the United States;

(ii) The financial instrument is an obligation of, or issued or guaranteed by, the foreign sovereign under the laws of which the foreign banking entity referred to in paragraph (b)(1)(i) of this section is organized (including any multinational central bank of which the foreign sovereign is a member), or any agency or political subdivision of that foreign sovereign; and

(iii) The purchase or sale as principal is not made by an insured depository institution.

(2) *Foreign affiliates of a U.S. banking entity.* The prohibition contained in §248.3(a) does not apply to the purchase or sale of a financial instrument that is an obligation of, or issued or guaranteed by, a foreign sovereign (including any multinational central bank of which the foreign sovereign is a member), or any agency or political subdivision of that foreign sovereign, by a foreign entity that is owned or controlled by a banking entity organized or established under the laws of the United States or any State, so long as:

(i) The foreign entity is a foreign bank, as defined in section 211.2(j) of the Board's Regulation K (12 CFR 211.2(j)), or is regulated by the foreign sovereign as a securities dealer;

(ii) The financial instrument is an obligation of, or issued or guaranteed by, the foreign sovereign under the laws of which the foreign entity is organized (including any multinational central bank of which the foreign sovereign is a member), or any agency or political subdivision of that foreign sovereign; and

(iii) The financial instrument is owned by the foreign entity and is not financed by an affiliate that is located in the United States or organized under the laws of the United States or of any State.

(c) *Permitted trading on behalf of customers*—(1) *Fiduciary transactions.* The prohibition contained in §248.3(a) does not apply to the purchase or sale of financial instruments by a banking entity acting as trustee or in a similar fiduciary capacity, so long as:

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

(ii) The banking entity does not have or retain beneficial ownership of the financial instruments.

(2) *Riskless principal transactions.* The prohibition contained in §248.3(a) does not apply to the purchase or sale of financial instruments by a banking entity acting as riskless principal in a transaction in which the banking entity, after receiving an order to purchase (or sell) a financial instrument from a customer, purchases (or sells) the financial instrument for its own account to offset a contemporaneous sale to (or purchase from) the customer.

(d) *Permitted trading by a regulated insurance company.* The prohibition contained in §248.3(a) does not apply to the purchase or sale of financial instruments by a banking entity that is an insurance company or an affiliate of an insurance company if:

(1) The insurance company or its affiliate purchases or sells the financial instruments solely for:

(i) The general account of the insurance company; or

(ii) A separate account established by the insurance company;

(2) The purchase or sale is conducted in compliance with, and subject to, the insurance company investment laws, regulations, and written guidance 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,

regulation, or written guidance described in paragraph (d)(2) of this section is insufficient to protect the safety and soundness of the covered banking entity, or the financial stability of the United States.

(e) *Permitted trading activities of foreign banking entities.* (1) The prohibition contained in §248.3(a) does not apply to the purchase or sale of financial instruments by a banking entity 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 any State;

(ii) The purchase or sale by the banking entity is made pursuant to paragraph (9) or (13) of section 4(c) of the BHC Act; and

(iii) The purchase or sale meets the requirements of paragraph (e)(3) of this section.

(2) A purchase or sale of financial instruments by a banking entity is made pursuant to paragraph (9) or (13) of section 4(c) of the BHC Act for purposes of paragraph (e)(1)(ii) of this section only if:

(i) The purchase or sale is conducted in accordance with the requirements of paragraph (e) 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 any State 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) A purchase or sale by a banking entity is permitted for purposes of this paragraph (e) if:

(i) The banking entity engaging as principal in the purchase or sale (including ~~any~~ relevant personnel ~~of the banking entity or its affiliate that arrange, negotiate or execute such purchase or sale~~) is not 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 purchase or sell as principal is not located in the United States or organized under the laws of the United States or of any State; and

(iii) The purchase or sale, including any transaction arising from risk-mitigating hedging related to the instruments purchased or sold, is not accounted for as principal directly or 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~~;~~.

~~(iv) No financing for the banking entity's purchases or sales is provided, directly or indirectly, 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; and~~

~~(v) The purchase or sale is not conducted with or through any U.S. entity, other than:~~

~~(A) A purchase or sale with the foreign operations of a U.S. entity if no personnel of such U.S. entity that are located in the United States are involved in the arrangement, negotiation, or execution of such purchase or sale;~~

~~(B) A purchase or sale with an unaffiliated market intermediary acting as principal, provided the purchase or sale is promptly cleared and settled through a clearing agency or derivatives clearing organization acting as a central counterparty; or~~

~~(C) A purchase or sale through an unaffiliated market intermediary acting as agent, provided the purchase or sale is conducted anonymously on an exchange or similar trading facility and is promptly cleared and settled through a clearing agency or derivatives clearing organization acting as a central counterparty.~~

~~(4) For purposes of this paragraph (e), a U.S. entity is any entity that is, or is controlled by, or is acting on behalf of, or at the direction of, any other entity that is, located in the United States or organized under the laws of the United States or of any State.~~

(4~~5~~) For purposes of this paragraph (e), a U.S. branch, agency, or subsidiary of a foreign banking entity is considered to be 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.

~~(6) For purposes of this paragraph (e), *unaffiliated market intermediary* means an unaffiliated entity, acting as an intermediary, that is:~~

~~(i) A broker or dealer registered with the SEC under section 15 of the Exchange Act or exempt from registration or excluded from regulation as such;~~

~~(ii) A swap dealer registered with the CFTC under section 4s of the Commodity Exchange Act or exempt from registration or excluded from regulation as such;~~

~~(iii) A security-based swap dealer registered with the SEC under section 15F of the Exchange Act or exempt from registration or excluded from regulation as such; or~~

~~(iv) A futures commission merchant registered with the CFTC under section 4f of the Commodity Exchange Act or exempt from registration or excluded from regulation as such.~~

§248.7 Limitations on permitted proprietary trading activities.

(a) No transaction, class of transactions, or activity may be deemed permissible under §§248.4 through 248.6 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.

§§248.8-248.9 [Reserved]

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;

(B) Is authorized to offer and sell ownership interests to retail investors in the issuer's home jurisdiction; and

(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 of such entities.

(iii) For purposes of paragraph (c)(1)(i)(C) 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;

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

(C) 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 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 ~~supervisory guidance~~ 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 solely of:

(A) Loans as defined in §~~248~~ ___.2(~~s~~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 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.

(ii) *Impermissible assets.* For purposes of this paragraph (c)(8), 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 paragraph (c)(8)(iii) 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 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 derivative directly relate to the loans, the asset-backed securities, or the contractual rights of 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 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

(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.

(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);

(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: *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) 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) 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;

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

(D) 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.

(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) of this subpart 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 §~~248~~___.4(b) of subpart 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~~; or, directly or indirectly, guarantees, assumes, or otherwise insures the obligations or performance of the covered fund or of any covered fund in which such fund invests~~, 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)[; § ___.12(a)(2)(iii),] and §~~248~~ ___.12(d) of this subpart.~~; and~~

~~(3) With respect to any banking entity, the aggregate value of all ownership interests of the banking entity and its affiliates in all covered funds acquired and retained under §248.11 of this subpart, including all covered funds in which the banking entity holds an ownership interest in connection with underwriting and market making related activities permitted under this paragraph (c), are included in the calculation of all ownership interests under §248.12(a)(2)(iii) and §248.12(d) of this subpart.~~

§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 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 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.

(c) *Aggregate permitted investments in all covered funds.* (1) 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.

(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) 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) 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.

(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:

(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) 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) *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;

~~(vii) [Reserved]~~

(viii) Market conditions; and

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

(3) *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) *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) of this subpart does not apply with respect to an ownership interest in a covered fund acquired or retained by a banking entity that is designed to ~~demonstrably~~ reduce or otherwise significantly mitigate the specific, identifiable risks to the banking entity in connection with:

(i) ~~a~~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 ~~required by~~ 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 ~~and demonstrably reduces or otherwise significantly mitigates~~ 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*) ~~i~~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), ~~T~~the compensation arrangement relates solely to the covered fund in which the banking entity or any affiliate has acquired an ownership interest pursuant to ~~this~~ 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 ~~or~~and has not been sold pursuant to an offering that ~~does not~~ 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;

(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; and

~~(iv) No financing for the banking entity's ownership or sponsorship is provided, directly or indirectly, 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~~, and written guidance~~ 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~~, or written guidance~~ 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.

§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~~ [Agency] (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.

(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 transactions.* A prime brokerage transaction permitted under paragraph (a)(2)(ii) 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.

§§248.17-248.19 [Reserved]

Subpart D—Compliance Program Requirement; Violations

§248.20 Program for compliance; reporting.

(a) *Program requirement.* Each banking entity (other than a banking entity with limited trading assets and liabilities) shall develop and provide for the continued administration of a compliance program reasonably designed to ensure and monitor compliance with the prohibitions and restrictions on proprietary trading and covered fund activities and investments set forth in section 13 of the BHC Act and this part. The terms, scope, and detail of the compliance program shall be appropriate for the types, size, scope, and complexity of activities and business structure of the banking entity.

(b) ~~*Contents of compliance program*~~*Banking entities with significant trading assets and liabilities*. ~~Except as provided in paragraph (f) of this section~~With respect to a banking entity with significant trading assets and liabilities, the compliance program required by paragraph (a) of this section, at a minimum, shall include:

(1) Written policies and procedures reasonably designed to document, describe, monitor and limit trading activities subject to subpart B (including those permitted under §§248.3 to 248.6 of subpart B), including setting, monitoring and managing required limits set out in §§248.4 and 248.5, and activities and investments with respect to a covered fund subject to subpart C (including those permitted under §§248.11 through 248.14 of subpart C) conducted by the banking entity to ensure that all activities and investments conducted by the banking entity that are subject to section 13 of the BHC Act and this part comply with section 13 of the BHC Act and this part;

(2) A system of internal controls reasonably designed to monitor compliance with section 13 of the BHC Act and this part and to prevent the occurrence of activities or investments that are prohibited by section 13 of the BHC Act and this part;

(3) A management framework that clearly delineates responsibility and accountability for compliance with section 13 of the BHC Act and this part and includes appropriate management review of trading limits, strategies, hedging activities, investments, incentive compensation and other matters identified in this part or by management as requiring attention;

(4) Independent testing and audit of the effectiveness of the compliance program conducted periodically by qualified personnel of the banking entity or by a qualified outside party;

(5) Training for trading personnel and managers, as well as other appropriate personnel, to effectively implement and enforce the compliance program; and

(6) Records sufficient to demonstrate compliance with section 13 of the BHC Act and this part, which a banking entity must promptly provide to the Board upon request and retain for a period of no less than 5 years or such longer period as required by the Board.

~~(c) *Additional standards.* In addition to the requirements in paragraph (b) of this section, the compliance program of a banking entity must satisfy the requirements and other standards contained in appendix B, if:~~

~~(1) The banking entity engages in proprietary trading permitted under subpart B and is required to comply with the reporting requirements of paragraph (d) of this section;~~

~~(2) The banking entity has reported total consolidated assets as of the previous calendar year end of $50 billion or more or, in the case of a foreign banking entity, has total U.S. assets as of the previous calendar year end of $50 billion or more (including all subsidiaries, affiliates, branches and agencies of the foreign banking entity operating, located or organized in the United States); or~~

~~(3) The Board notifies the banking entity in writing that it must satisfy the requirements and other standards contained in appendix B to this part.~~

(c) *CEO attestation.* The CEO of a banking entity that has significant trading assets and liabilities must, based on a review by the CEO of the banking entity, attest in writing to the [Agency], each year no later than March 31, that the banking entity has in place processes to establish, maintain, enforce, review, test and modify the compliance program required by paragraph (b) of this section in a manner reasonably designed to achieve compliance with section 13 of the BHC Act and this part. In the case of a U.S. branch or agency of a foreign banking entity, the attestation may be provided for the entire U.S. operations of the foreign banking entity by the senior management officer of the U.S. operations of the foreign banking entity who is located in the United States.

(d) *Reporting requirements under the ~~a~~Appendix ~~A~~ to this part.* (1) A banking entity engaged in proprietary trading activity permitted under subpart B shall comply with the reporting requirements described in the ~~a~~Appendix ~~A~~, if:

~~(i) The banking entity (other than a foreign banking entity as provided in paragraph (d)(1)(ii) of this section) has, together with its affiliates and subsidiaries, trading assets and liabilities (excluding trading assets and liabilities involving obligations of or guaranteed by the United States or any agency of the United States) the average gross sum of which (on a worldwide consolidated basis) over the previous consecutive four quarters, as measured as of the last day of each of the four prior calendar quarters, equals or exceeds the threshold established in paragraph (d)(2) of this section;~~

~~(ii) In the case of a foreign banking entity, the average gross sum of the trading assets and liabilities of the combined U.S. operations of the foreign banking entity (including all subsidiaries, affiliates, branches and agencies of the foreign banking entity operating, located or organized in the United States and excluding trading assets and liabilities involving obligations of or guaranteed by the United States or any agency of the United States) over the previous consecutive four quarters, as measured as of the last day of each of the four prior calendar quarters, equals or exceeds the threshold established in paragraph (d)(2) of this section; or~~

(i) The banking entity has significant trading assets and liabilities; or

(~~ii~~iii) The ~~Board~~ [Agency] notifies the banking entity in writing that it must satisfy the reporting requirements contained in the ~~a~~Appendix ~~A~~.

~~(2) The threshold for reporting under paragraph (d)(1) of this section shall be $50 billion beginning on June 30, 2014; $25 billion beginning on April 30, 2016; and $10 billion beginning on December 31, 2016.~~

(~~3~~2) Frequency of reporting: Unless the ~~Board~~ [Agency] notifies the banking entity in writing that it must report on a different basis, a banking entity ~~with $50 billion or more in trading assets and liabilities (as calculated in accordance with paragraph (d)(1) of this section)~~ subject to the Appendix shall report the information required by the ~~a~~Appendix ~~A for each calendar month within 30 days of the end of the relevant calendar month; beginning with information for the month of January 2015, such information shall be reported within 10 days of the end of each calendar month. Any other banking entity subject to appendix A shall report the information required by appendix A~~ for each ~~calendar~~ quarter within 30 days of the end of ~~that calendar~~ the quarter ~~unless the Board notifies the banking entity in writing that it must report on a different basis~~.

(e) *Additional documentation for covered funds.* A~~ny~~ banking entity ~~that has more than $10 billion in total consolidated~~ with significant trading assets and liabilities ~~as reported on December 31 of the previous two calendar years~~ shall maintain records that include:

(1) Documentation of the exclusions or exemptions other than sections 3(c)(1) and 3(c)(7) of the Investment Company Act of 1940 relied on by each fund sponsored by the banking entity (including all subsidiaries and affiliates) in determining that such fund is not a covered fund;

(2) For each fund sponsored by the banking entity (including all subsidiaries and affiliates) for which the banking entity relies on one or more of the exclusions from the definition of covered fund provided by §§248.10(c)(1),248.10(c)(5), 248.10(c)(8), 248.10(c)(9), or 248.10(c)(10) of subpart C, documentation supporting the banking entity's determination that the fund is not a covered fund pursuant to one or more of those exclusions;

(3) For each seeding vehicle described in §248.10(c)(12)(i) or (iii) of subpart C that will become a registered investment company or SEC-regulated business development company, a written plan documenting the banking entity's determination that the seeding vehicle will become a registered investment company or SEC-regulated business development company; the period of time during which the vehicle will operate as a seeding vehicle; and the banking entity's plan to market the vehicle to third-party investors and convert it into a registered investment company or SEC-regulated business development company within the time period specified in §248.12(a)(2)(i)(B) of subpart C;

(4) 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, if the aggregate amount of ownership interests in foreign public funds that are described in §248.10(c)(1) of subpart C owned by such banking entity (including ownership interests owned by any affiliate that 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) exceeds $50 million at the end of two or more consecutive calendar quarters, beginning with the next succeeding calendar quarter, documentation of the value of the ownership interests owned by the banking entity (and such affiliates) in each foreign public fund and each jurisdiction in which any such foreign public fund is organized, calculated as of the end of each calendar quarter, which documentation must continue until the banking entity's aggregate amount of ownership interests in foreign public funds is below $50 million for two consecutive calendar quarters; and

(5) For purposes of paragraph (e)(4) 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.

(f) *Simplified programs for less active banking entities*—(1) *Banking entities with no covered activities.* A banking entity that does not engage in activities or investments pursuant to subpart B or

subpart C (other than trading activities permitted pursuant to §248.6(a) of subpart B) may satisfy the requirements of this section by establishing the required compliance program prior to becoming engaged in such activities or making such investments (other than trading activities permitted pursuant to §248.6(a) of subpart B).

(2) *Banking entities with ~~modest activities~~moderate trading assets and liabilities.* A banking entity with ~~total consolidated assets of $10 billion or less as reported on December 31 of the previous two calendar years that engages in activities or investments pursuant to subpart B or subpart C (other than trading activities permitted under §248.6(a) of subpart B)~~moderate trading assets and liabilities may satisfy the requirements of this section by including in its existing compliance policies and procedures appropriate references to the requirements of section 13 of the BHC Act and this part and adjustments as appropriate given the activities, size, scope, and complexity of the banking entity.

(g) *Rebuttable presumption of compliance for banking entities with limited trading assets and liabilities.*

(1) *Rebuttable presumption.* Except as otherwise provided in this paragraph, a banking entity with limited trading assets and liabilities shall be presumed to be compliant with subpart B and subpart C and shall have no obligation to demonstrate compliance with this part on an ongoing basis.

(2) *Rebuttal of presumption.* If upon examination or audit, the [Agency] determines that the banking entity has engaged in proprietary trading or covered fund activities that are otherwise prohibited under subpart B or subpart C, the [Agency] may require the banking entity to be treated under this part as if it did not have limited trading assets and liabilities. The [Agency]'s rebuttal of the presumption in this paragraph must be made in accordance with the notice and response procedures in paragraph (i) of this Subpart.

(h) *Reservation of authority.* Notwithstanding any other provision of this part, the [Agency] retains its authority to require a banking entity without significant trading assets and liabilities to apply any requirements of this part that would otherwise apply if the banking entity had significant or moderate trading assets and liabilities if the [Agency] determines that the size or complexity of the banking entity's trading or investment activities, or the risk of evasion of subpart B or subpart C, does not warrant a presumption of compliance under paragraph (g) of this section or treatment as a banking entity with moderate trading assets and liabilities, as applicable. The [Agency]'s exercise of this reservation of authority must be made in accordance with the notice and response procedures in paragraph (i) of this Subpart.

(i) Notice and Response Procedures.

(1) Notice. The [Agency] will notify the banking entity in writing of any determination requiring notice under this part and will provide an explanation of the determination.

(2) Response. The banking entity may respond to any or all items in the notice described in paragraph (i)(1) of this section. The response should include any matters that the banking entity would have the [Agency] consider in deciding whether to make the determination. The response must be in writing and delivered to the designated [Agency] official within 30 days after the date on which the banking entity received the notice. The [Agency] may shorten the time period when, in the opinion of the [Agency], the activities or condition of the banking entity so requires, provided that the banking entity is informed of the time period at the time of notice, or with the consent of the banking entity. In its discretion, the [Agency] may extend the time period for good cause.

(3) Failure to respond within 30 days or such other time period as may be specified by the [Agency] shall constitute a waiver of any objections to the [Agency's] determination.

(4) The [Agency] will notify the banking entity of the decision in writing. The notice will include an explanation of the decision.

§248.21 Termination of activities or investments; penalties for violations.

(a) Any banking entity that engages in an activity or makes an investment in violation of section 13 of the BHC Act or this part, or acts in a manner that functions as an evasion of the requirements of section 13 of the BHC Act or this part, including through an abuse of any activity or investment permitted under subparts B or C, or otherwise violates the restrictions and requirements of section 13 of the BHC Act or this part, shall, upon discovery, promptly terminate the activity and, as relevant, dispose of the investment.

(b) Whenever the Board finds reasonable cause to believe any banking entity has engaged in an activity or made an investment in violation of section 13 of the BHC Act or this part, or engaged in any activity or made any investment that functions as an evasion of the requirements of section 13 of the BHC Act or this part, the Board may take any action permitted by law to enforce compliance with section 13 of the BHC Act and this part, including directing the banking entity to restrict, limit, or terminate any or all activities under this part and dispose of any investment.

Appendix ~~A~~ to Part ~~248~~ ___—Reporting and Recordkeeping Requirements for Covered Trading Activities

I. PURPOSE

a. This appendix sets forth reporting and recordkeeping requirements that certain banking entities must satisfy in connection with the restrictions on proprietary trading set forth in subpart B ("proprietary trading restrictions"). Pursuant to §~~248~~ ___.20(d), this appendix ~~generally~~ applies to a banking entity that, together with its affiliates and subsidiaries, has significant trading assets and liabilities. These entities are required to (i) furnish periodic reports to the ~~Board~~ [Agency] regarding a variety of quantitative measurements of their covered trading activities, which vary depending on the scope and size of covered trading activities, and (ii) create and maintain records documenting the preparation and content of these reports. The requirements of this appendix must be incorporated into the banking entity's internal compliance program under §~~248~~ ___.20 ~~and Appendix B~~.

b. The purpose of this appendix is to assist banking entities and the ~~Board~~ [Agency] in:

(~~i~~1) Better understanding and evaluating the scope, type, and profile of the banking entity's covered trading activities;

(~~ii~~2) Monitoring the banking entity's covered trading activities;

(~~iii~~3) Identifying covered trading activities that warrant further review or examination by the banking entity to verify compliance with the proprietary trading restrictions;

(~~iv~~4) Evaluating whether the covered trading activities of trading desks engaged in market making-related activities subject to §~~248~~ ___.4(b) are consistent with the requirements governing permitted market making-related activities;

(~~v~~5) Evaluating whether the covered trading activities of trading desks that are engaged in permitted trading activity subject to ~~§~~§~~248~~___.4, ~~248~~___.5, or ~~248~~___.6(a)-(b) (i.e., underwriting and market making-related ~~related~~ activity, risk-mitigating hedging, or trading in certain government obligations) are consistent with the requirement that such activity not result, directly or indirectly, in a material exposure to high-risk assets or high-risk trading strategies;

(~~vi~~6) Identifying the profile of particular covered trading activities of the banking entity, and the individual trading desks of the banking entity, to help establish the appropriate frequency and scope of examination by ~~the Board~~ [Agency] of such activities; and

(~~vii~~7) Assessing and addressing the risks associated with the banking entity's covered trading activities.

c. ~~The quantitative measurements~~ Information that must be furnished pursuant to this appendix ~~are~~is not intended to serve as a dispositive tool for the identification of permissible or impermissible activities.

~~d. In order to allow banking entities and the Agencies to evaluate the effectiveness of these metrics, banking entities must collect and report these metrics for all trading desks beginning on the dates established in §248.20 of the final rule. The Agencies will review the data collected and revise this collection requirement as appropriate based on a review of the data collected prior to September 30, 2015.~~

~~e~~d. In addition to the quantitative measurements required in this appendix, a banking entity may need to develop and implement other quantitative measurements in order to effectively monitor its covered trading activities for compliance with section 13 of the BHC Act and this part and to have an effective compliance program, as required by §~~248~~___.20 ~~and Appendix B to this part~~. The effectiveness of particular quantitative measurements may differ based on the profile of the banking entity's businesses in general and, more specifically, of the particular trading desk, including types of instruments traded, trading activities and strategies, and history and experience (e.g., whether the trading desk is an established, successful market maker or a new entrant to a competitive market). In all cases, banking entities must ensure that they have robust measures in place to identify and monitor the risks taken in their trading activities, to ensure that the activities are within risk tolerances established by the banking entity, and to monitor and examine for compliance with the proprietary trading restrictions in this part.

~~f~~e. On an ongoing basis, banking entities must carefully monitor, review, and evaluate all furnished quantitative measurements, as well as any others that they choose to utilize in order to maintain compliance with section 13 of the BHC Act and this part. All measurement results that indicate a heightened risk of impermissible proprietary trading, including with respect to otherwise-permitted activities under ~~§~~§~~248~~___.4 through ~~248~~___.6(a) ~~and~~ -(b), or that result in a material exposure to high-risk assets or high-risk trading strategies, must be escalated within the banking entity for review, further analysis, explanation to ~~the Board~~[Agency], and remediation, where appropriate. The quantitative measurements discussed in this appendix should be helpful to banking entities in identifying and managing the risks related to their covered trading activities.

II. DEFINITIONS

The terms used in this appendix have the same meanings as set forth in ~~§~~§~~248~~___.2 and §~~248~~___.3. In addition, for purposes of this appendix, the following definitions apply:

Applicability identifies the trading desks for which a banking entity is required to calculate and report a particular quantitative measurement based on the type of covered trading activity conducted by the trading desk.

Calculation period means the period of time for which a particular quantitative measurement must be calculated.

Comprehensive profit and loss means the net profit or loss of a trading desk's material sources of trading revenue over a specific period of time, including, for example, any increase or decrease in the market value of a trading desk's holdings, dividend income, and interest income and expense.

Covered trading activity means trading conducted by a trading desk under ~~§~~§~~248~~___.4, ~~248~~___.5, ~~248~~___.6(a), or ~~248~~___.6(b). A banking entity may include in its covered trading activity trading conducted under ~~§~~§~~248~~___.3(d), ~~248~~___.6(c), ~~248~~___.6(d) or ~~248~~___.6(e).

Measurement frequency means the frequency with which a particular quantitative metric must be calculated and recorded.

Trading day means a calendar day on which a trading desk is open for trading.

~~*Trading desk* means the smallest discrete unit of organization of a banking entity that purchases or sells financial instruments for the trading account of the banking entity or an affiliate thereof.~~

III. REPORTING AND RECORDKEEPING ~~OF QUANTITATIVE MEASUREMENTS~~

a. Scope of Required Reporting

1. ~~*General scope*~~Quantitative measurements. Each banking entity made subject to this ~~part~~ appendix by §~~248~~___.20 must furnish the following quantitative measurements, as applicable, for each trading desk of the banking entity engaged in covered trading activities and~~,~~ calculate~~d~~ these quantitative measurements in accordance with this appendix:

- i. ~~Risk and Position~~ Internal Limits and Usage;

- ~~Risk Factor Sensitivities;~~

- ii. Value-at-Risk ~~and Stress VaR~~;

- iii. Comprehensive Profit and Loss Attribution;

- ~~Inventory Turnover;~~

- ~~Inventory Aging; and~~

- ~~Customer-Facing Trade Ratio~~

iv. Positions; and

v. Transaction Volumes.

2. Trading desk information. Each banking entity made subject to this appendix by § __.20 must provide certain descriptive information, as further described in this appendix, regarding each trading desk engaged in covered trading activities.

3. Quantitative measurements identifying information. Each banking entity made subject to this appendix by § __.20 must provide certain identifying and descriptive information, as further described in this appendix, regarding its quantitative measurements.

4. Narrative statement. Each A [sic] banking entity made subject to this appendix by § __.20 may provide an optional narrative statement, as further described in this appendix.

5. File identifying information. Each banking entity made subject to this appendix by § __.20 must provide file identifying information in each submission to the [Agency] pursuant to this appendix, including the name of the banking entity, the RSSD ID assigned to the top-tier banking entity by the Board, and identification of the reporting period and creation date and time.

b. *Trading Desk Information*

1. Each banking entity must provide descriptive information regarding each trading desk engaged in covered trading activities, including:

i. Name of the trading desk used internally by the banking entity and a unique identification label for the trading desk;

ii. Identification of each type of covered trading activity in which the trading desk is engaged;

iii. Brief description of the general strategy of the trading desk;

v. [sic] A list identifying each Agency receiving the submission of the trading desk;

2. Indication of whether each calendar date is a trading day or not a trading day for the trading desk; and

3. Currency reported and daily currency conversion rate.

c. *Quantitative Measurements Identifying Information*

Each banking entity must provide the following information regarding the quantitative measurements:

1. An Internal Limits Information Schedule that provides identifying and descriptive information for each limit reported pursuant to the Internal Limits and Usage quantitative measurement, including the name of the limit, a unique identification label for the limit, a description of the limit, the unit of measurement for the limit, the type of limit, and identification of the corresponding risk factor attribution in the particular case that the limit type is a limit on a risk factor sensitivity and profit and loss attribution to the same risk factor is reported; and

2. A Risk Factor Attribution Information Schedule that provides identifying and descriptive information for each risk factor attribution reported pursuant to the Comprehensive Profit and Loss Attribution quantitative measurement, including the name of the risk factor or other factor, a unique

identification label for the risk factor or other factor, a description of the risk factor or other factor, and the risk factor or other factor's change unit.

d. *Narrative Statement*

Each banking entity made subject to this appendix by § ___.20 may submit in a separate electronic document a Narrative Statement to the [Agency] with any information the banking entity views as relevant for assessing the information reported. The Narrative Statement may include further description of or changes to calculation methods, identification of material events, description of and reasons for changes in the banking entity's trading desk structure or trading desk strategies, and when any such changes occurred.

~~b~~e. *Frequency and Method of Required Calculation and Reporting*

A banking entity must calculate any applicable quantitative measurement for each trading day. A banking entity must report the Trading Desk Information, the Quantitative Measurements Identifying Information, and each applicable quantitative measurement electronically to ~~the Board~~ [Agency] on the reporting schedule established in §~~248~~___.20 unless otherwise requested by ~~the Board~~[Agency]. ~~All quantitative measurements for any calendar month must be reported within the time period required by §248.20.~~ A banking entity must report the Trading Desk Information, the Quantitative Measurements Identifying Information, and each applicable quantitative measurement to the [Agency] in accordance with the XML Schema specified and published on the [Agency's] website.

~~c~~f. *Recordkeeping*

A banking entity must, for any quantitative measurement furnished to ~~the Board~~ [Agency] pursuant to this appendix and §~~248~~___.20(d), create and maintain records documenting the preparation and content of these reports, as well as such information as is necessary to permit ~~the Board~~ [Agency] to verify the accuracy of such reports, for a period of ~~5~~five years from the end of the calendar year for which the measurement was taken. A banking entity must retain the Narrative Statement, the Trading Desk Information, and the Quantitative Measurements Identifying Information for a period of five years from the end of the calendar year for which the information was reported to the [Agency].

IV. QUANTITATIVE MEASUREMENTS

a. Risk-Management Measurements

1. ~~Risk and Position~~ Internal Limits and Usage

i. *Description:* For purposes of this appendix, ~~Risk and Position~~ Internal Limits are the constraints that define the amount of risk and the positions that a trading desk is permitted to take at a point in time, as defined by the banking entity for a specific trading desk. Usage represents the ~~portion~~ value of the trading desk's ~~limits~~ risk or positions that are accounted for by the current activity of the desk. ~~Risk and position~~ Internal limits and their usage are key compliance and risk management tools used to control and monitor risk taking and include, but are not limited~~,~~ to, the limits set out in §~~248~~___.4 and §~~248~~___.5. A ~~number of the metrics that are described below, including "Risk Factor Sensitivities" and "Value-at-Risk and Stress Value-at-Risk," relate to a~~ trading desk's risk ~~and position~~ limits ~~and~~, commonly including a limit on "Value-at-Risk," are useful in ~~evaluating and setting these limits in~~ the broader context of the trading desk's overall activities, particularly for the market making activities under §~~248~~___.4(b) and hedging activity under

§248___.5. Accordingly, the limits required under §248___.4(b)(2)(iii)(C) and §248___.5(b)(1)(i)(A) must meet the applicable requirements under §248___.4(b)(2)(iii)(C) and §248___.5(b)(1)(i)(A) and also must include appropriate metrics for the trading desk limits including, at a minimum, the "Risk Factor Sensitivities" and "Value-at-Risk and Stress Value-at-Risk" metrics except to the extent any of the "Risk Factor Sensitivities" or "Value-at-Risk and Stress Value-at-Risk" metrics areis demonstrably ineffective for measuring and monitoring the risks of a trading desk based on the types of positions traded by, and risk exposures of, that desk.

ii. *General Calculation Guidance:* Risk and Position Limits must be reported in the format used by the banking entity for the purposes of risk management of each trading desk. Risk and Position Limits are often expressed in terms of risk measures, such as VaR and Risk Factor Sensitivities, but may also be expressed in terms of other observable criteria, such as net open positions. When criteria other than VaR or Risk Factor Sensitivities are used to define the Risk and Position Limits, both the value of the Risk and Position Limits and the value of the variables used to assess whether these limits have been reached must be reported.

A. A banking entity must provide the following information for each limit reported pursuant to this quantitative measurement: the unique identification label for the limit reported in the Internal Limits Information Schedule, the limit size (distinguishing between an upper and a lower limit), and the value of usage of the limit.

iii. *Calculation Period:* One trading day.

iiiv. *Measurement Frequency:* Daily.

iv. *Applicability*: All trading desks engaged in covered trading activities.

2. Risk Factor Sensitivities

i. *Description:* For purposes of this appendix, Risk Factor Sensitivities are changes in a trading desk's Comprehensive Profit and Loss that are expected to occur in the event of a change in one or more underlying variables that are significant sources of the trading desk's profitability and risk.

ii. *General Calculation Guidance:* A banking entity must report the Risk Factor Sensitivities that are monitored and managed as part of the trading desk's overall risk management policy. The underlying data and methods used to compute a trading desk's Risk Factor Sensitivities will depend on the specific function of the trading desk and the internal risk management models employed. The number and type of Risk Factor Sensitivities that are monitored and managed by a trading desk, and furnished to the Board, will depend on the explicit risks assumed by the trading desk. In general, however, reported Risk Factor Sensitivities must be sufficiently granular to account for a preponderance of the expected price variation in the trading desk's holdings.

A. Trading desks must take into account any relevant factors in calculating Risk Factor Sensitivities, including, for example, the following with respect to particular asset classes:

• *Commodity derivative positions:* risk factors with respect to the related commodities set out in 17 CFR 20.2, the maturity of the positions, volatility and/or correlation sensitivities (expressed in a manner that demonstrates any significant non-linearities), and the maturity profile of the positions;

• *Credit positions:* risk factors with respect to credit spreads that are sufficiently granular to account for specific credit sectors and market segments, the maturity profile of the positions, and risk factors with respect to interest rates of all relevant maturities;

• *Credit-related derivative positions:* risk factor sensitivities, for example credit spreads, shifts (parallel and non-parallel) in credit spreads—volatility, and/or correlation sensitivities (expressed in a manner that demonstrates any significant non-linearities), and the maturity profile of the positions;

• *Equity derivative positions:* risk factor sensitivities such as equity positions, volatility, and/or correlation sensitivities (expressed in a manner that demonstrates any significant non-linearities), and the maturity profile of the positions;

• *Equity positions:* risk factors for equity prices and risk factors that differentiate between important equity market sectors and segments, such as a small capitalization equities and international equities;

• *Foreign exchange derivative positions:* risk factors with respect to major currency pairs and maturities, exposure to interest rates at relevant maturities, volatility, and/or correlation sensitivities (expressed in a manner that demonstrates any significant non-linearities), as well as the maturity profile of the positions; and

• *Interest rate positions, including interest rate derivative positions:* risk factors with respect to major interest rate categories and maturities and volatility and/or correlation sensitivities (expressed in a manner that demonstrates any significant non-linearities), and shifts (parallel and non-parallel) in the interest rate curve, as well as the maturity profile of the positions.

B. The methods used by a banking entity to calculate sensitivities to a common factor shared by multiple trading desks, such as an equity price factor, must be applied consistently across its trading desks so that the sensitivities can be compared from one trading desk to another.

iii. *Calculation Period:* One trading day.

iv. *Measurement Frequency:* Daily.

32. Value-at-Risk and Stress Value-at-Risk

i. *Description:* For purposes of this appendix, Value-at-Risk ("VaR") is the commonly used percentile measurement of the risk of future financial loss in the value of a given set of trading desk's aggregated positions at the ninety-nine percent confidence level over a specified one-day period of time, based on current market conditions. For purposes of this appendix, Stress Value-at-Risk ("Stress VaR") is the percentile measurement of the risk of future financial loss in the value of a given set of aggregated positions over a specified period of time, based on market conditions during a period of significant financial stress.

ii. *General Calculation Guidance:* Banking entities must compute and report VaR and Stress VaR by employing generally accepted standards and methods of calculation. VaR should reflect a loss in a trading desk that is expected to be exceeded less than one percent of the time over a one-day period. For those banking entities that are subject to regulatory capital requirements imposed by a Federal banking agency, VaR and Stress VaR must be computed and reported in a manner that is consistent with such regulatory capital requirements. In cases where a trading desk does not have a standalone VaR or Stress VaR calculation but is part of a larger aggregation of positions for which a

~~VaR or Stress VaR calculation is performed, a VaR or Stress VaR calculation that includes only the trading desk's holdings must be performed consistent with the VaR or Stress VaR model and methodology used for the larger aggregation of positions.~~

ii~~i~~. *Calculation Period:* One trading day.

iii~~v~~. *Measurement Frequency:* Daily.

iv. *Applicability*: All trading desks engaged in covered trading activities.

b. Source-of-Revenue Measurements

1. Comprehensive Profit and Loss Attribution

i. *Description:* For purposes of this appendix, Comprehensive Profit and Loss Attribution is an analysis that attributes the daily fluctuation in the value of a trading desk's positions to various sources. First, the daily profit and loss of the aggregated positions is divided into ~~three~~ two categories: (i) profit and loss attributable to a trading desk's existing positions that were also positions held by the trading desk as of the end of the prior day ("existing positions"); and (ii) profit and loss attributable to new positions resulting from the current day's trading activity ("new positions")~~; and (iii) residual profit and loss that cannot be specifically attributed to existing positions or new positions. The sum of (i), (ii), and (iii) must equal the trading desk's comprehensive profit and loss at each point in time. In addition, profit and loss measurements must calculate volatility of comprehensive profit and loss (i.e., the standard deviation of the trading desk's one-day profit and loss, in dollar terms) for the reporting period for at least a 30-, 60- and 90-day lag period, from the end of the reporting period, and any other period that the banking entity deems necessary to meet the requirements of the rule~~.

A. The comprehensive profit and loss associated with existing positions must reflect changes in the value of these positions on the applicable day. The comprehensive profit and loss from existing positions must be further attributed, as applicable, to (i) changes in ~~(i)~~ the specific ~~R~~risk ~~F~~factors and other factors that are monitored and managed as part of the trading desk's overall risk management policies and procedures; and (ii) any other applicable elements, such as cash flows, carry, changes in reserves, and the correction, cancellation, or exercise of a trade.

B. For the attribution of comprehensive profit and loss from existing positions to specific risk factors and other factors, a banking entity must provide the following information for the factors that explain the preponderance of the profit or loss changes due to risk factor changes: the unique identification label for the risk factor or other factor listed in the Risk Factor Attribution Information Schedule, and the profit or loss due to the risk factor or other factor change.

~~B~~C. The comprehensive profit and loss attributed to new positions must reflect commissions and fee income or expense and market gains or losses associated with transactions executed on the applicable day. New positions include purchases and sales of financial instruments and other assets/liabilities and negotiated amendments to existing positions. The comprehensive profit and loss from new positions may be reported in the aggregate and does not need to be further attributed to specific sources.

~~C~~D. The portion of comprehensive profit and loss from existing positions that ~~cannot be specifically~~ is not attributed to ~~known sources~~ changes in specific risk factors and other factors must be allocated to a residual category~~ identified as an unexplained portion of the comprehensive profit~~

~~and loss~~. Significant unexplained profit and loss must be escalated for further investigation and analysis.

~~ii. *General Calculation Guidance:* The specific categories used by a trading desk in the attribution analysis and amount of detail for the analysis should be tailored to the type and amount of trading activities undertaken by the trading desk. The new position attribution must be computed by calculating the difference between the prices at which instruments were bought and/or sold and the prices at which those instruments are marked to market at the close of business on that day multiplied by the notional or principal amount of each purchase or sale. Any fees, commissions, or other payments received (paid) that are associated with transactions executed on that day must be added (subtracted) from such difference. These factors must be measured consistently over time to facilitate historical comparisons.~~

~~i~~ii. *Calculation Period:* One trading day.

iii~~v~~. *Measurement Frequency:* Daily.

iv. *Applicability*: All trading desks engaged in covered trading activities.

~~*c. Customer-Facing Activity Measurements*~~

~~1. Inventory Turnover~~

~~i. *Description:* For purposes of this appendix, Inventory Turnover is a ratio that measures the turnover of a trading desk's inventory. The numerator of the ratio is the absolute value of all transactions over the reporting period. The denominator of the ratio is the value of the trading desk's inventory at the beginning of the reporting period.~~

~~ii. *General Calculation Guidance:* For purposes of this appendix, for derivatives, other than options and interest rate derivatives, value means gross notional value, for options, value means delta adjusted notional value, and for interest rate derivatives, value means 10-year bond equivalent value.~~

~~iii. *Calculation Period:* 30 days, 60 days, and 90 days.~~

~~iv. *Measurement Frequency:* Daily.~~

~~2. Inventory Aging~~

~~i. *Description:* For purposes of this appendix, Inventory Aging generally describes a schedule of the trading desk's aggregate assets and liabilities and the amount of time that those assets and liabilities have been held. Inventory Aging should measure the age profile of the trading desk's assets and liabilities.~~

~~ii. *General Calculation Guidance:* In general, Inventory Aging must be computed using a trading desk's trading activity data and must identify the value of a trading desk's aggregate assets and liabilities. Inventory Aging must include two schedules, an asset-aging schedule and a liability-aging schedule. Each schedule must record the value of assets or liabilities held over all holding periods. For derivatives, other than options, and interest rate derivatives, value means gross notional value, for options, value means delta adjusted notional value and, for interest rate derivatives, value means 10-year bond equivalent value.~~

~~iii. *Calculation Period:* One trading day.~~

~~iv. *Measurement Frequency:* Daily.~~

~~3. Customer-Facing Trade Ratio—Trade Count Based and Value Based~~

~~i. *Description:* For purposes of this appendix, the Customer-Facing Trade Ratio is a ratio comparing (i) the transactions involving a counterparty that is a customer of the trading desk to (ii) the transactions involving a counterparty that is not a customer of the trading desk. A trade count based ratio must be computed that records the number of transactions involving a counterparty that is a customer of the trading desk and the number of transactions involving a counterparty that is not a customer of the trading desk. A value based ratio must be computed that records the value of transactions involving a counterparty that is a customer of the trading desk and the value of transactions involving a counterparty that is not a customer of the trading desk.~~

~~ii. *General Calculation Guidance:* For purposes of calculating the Customer-Facing Trade Ratio, a counterparty is considered to be a customer of the trading desk if the counterparty is a market participant that makes use of the banking entity's market making-related services by obtaining such services, responding to quotations, or entering into a continuing relationship with respect to such services. However, a trading desk or other organizational unit of another banking entity would not be a client, customer, or counterparty of the trading desk if the other entity has trading assets and liabilities of $50 billion or more as measured in accordance with §248.20(d)(1) unless the trading desk documents how and why a particular trading desk or other organizational unit of the entity should be treated as a client, customer, or counterparty of the trading desk. Transactions conducted anonymously on an exchange or similar trading facility that permits trading on behalf of a broad range of market participants would be considered transactions with customers of the trading desk. For derivatives, other than options, and interest rate derivatives, value means gross notional value, for options, value means delta adjusted notional value, and for interest rate derivatives, value means 10-year bond equivalent value.~~

~~iii. *Calculation Period:* 30 days, 60 days, and 90 days.~~

~~iv. *Measurement Frequency:* Daily.~~

c. *Positions and Transaction Volumes Measurements*

1. Positions

i. *Description:* For purposes of this appendix, Positions is the value of securities and derivatives positions managed by the trading desk. For purposes of the Positions quantitative measurement, do not include in the Positions calculation for "securities" those securities that are also "derivatives," as those terms are defined under subpart A; instead, report those securities that are also derivatives as "derivatives."[2] A banking entity must separately report the trading desk's market value of long securities positions, short securities positions, derivatives receivables, and derivatives payables.

ii. *Calculation Period:* One trading day.

[2] *See* § __.2(h), (aa). For example, under this part, a security-based swap is both a "security" and a "derivative." For purposes of the Positions quantitative measurement, security-based swaps are reported as derivatives rather than securities.

iii. *Measurement Frequency:* Daily.

iv. *Applicability:* All trading desks that rely on § __.4(a) or § __.4(b) to conduct underwriting activity or market-making-related activity, respectively.

2. Transaction Volumes

i. *Description:* For purposes of this appendix, Transaction Volumes measures three exclusive categories of covered trading activity conducted by a trading desk. A banking entity is required to report the value and number of security and derivative transactions conducted by the trading desk with: (i) customers, excluding internal transactions; (ii) non-customers, excluding internal transactions; and (iii) trading desks and other organizational units where the transaction is booked into either the same banking entity or an affiliated banking entity. For securities, value means gross market value. For derivatives, value means gross notional value. For purposes of calculating the Transaction Volumes quantitative measurement, do not include in the Transaction Volumes calculation for "securities" those securities that are also "derivatives," as those terms are defined under subpart A; instead, report those securities that are also derivatives as "derivatives."[3] Further, for purposes of the Transaction Volumes quantitative measurement, a customer of a trading desk that relies on § __.4(a) to conduct underwriting activity is a market participant identified in § __.4(a)(7), and a customer of a trading desk that relies on § __.4(b) to conduct market making-related activity is a market participant identified in § __.4(b)(3).

ii. *Calculation Period:* One trading day.

iii. *Measurement Frequency:* Daily.

iv. *Applicability:* All trading desks that rely on § __.4(a) or § __.4(b) to conduct underwriting activity or market-making-related activity, respectively.

[N.B.: Appendix B to the 2013 Rule is omitted in its entirety.]

[3] *See* § __.2(h), (aa).

APPENDIX B

Volcker Rule Implementing Regulations

(Textual Comparison of the Proposed Rule against the 2019 Rule)[1]

Subpart A—Authority and Definitions

§ 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

[1] **[N.B.: The base text that was used to generate this comparison is drawn from the amendments proposed in the Agencies' July 17, 2018 Notice of Proposed Rulemaking (as applicable to the Federal Reserve's Regulation VV (12 C.F.R. § 248.1)) and includes the amendments adopted on July 9, 2019 implementing Sections 203 and 204 of the Economic Growth, Regulatory Relief, and Consumer Protection Act.]**

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

~~(c)~~(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).

~~(d)~~(c) *Banking entity.* (1) Except as provided in paragraph (~~d~~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 (~~d~~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 paragraphs (~~d~~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 paragraphs (~~d~~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.

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

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

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

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

~~(i)~~(h) *Derivative.* (1) Except as provided in paragraph (~~i~~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, ~~guidance,~~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)).

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

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

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

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

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

~~(o)~~(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.

~~(p)~~(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.

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

~~(r)~~(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).

~~(s)~~(r) *Insured depository institution*~~, unless otherwise indicated,~~ 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.*

(1) ~~(t)~~*Limited trading assets and liabilities* means, with respect to a banking entity, that:

(i) ~~(1)~~The banking entity has, together with its affiliates and subsidiaries ~~on a worldwide consolidated basis~~, trading assets and liabilities (excluding trading assets and liabilities ~~involving obligations of or guaranteed by the United States or any agency of the United~~

~~States~~attributable to trading activities permitted pursuant to § .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~~,000,000,000~~ billion; and

(ii) ~~(2)~~The [Agency] has not determined pursuant to § .20(g) or (h) of this part that the banking entity should not be treated as having limited trading assets and liabilities.

~~(1)~~(2) With respect to a banking entity other than a banking entity described in paragraph (3), 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 § _.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 § _.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.

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

~~(v)~~(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.

~~(w)~~(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)).

~~(x)~~(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.

~~(y)~~(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)).

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

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

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

(dd) ~~(ee)~~*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) ~~(ff)~~*Significant trading assets and liabilities.*

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

(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 $~~1~~20~~,000,000,000~~ billion; or

(ii) The [Agency] has determined pursuant to §__.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 (3) of this section, trading assets and liabilities for purposes of this paragraph (~~ff~~ee) means trading assets and liabilities (excluding trading assets and liabilities ~~involving obligations of or guaranteed by the United States or any agency of the United States~~attributable to trading activities permitted pursuant to § .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 (~~ff~~ee) means the trading assets and liabilities (excluding trading assets and liabilities ~~involving obligations of or guaranteed by~~attributable to trading activities permitted pursuant to § .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~~any~~ agency of the foreign banking entity operating, located or organized in the United States~~) 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 (~~ff~~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) ~~(gg)~~*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) ~~(hh)~~*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) ~~(ii)~~*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) ~~(jj)~~*Swap dealer* has the same meaning as in section 1(a)(49) of the Commodity Exchange Act (7 U.S.C. 1a(49)).

Subpart B—Proprietary Trading

§ 248.3 Prohibition on proprietary trading.

(a) *Prohibition.* Except as otherwise provided in this subpart, a banking entity may not engage in proprietary trading. *Proprietary trading* means engaging as principal for the trading account of the banking entity in any purchase or sale of one or more financial instruments.

(b) *Definition of trading account.* (1) *Trading account* means:

(i) any account that is used by a banking entity to~~:~~ purchase or sell one or more financial instruments 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 the purchases or sales of financial instruments described in this paragraph;

(ii) Any account that is used by a banking entity to purchase or sell one or more financial instruments that are both market risk capital rule covered positions and trading positions (or hedges of other market risk capital rule covered positions), if the banking entity, or any affiliate ~~of~~with which the banking entity~~,~~ is ~~an insured depository institution, bank holding company, or savings and loan holding company, and~~consolidated for regulatory reporting purposes, calculates risk- based capital ratios under the market risk capital rule; or

(iii) Any account that is ~~not, and is not controlled directly or indirectly~~used by a banking entity ~~that is, located in or organized under the laws of the United States or any State,~~to purchase or sell one or more financial instruments, if the banking entity:~~that are subject to capital requirements under a market risk framework established by the home-country supervisor that is consistent with the market risk framework published by the Basel Committee on Banking Supervision, as amended from time to time.~~

~~(2)Purchase or sell one or more financial instruments for any purpose, if the banking entity:~~

(A) ~~(i)~~Is licensed or registered, or is required to be licensed or registered, to engage in the business of a dealer, swap dealer, or security-based swap dealer, to the extent the instrument is purchased or sold in connection with the activities that require the banking entity to be licensed or registered as such; or ~~(ii)~~

(B) Is engaged in the business of a dealer, swap dealer, or security-based swap dealer outside of the United States, to the extent the instrument is purchased or sold in connection with the activities of such business~~; or~~.

(2)(i) A banking entity that is subject to paragraph (b)(1)(ii) in determining the scope of its trading account is not subject to paragraph (b)(1)(i). ~~(3)Purchase or sell one or more financial instruments, with respect to a financial instrument that is recorded at fair value on a recurring basis under applicable accounting standards.~~

~~(c)*Presumption of compliance*.(1)(i) Each trading desk that does not purchase or sell financial instruments for a trading account defined in paragraphs (b)(1) or (b)(2) of this section may calculate the net gain or net loss on the trading desk's portfolio of financial instruments each business day, reflecting realized and unrealized gains and losses since the previous business day, based on the banking entity's fair value for such financial instruments.(ii) If the sum of the absolute values of the daily net gain and loss figures determined in accordance with paragraph (c)(1)(i) of this section for the preceding 90-calendar-day period does not exceed $25 million, the activities of the trading desk shall be presumed to be in compliance with the prohibition in paragraph (a) of this section.~~

(ii) A banking entity that does not calculate risk-based capital ratios under the market risk capital rule and is not a consolidated affiliate for regulatory reporting purposes of a banking entity that calculates risk based capital ratios under the market risk capital rule may elect to apply paragraph (b)(1)(ii) of this section in determining the scope of its trading account as if it were subject to that paragraph. A banking entity that elects under this subsection to

apply paragraph (b)(1)(ii) of this section in determining the scope of its trading account as if it were subject to that paragraph is not required to apply paragraph (b)(1)(i) of this section.

(3) *Consistency of account election for certain banking entities*.

(i) Any election or change to an election under paragraph (b)(2)(ii) of this section must apply to the electing banking entity and all of its wholly owned subsidiaries. The primary financial regulatory agency of a banking entity that is affiliated with but is not a wholly owned subsidiary of such electing banking entity may require that the banking entity be subject to this uniform application requirement if the primary financial regulatory agency determines that it is necessary to prevent evasion of the requirements of this part after notice and opportunity for response as provided in Subpart D.

(ii) Transition. A banking entity that does not elect under paragraph (b)(2)(ii) of this section to be subject to the trading account definition in (b)(1)(ii) may continue to apply the trading account definition in paragraph (b)(1)(i) of this section for one year from the date on which it becomes, or becomes a consolidated affiliate for regulatory reporting purposes with, a banking entity that calculates risk-based capital ratios under the market risk capital rule.

(4) ~~(2)The [Agency] may rebut the~~*Rebuttable* *presumption* *for certain purchases and sales* ~~of compliance in paragraph (c)(1)(ii) of this section by providing written notice to the banking entity that the [Agency] has determined that one or more of the banking entity's activities violates the prohibitions under subpart B.~~

~~(3)If a trading desk operating pursuant to paragraph (c)(1)(ii) of this section exceeds the $25 million threshold in that paragraph at any point, the banking entity shall, in accordance with any policies and procedures adopted by the [Agency]:~~

~~(i)Promptly notify the [Agency];~~
~~(ii)Demonstrate that the trading desk's *purchases and sales*~~. The purchase (or sale) of a financial ~~instruments comply with subpart B; and~~
~~(iii)Demonstrate, with respect to the trading desk, how the banking entity will maintain compliance with subpart B on an ongoing basis.~~instrument by a banking entity shall be presumed not to be for the trading account of the banking entity under paragraph (b)(1)(i) of this section if the banking entity holds the financial instrument for sixty days or longer and does not transfer substantially all of the risk of the financial instrument within sixty days of the purchase (or sale).

~~(d)~~(c) *Financial instrument.*

(1) *Financial instrument* means:

(i) A security, including an option on a security;

(ii) A derivative, including an option on a derivative; or

(iii) A contract of sale of a commodity for future delivery, or option on a contract of sale of a commodity for future delivery.

(2) A financial instrument does not include:

(i) A loan;

(ii) A commodity that is not:

(A) An excluded commodity (other than foreign exchange or currency);

(B) A derivative;

(C) A contract of sale of a commodity for future delivery; or

(D) An option on a contract of sale of a commodity for future delivery; or

(iii) Foreign exchange or currency.

~~(e)~~(d) *Proprietary trading.* Proprietary trading does not include:

(1) Any purchase or sale of one or more financial instruments by a banking entity that arises under a repurchase or reverse repurchase agreement pursuant to which the banking entity has simultaneously agreed, in writing, to both purchase and sell a stated asset, at stated prices, and on stated dates or on demand with the same counterparty;

(2) Any purchase or sale of one or more financial instruments by a banking entity that arises under a transaction in which the banking entity lends or borrows a security temporarily to or from another party pursuant to a written securities lending agreement under which the lender retains the economic interests of an owner of such security, and has the right to terminate the transaction and to recall the loaned security on terms agreed by the parties;

(3) Any purchase or sale of a security, foreign exchange forward (as that term is defined in section 1a(24) of the Commodity Exchange Act (7 U.S.C. 1a(24)), foreign exchange swap (as that term is defined in section 1a(25) of the Commodity Exchange Act (7 U.S.C. 1a(25)), or ~~physically-settled~~cross- currency swap~~,~~ by a banking entity for the purpose of liquidity management in accordance with a documented liquidity management plan of the banking entity that~~, with respect to such financial instruments~~:

(i) Specifically contemplates and authorizes the particular financial instruments to be used for liquidity management purposes, the amount, types, and risks of these financial instruments that are consistent with liquidity management, and the liquidity circumstances in which the particular financial instruments may or must be used;

(ii) Requires that any purchase or sale of financial instruments contemplated and authorized by the plan be principally for the purpose of managing the liquidity of the banking entity, and not for the purpose of short-term resale, benefitting from actual or expected short-term price movements, realizing short-term arbitrage profits, or hedging a position taken for such short-term purposes;

(iii) Requires that any financial instruments purchased or sold for liquidity management purposes be highly liquid and limited to financial instruments the market, credit, and other risks of which the banking entity does not reasonably expect to give rise to appreciable profits or

losses as a result of short-term price movements;

(iv) Limits any financial instruments purchased or sold for liquidity management purposes, together with any other financial instruments purchased or sold for such purposes, to an amount that is consistent with the banking entity's near-term funding needs, including deviations from normal operations of the banking entity or any affiliate thereof, as estimated and documented pursuant to methods specified in the plan;

(v) Includes written policies and procedures, internal controls, analysis, and independent testing to ensure that the purchase and sale of financial instruments that are not permitted under §§ .6(a) or (b) of this subpart are for the purpose of liquidity management and in accordance with the liquidity management plan described in paragraph (ed)(3) of this section; and

(vi) Is consistent with [Agency]'s [supervisory/regulatory] requirements~~, guidance, and expectations~~ regarding liquidity management;

(4) Any purchase or sale of one or more financial instruments by a banking entity that is a derivatives clearing organization or a clearing agency in connection with clearing financial instruments;

(5) Any excluded clearing activities by a banking entity that is a member of a clearing agency, a member of a derivatives clearing organization, or a member of a designated financial market utility;

(6) Any purchase or sale of one or more financial instruments by a banking entity, so long as:

(i) The purchase (or sale) satisfies an existing delivery obligation of the banking entity or its customers, including to prevent or close out a failure to deliver, in connection with delivery, clearing, or settlement activity; or

(ii) The purchase (or sale) satisfies an obligation of the banking entity in connection with a judicial, administrative, self-regulatory organization, or arbitration proceeding;

(7) Any purchase or sale of one or more financial instruments by a banking entity that is acting solely as agent, broker, or custodian;

(8) Any purchase or sale of one or more financial instruments by a banking entity through a deferred compensation, stock-bonus, profit-sharing, or pension plan of the banking entity that is established and administered in accordance with the law of the United States or a foreign sovereign, if the purchase or sale is made directly or indirectly by the banking entity as trustee for the benefit of persons who are or were employees of the banking entity; or

(9) Any purchase or sale of one or more financial instruments by a banking entity in the ordinary course of collecting a debt previously contracted in good faith, provided that the banking entity divests the financial instrument as soon as practicable, and in no event may the banking entity retain such instrument for longer than such period permitted by the Board.

(10) Any purchase ~~(~~or sale~~)~~ of one or more financial instruments that was made in error by a banking entity in the course of conducting a permitted or excluded activity or is a subsequent transaction to correct such an error~~, and the erroneously purchased (or sold) financial instrument is promptly transferred to a separately-managed trade error account for disposition.~~;

(11) Contemporaneously entering into a customer-driven swap or customer-driven security-based swap and a matched swap or security-based swap if:

(i) The banking entity retains no more than minimal price risk; and

(ii) The banking entity is not a registered dealer, swap dealer, or security-based swap dealer;

(12) Any purchase or sale of one or more financial instruments that the banking entity uses to hedge mortgage servicing rights or mortgage servicing assets in accordance with a documented hedging strategy;

(13) Any purchase or sale of a financial instrument that does not meet the definition of trading asset or trading liability under the applicable reporting form for a banking entity as of January 1, 2020.

~~(f)~~(e) *Definition of other terms related to proprietary trading.* For purposes of this subpart:

(1) *Anonymous* means that each party to a purchase or sale is unaware of the identity of the other party(ies) to the purchase or sale.

(2) *Clearing agency* has the same meaning as in section 3(a)(23) of the Exchange Act (15 U.S.C. 78c(a)(23)).

(3) *Commodity* has the same meaning as in section 1a(9) of the Commodity Exchange Act (7 U.S.C. 1a(9)), except that a commodity does not include any security;

(4) *Contract of sale of a commodity for future delivery* means a contract of sale (as that term is defined in section 1a(13) of the Commodity Exchange Act (7 U.S.C. 1a(13)) for future delivery (as that term is defined in section 1a(27) of the Commodity Exchange Act (7 U.S.C. 1a(27))).

(5) *Cross-currency swap* means a swap in which one party exchanges with another party principal and interest rate payments in one currency for principal and interest rate payments in another currency, and the exchange of principal occurs on the date the swap is entered into, with a reversal of the exchange of principal at a later date that is agreed upon when the swap is entered into.

(6) *Derivatives clearing organization* means:

(i) A derivatives clearing organization registered under section 5b of the Commodity Exchange Act (7 U.S.C. 7a-1);

(ii) A derivatives clearing organization that, pursuant to CFTC regulation, is exempt from the registration requirements under section 5b of the Commodity Exchange Act (7 U.S.C. 7a-1); or

(iii) A foreign derivatives clearing organization that, pursuant to CFTC regulation, is permitted to clear for a foreign board of trade that is registered with the CFTC.

(7) *Exchange,* unless the context otherwise requires, means any designated contract market, swap execution facility, or foreign board of trade registered with the CFTC, or, for purposes of securities or security-based swaps, an exchange, as defined under section 3(a)(1) of the Exchange Act (15 U.S.C. 78c(a)(1)), or security-based swap execution facility, as defined under section 3(a)(77) of the Exchange Act (15 U.S.C. 78c(a)(77)).

(8) *Excluded clearing activities* means:

(i) With respect to customer transactions cleared on a derivatives clearing organization, a clearing agency, or a designated financial market utility, any purchase or sale necessary to correct trading errors made by or on behalf of a customer provided that such purchase or sale is conducted in accordance with, for transactions cleared on a derivatives clearing organization, the Commodity Exchange Act, CFTC regulations, and the rules or procedures of the derivatives clearing organization, or, for transactions cleared on a clearing agency, the rules or procedures of the clearing agency, or, for transactions cleared on a designated financial market utility that is neither a derivatives clearing organization nor a clearing agency, the rules or procedures of the designated financial market utility;

(ii) Any purchase or sale in connection with and related to the management of a default or threatened imminent default of a customer provided that such purchase or sale is conducted in accordance with, for transactions cleared on a derivatives clearing organization, the Commodity Exchange Act, CFTC regulations, and the rules or procedures of the derivatives clearing organization, or, for transactions cleared on a clearing agency, the rules or procedures of the clearing agency, or, for transactions cleared on a designated financial market utility that is neither a derivatives clearing organization nor a clearing agency, the rules or procedures of the designated financial market utility;

(iii) Any purchase or sale in connection with and related to the management of a default or threatened imminent default of a member of a clearing agency, a member of a derivatives clearing organization, or a member of a designated financial market utility;

(iv) Any purchase or sale in connection with and related to the management of the default or threatened default of a clearing agency, a derivatives clearing organization, or a designated financial market utility; and

(v) Any purchase or sale that is required by the rules or procedures of a clearing agency, a derivatives clearing organization, or a designated financial market utility to mitigate the risk to the clearing agency, derivatives clearing organization, or designated financial market utility that would result from the clearing by a member of security-based swaps that reference the member or an affiliate of the member.

(9) *Designated financial market utility* has the same meaning as in section 803(4) of the

Dodd- Frank Act (12 U.S.C. 5462(4)).

(10) *Issuer* has the same meaning as in section 2(a)(4) of the Securities Act of 1933 (15 U.S.C. 77b(a)(4)).

(11) *Market risk capital rule covered position and trading position* means a financial instrument that ~~is both~~meets the criteria to be a covered position and a trading position, as those terms are respectively defined, without regard to whether the financial instrument is reported as a covered position or trading position on any applicable regulatory reporting forms:

(i) In the case of a banking entity that is a bank holding company, savings and loan holding company, or insured depository institution, under the market risk capital rule that is applicable to the banking entity; and

(ii) In the case of a banking entity that is affiliated with a bank holding company or savings and loan holding company, other than a banking entity to which a market risk capital rule is applicable, under the market risk capital rule that is applicable to the affiliated bank holding company or savings and loan holding company.

(12) *Market risk capital rule* means the market risk capital rule that is contained in subpart F of 12 CFR part 3 with respect to a banking entity for which the OCC is the primary financial regulatory agency, 12 CFR part~~s~~ 2~~08 and 225, or 12 CFR part 324, as applicable~~17 with respect to a banking entity for which the Board is the primary financial regulatory agency, or 12 CFR part 324 with respect to a banking entity for which the FDIC is the primary financial regulatory agency.

(13) *Municipal security* means a security that is a direct obligation of or issued by, or an obligation guaranteed as to principal or interest by, a State or any political subdivision thereof, or any agency or instrumentality of a State or any political subdivision thereof, or any municipal corporate instrumentality of one or more States or political subdivisions thereof.

(14) *Trading desk* means ~~the smallest discrete~~a unit of organization of a banking entity that purchases or sells financial instruments for the trading account of the banking entity or an affiliate thereof that is~~.~~

~~(g)*Reservation of Authority* that is~~:

(i)(A) Structured by the banking entity to implement a well-defined business strategy;

~~(1)The [Agency] may determine, on a case-by-case basis, that a purchase or sale of one or more financial instruments by a banking entity either is or is not for the trading account as defined at 12 U.S.C. 1851(h)(6).~~

(B) Organized to ensure appropriate setting, monitoring, and management review of the desk's trading and hedging limits, current and potential future loss exposures, and strategies; and ~~(2)Notice and Response Procedures.~~

~~(i)Notice. When the [Agency] determines that the purchase or sale of one or more financial instruments is for the trading account under paragraph (g)(1) of this section, the [Agency] will notify the banking entity in writing of the determination and provide an explanation of the determination.~~

~~(ii)Response.~~

~~(A)The banking entity may respond to any or all items in the notice. The response should include any matters that the banking entity would have the [Agency] consider in deciding whether the purchase or sale is for the trading account. The response must be in writing and delivered to the designated [Agency] official within 30 days after the date on which the banking entity received the notice. The [Agency] may shorten the time period when, in the opinion of the [Agency], the activities or condition of the banking entity so requires, provided that the banking entity is informed promptly of the new time period, or with the consent of the banking entity. In its discretion, the [Agency] may extend the time period for good cause.~~

~~(B)Failure to respond within 30 days or such other time period as may be specified by the [Agency] shall constitute a waiver of any objections to the [Agency]'s determination.~~

~~(iii)After the close of banking entity's response period, the [Agency] will decide, based on a review of the banking entity's response and other information concerning the banking entity, whether to maintain the [Agency]'s determination that the purchase or sale of one or more financial instruments is for the trading account. The banking entity will be notified of the decision in writing. The notice will include an explanation of the decision.~~

(C) Characterized by a clearly defined unit that:

(1) Engages in coordinated trading activity with a unified approach to its key elements;

(2) Operates subject to a common and calibrated set of risk metrics, risk levels, and joint trading limits;

(3) Submits compliance reports and other information as a unit for monitoring by management; and

(4) Books its trades together; or

(ii) For a banking entity that calculates risk-based capital ratios under the market risk capital rule, or a consolidated affiliate for regulatory reporting purposes of a banking entity that calculates risk-based capital ratios under the market risk capital rule, established by the banking entity or its affiliate for purposes of market risk capital calculations under the market risk capital rule.

§ 248.4 Permitted underwriting and market making-related activities.

(a) *Underwriting activities*—(1) *Permitted underwriting activities.* The prohibition contained in §____.3(a) does not apply to a banking entity's underwriting activities conducted in accordance with this paragraph (a).

(2) *Requirements.* The underwriting activities of a banking entity are permitted under paragraph (a)(1) of this section only if:

(i) The banking entity is acting as an underwriter for a distribution of securities and the trading desk's underwriting position is related to such distribution;

(ii) (A) The amount and type of the securities in the trading desk's underwriting position are designed not to exceed the reasonably expected near term demands of clients, customers,

or counterparties, taking into account the liquidity, maturity, and depth of the market for the relevant types of securities; and (B) reasonable efforts are made to sell or otherwise reduce the underwriting position within a reasonable period, taking into account the liquidity, maturity, and depth of the market for the relevant types of securities;

(iii) In the case of a banking entity with significant trading assets and liabilities, the banking entity has established and implements, maintains, and enforces an internal compliance program required by subpart D of this part that is reasonably designed to ensure the banking entity's compliance with the requirements of paragraph (a) of this section, including reasonably designed written policies and procedures, internal controls, analysis, and independent testing identifying and addressing:

(A) The products, instruments or exposures each trading desk may purchase, sell, or manage as part of its underwriting activities;

(B) Limits for each trading desk, in accordance with paragraph (a)(8)(i) (a)(2)(ii)(A) of this section;

(C)Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits; and

(D)Authorization

(C) Written authorization procedures, including escalation procedures that require review and approval of any trade that would exceed a trading desk's limit(s), demonstrable analysis of the basis for any temporary or permanent increase to a trading desk's limit(s), and independent review of such demonstrable analysis and approval; and

(D) Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits.

A banking entity with significant trading assets and liabilities may satisfy the requirements in (B) and (C) by complying with the requirements set forth below in paragraph (c) of this section;

(iv) The compensation arrangements of persons performing the activities described in this paragraph (a) are designed not to reward or incentivize prohibited proprietary trading; and

(v) The banking entity is licensed or registered to engage in the activity described in this paragraph (a) in accordance with applicable law.

(3) *Definition of distribution.* For purposes of this paragraph (a), a *distribution* of securities means:

(i) An offering of securities, whether or not subject to registration under the Securities Act of 1933, that is distinguished from ordinary trading transactions by the presence of special selling efforts and selling methods; or

(ii) An offering of securities made pursuant to an effective registration statement under the Securities Act of 1933.

(4) *Definition of underwriter.* For purposes of this paragraph (a), *underwriter* means:

(i) A person who has agreed with an issuer or selling security holder to:

(A) Purchase securities from the issuer or selling security holder for distribution;

(B) Engage in a distribution of securities for or on behalf of the issuer or selling security holder; or

(C) Manage a distribution of securities for or on behalf of the issuer or selling security holder; or

(ii) A person who has agreed to participate or is participating in a distribution of such securities for or on behalf of the issuer or selling security holder.

(5) *Definition of selling security holder.* For purposes of this paragraph (a), *selling security holder* means any person, other than an issuer, on whose behalf a distribution is made.

(6) *Definition of underwriting position.* For purposes of this ~~paragraph(a)~~section, *underwriting position* means the long or short positions in one or more securities held by a banking entity or its affiliate, and managed by a particular trading desk, in connection with a particular distribution of securities for which such banking entity or affiliate is acting as an underwriter.

(7) *Definition of client, customer, and counterparty.* For purposes of this paragraph (a), the terms *client, customer, and counterparty,* on a collective or individual basis, refer to market participants that may transact with the banking entity in connection with a particular distribution for which the banking entity is acting as underwriter.

~~(8)*Rebuttable presumption of compliance*.~~

~~(i)*Risk limits*.~~

~~(A)A banking entity shall be presumed to meet the requirements of paragraph (a)(2)(ii)(A) of this section with respect to the purchase or sale of a financial instrument if the banking entity has established and implements, maintains, and enforces the limits described in paragraph (a)(8)(i)(B) and does not exceed such limits.~~

~~(B)The presumption described in paragraph (8)(i)(A) of this section shall be available with respect to limits for each trading desk that are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties, based on the nature and amount of the trading desk's underwriting activities, on the:~~

~~(1)Amount, types, and risk of its underwriting position;~~

~~(2)Level of exposures to relevant risk factors arising from its underwriting position; and~~

~~(3)Period of time a security may be held.~~

~~(ii)*Supervisory review and oversight*. The limits described in paragraph (a)(8)(i) of this section shall be subject to supervisory review and oversight by the [Agency] on an ongoing~~

~~basis. Any review of such limits will include assessment of whether the limits are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties.~~

~~(iii)*Reporting*. With respect to any limit identified pursuant to paragraph (a)(8)(i) of this section, a banking entity shall promptly report to the [Agency] (A) to the extent that any limit is exceeded and (B) any temporary or permanent increase to any limit(s), in each case in the form and manner as directed by the [Agency].~~

~~(iv)*Rebutting the presumption*. The presumption in paragraph (a)(8)(i) of this section may be rebutted by the [Agency] if the [Agency] determines, based on all relevant facts and circumstances, that a trading desk is engaging in activity that is not based on the reasonably expected near term demands of clients, customers, or counterparties. The [Agency] will provide notice of any such determination to the banking entity in writing.~~

(b) *Market making-related activities*—(1) *Permitted market making-related activities.* The prohibition contained in §__.3(a) does not apply to a banking entity's market making-related activities conducted in accordance with this paragraph (b).

(2) *Requirements.* The market making-related activities of a banking entity are permitted under paragraph (b)(1) of this section only if:

(i) The trading desk that establishes and manages the financial exposure, routinely stands ready to purchase and sell one or more types of financial instruments related to its financial exposure, and is willing and available to quote, purchase and sell, or otherwise enter into long and short positions in those types of financial instruments for its own account, in commercially reasonable amounts and throughout market cycles on a basis appropriate for the liquidity, maturity, and depth of the market for the relevant types of financial instruments;

(ii) The trading desk's market-making related activities are designed not to exceed, on an ongoing basis, the reasonably expected near term demands of clients, customers, or counterparties, ~~based on~~taking into account the liquidity, maturity, and depth of the market for the relevant types of financial ~~instrument(s).~~instruments;

(iii) In the case of a banking entity with significant trading assets and liabilities, the banking entity has established and implements, maintains, and enforces an internal compliance program required by subpart D of this part that is reasonably designed to ensure the banking entity's compliance with the requirements of paragraph (b) of this section, including reasonably designed written policies and procedures, internal controls, analysis and independent testing identifying and addressing:

(A) The financial instruments each trading desk stands ready to purchase and sell in accordance with paragraph (b)(2)(i) of this section;

(B) The actions the trading desk will take to demonstrably reduce or otherwise significantly mitigate promptly the risks of its financial exposure consistent with the limits required under paragraph (b)(2)(iii)(C) of this section; the products, instruments, and exposures each trading desk may use for risk management purposes; the techniques and strategies each trading desk may use to manage the risks of its market making-related activities and positions; and the process, strategies, and personnel responsible for ensuring that the actions taken by the trading desk to mitigate these risks are and continue to be effective;

(C) Limits for each trading desk, in accordance with paragraph~~(b)(6)(i)~~ (b)(2)(ii) of this section;

~~(D)Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits; and~~

~~(E)Authorization~~

(D) Written authorization procedures, including escalation procedures that require review and approval of any trade that would exceed a trading desk's limit(s), demonstrable analysis ~~that~~of the basis for any temporary or permanent increase to a trading desk's limit(s~~) is consistent with the requirements of this paragraph (b~~), and independent review of such demonstrable analysis and approval; and

(E) ~~In the case of a~~ Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits.

A banking entity with significant trading assets and liabilities~~, to~~ may satisfy the ~~extent that any limit identified pursuant to~~requirements in (C) and (D) by complying with the requirements set forth below in paragraph (~~b)(2)(iii)(C~~c) of this section~~is exceeded, the trading desk takes action to bring the trading desk into compliancewith the limits as promptly as possible after the limit is exceeded~~;

~~(v)~~(iv) The compensation arrangements of persons performing the activities described in this paragraph (b) are designed not to reward or incentivize prohibited proprietary trading; and

~~(vi)~~(v) The banking entity is licensed or registered to engage in activity described in this paragraph (b) in accordance with applicable law.

(3) *Definition of client, customer, and counterparty.* For purposes of paragraph (b) of this section, the terms *client, customer, and counterparty,* on a collective or individual basis refer to market participants that make use of the banking entity's market making-related services by obtaining such services, responding to quotations, or entering into a continuing relationship with respect to such services, provided that:

(i) A trading desk or other organizational unit of another banking entity is not a client, customer, or counterparty of the trading desk if that other entity has trading assets and liabilities of $50 billion or more as measured in accordance with the methodology described in ~~definition of "significant trading assets and liabilities" contained in~~§__.2(ee) of this part, unless:

(A) The trading desk documents how and why a particular trading desk or other organizational unit of the entity should be treated as a client, customer, or counterparty of the trading desk for purposes of paragraph (b)(2) of this section; or

(B) The purchase or sale by the trading desk is conducted anonymously on an exchange or similar trading facility that permits trading on behalf of a broad range of market participants.

(4) *Definition of financial exposure.* For purposes of this ~~paragraph (b)~~section, *financial*

exposure means the aggregate risks of one or more financial instruments and any associated loans, commodities, or foreign exchange or currency, held by a banking entity or its affiliate and managed by a particular trading desk as part of the trading desk's market making- related activities.

(5) *Definition of market-maker positions.* For the purposes of this ~~paragraph (b)~~section, *market-maker positions* means all of the positions in the financial instruments for which the trading desk stands ready to make a market in accordance with paragraph (b)(2)(i) of this section, that are managed by the trading desk, including the trading desk's open positions or exposures arising from open transactions.

(c)~~(6)~~*Rebuttable presumption of compliance.*

(1) ~~(i)Risk limits.~~Internal Limits.

(i) ~~*(A)*~~A banking entity shall be presumed to meet the requirement~~sof~~ in paragraph (a)(2)(ii)(A) or (b)(2)(ii) of this section with respect to the purchase or sale of a financial instrument if the banking entity has established and implements, maintains, and enforces the internal limits for the relevant trading desk as described in paragraph (~~b~~c)(~~6~~1)(~~i~~ii)~~(B) and does not exceed such limits.~~

~~(B)The~~ of this section. (ii)(A) With respect to underwriting activities conducted pursuant to paragraph (a) of this section, the presumption described in paragraph (~~6~~c)(1)(i~~)(A~~) of this section shall be available ~~with respect~~to ~~limits for~~each trading desk that establishes, implements, maintains, and enforces internal limits that are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties, based on the nature and amount of the trading desk's underwriting activities, on the:

(1) Amount, types, and risk of its underwriting position;

(2) Level of exposures to relevant risk factors arising from its underwriting position; and

(3) Period of time a security may be held.

Such internal limits should take into account the liquidity, maturity, and depth of the market for the relevant types of securities.

(B) With respect to market making-related activities conducted pursuant to paragraph (b) of this section, the presumption described in paragraph (c)(1)(i) of this section shall be available to each trading desk that establishes, implements, maintains, and enforces internal limits that are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties, based on the nature and amount of the trading desk's market -making~~-~~ related activities, ~~on~~that address the:

(1) Amount, types, and risks of its market-maker positions;

(2) Amount, types, and risks of the products, instruments, and exposures the trading desk may use for risk management purposes;

(3) Level of exposures to relevant risk factors arising from its financial exposure; and

(4) Period of time a financial instrument may be held.

Such internal limits should take into account the liquidity, maturity, and depth of the market for the relevant types of financial instruments.

(2) ~~(ii)~~*Supervisory review and oversight.* The limits described in paragraph (~~b~~c)(~~6~~)(~~i~~1) of this section shall be subject to supervisory review and oversight by the [Agency] on an ongoing basis.~~Any review of such limits will include assessment of whether the~~

(3) ~~limits are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties.~~

~~(iii)*Reporting.*~~*Limit Breaches and Increases.* (i) With respect to any limit ~~identified~~set pursuant to paragraphs (~~b~~c)(~~6~~1)(~~i~~ii)(A) or (c)(1)(ii)(B) of this section, a banking entity shall ~~promptly report~~maintain and make available to the [Agency] ~~(A) to the extent that~~upon request records regarding (1) any limit that is exceeded and (~~B~~2) any temporary or permanent increase to any limit(s) , in each case in the form and manner as directed by the [Agency].

(ii) In the event of a breach or increase of any limit set pursuant to paragraphs (c)(1)(ii)(A) or (c)(1)(ii)(B) of this section, the presumption described in paragraph (c)(1)(i) of this section shall continue to be available only if the banking entity:

(1) Takes action as promptly as possible after a breach to bring the trading desk into compliance; and

(2) Follows established written authorization procedures, including escalation procedures that require review and approval of any trade that exceeds a trading desk's limit(s), demonstrable analysis of the basis for any temporary or permanent increase to a trading desk's limit(s), and independent review of such demonstrable analysis and approval.

(4) ~~(iv)~~*Rebutting the presumption.* The presumption in paragraph (~~b~~c)(~~6~~1)(i) of this section may be rebutted by the [Agency] if the [Agency] determines, taking into account the liquidity, maturity, and depth of the market for the relevant types of financial instruments and based on all relevant facts and circumstances, that a trading desk is engaging in activity that is not based on the reasonably expected near term demands of clients, customers, or counterparties. The [Agency]~~will provide notice of any such determination to the banking entity~~'s rebuttal of the presumption in paragraph (c)(1)(i) must be made in accordance with the notice and response procedures in ~~writing~~Subpart D.

§ 248.5 Permitted risk-mitigating hedging activities.

(a) *Permitted risk-mitigating hedging activities.* The prohibition contained in § 248.3(a) does not apply to the risk-mitigating hedging activities of a banking entity in connection with and related to individual or aggregated positions, contracts, or other holdings of the banking entity and designed to reduce the specific risks to the banking entity in connection with and related to such positions, contracts, or other holdings.

(b) Requirements.

(1) The risk-mitigating hedging activities of a banking entity that has significant trading assets and liabilities are permitted under paragraph (a) of this section only if:

(i) The banking entity has established and implements, maintains and enforces an internal compliance program required by 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 regarding the positions, techniques and strategies that may be used for hedging, including documentation indicating what positions, contracts or other holdings a particular trading desk may use in its risk-mitigating hedging activities, as well as position and aging limits with respect to such positions, contracts or other holdings;

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

(C) The conduct of analysis and independent testing designed to ensure that the positions, techniques and strategies that may be used for hedging may reasonably be expected to reduce or otherwise significantly mitigate the specific, identifiable risk(s) being hedged;

(ii) The risk-mitigating hedging activity:

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

(B) At the inception of the hedging activity, including, without limitation, any adjustments to the hedging activity, is designed to reduce or otherwise significantly mitigate one or more specific, identifiable risks, including market risk, counterparty or other credit risk, currency or foreign exchange risk, interest rate risk, commodity price risk, basis risk, or similar risks, arising in connection with and related to identified positions, contracts, or other holdings of the banking entity, based upon the facts and circumstances of the identified underlying and hedging positions, contracts or other holdings and the risks and liquidity thereof;

(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;

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

(1) Is consistent with the written hedging policies and procedures required under paragraph (b)(1)(i) of this section;

(2) Is designed to reduce or otherwise significantly mitigate the specific, identifiable risks that develop over time from the risk-mitigating hedging activities undertaken under this section and the underlying positions, contracts, and other holdings of the banking entity, based upon the facts and circumstances of the underlying and hedging positions, contracts and other

holdings of the banking entity and the risks and liquidity thereof; and

(3) Requires ongoing recalibration of the hedging activity by the banking entity to ensure that the hedging activity satisfies the requirements set out in paragraph (b)(1)(ii) of this section and is not prohibited proprietary trading; and

(iii) The compensation arrangements of persons performing risk- mitigating hedging activities are designed not to reward or incentivize prohibited proprietary trading.

(2) The risk-mitigating hedging activities of a banking entity that does not have significant trading assets and liabilities are permitted under paragraph (a) of this section only if the risk-mitigating hedging activity:

(i) At the inception of the hedging activity, including, without limitation, any adjustments to the hedging activity, is designed to reduce or otherwise significantly mitigate one or more specific, identifiable risks, including market risk, counterparty or other credit risk, currency or foreign exchange risk, interest rate risk, commodity price risk, basis risk, or similar risks, arising in connection with and related to identified positions, contracts, or other holdings of the banking entity, based upon the facts and circumstances of the identified underlying and hedging positions, contracts or other holdings and the risks and liquidity thereof; and

(ii) Is subject, as appropriate, to ongoing recalibration by the banking entity to ensure that the hedging activity satisfies the requirements set out in paragraph (b)(2) of this section and is not prohibited proprietary trading.

(c) *Documentation requirement.* (1) A banking entity that has significant trading assets and liabilities must comply with the requirements of paragraphs (c)(2) and (3) of this section, unless the requirements of paragraph (c)(4) of this section are met, with respect to any purchase or sale of financial instruments made in reliance on this section for risk-mitigating hedging purposes that is:

(i) Not established by the specific trading desk establishing or responsible for the underlying positions, contracts, or other holdings the risks of which the hedging activity is designed to reduce;

(ii) Established by the specific trading desk establishing or responsible for the underlying positions, contracts, or other holdings the risks of which the purchases or sales are designed to reduce, but that is effected through a financial instrument, exposure, technique, or strategy that is not specifically identified in the trading desk's written policies and procedures established under paragraph (b)(1) of this section or under § 248.4(b)(2)(iii)(B) of this subpart as a product, instrument, exposure, technique, or strategy such trading desk may use for hedging; or

(iii) Established to hedge aggregated positions across two or more trading desks.

(2) In connection with any purchase or sale identified in paragraph (c)(1) of this section, a banking entity must, at a minimum, and contemporaneously with the purchase or sale, document:

(i) The specific, identifiable risk(s) of the identified positions, contracts, or other holdings of

the banking entity that the purchase or sale is designed to reduce;

(ii) The specific risk-mitigating strategy that the purchase or sale is designed to fulfill; and

(iii) The trading desk or other business unit that is establishing and responsible for the hedge.

(3) A banking entity must create and retain records sufficient to demonstrate compliance with the requirements of this paragraph (c) for a period that is no less than five years in a form that allows the banking entity to promptly produce such records to the Board on request, or such longer period as required under other law or this part.

(4) The requirements of paragraphs (c)(2) and (3) of this section do not apply to the purchase or sale of a financial instrument described in paragraph (c)(1) of this section if:

(i) The financial instrument purchased or sold is identified on a written list of pre-approved financial instruments that are commonly used by the trading desk for the specific type of hedging activity for which the financial instrument is being purchased or sold; and

(ii) At the time the financial instrument is purchased or sold, the hedging activity (including the purchase or sale of the financial instrument) complies with written, pre-approved ~~hedging~~limits for the trading desk purchasing or selling the financial instrument for hedging activities undertaken for one or more other trading desks. The ~~hedging~~limits shall be appropriate for the:

(A) Size, types, and risks of the hedging activities commonly undertaken by the trading desk;

(B) Financial instruments purchased and sold for hedging activities by the trading desk; and

(C) Levels and duration of the risk exposures being hedged.

§ 248.6 Other permitted proprietary trading activities.

(a) *Permitted trading in domestic government obligations.* The prohibition contained in § 248.3(a) does not apply to the purchase or sale by a banking entity of a financial instrument that is:

(1) An obligation of, or issued or guaranteed by, the United States;

(2) An obligation, participation, or other instrument of, or issued or guaranteed by, an agency of the United States, the Government National Mortgage Association, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, a Federal Home Loan Bank, the Federal Agricultural Mortgage Corporation or a Farm Credit System institution chartered under and subject to the provisions of the Farm Credit Act of 1971 (12 U.S.C. 2001 *et seq.*);

(3) An obligation of any State or any political subdivision thereof, including any municipal security; or

(4) An obligation of the FDIC, or any entity formed by or on behalf of the FDIC for purpose of facilitating the disposal of assets acquired or held by the FDIC 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.

(b) *Permitted trading in foreign government obligations*—(1) *Affiliates of foreign banking entities in the United States.* The prohibition contained in § 248.3(a) does not apply to the purchase or sale of a financial instrument that is an obligation of, or issued or guaranteed by, a foreign sovereign (including any multinational central bank of which the foreign sovereign is a member), or any agency or political subdivision of such foreign sovereign, by a banking entity, so long as:

(i) The banking entity is organized under or is directly or indirectly controlled by a banking entity that is organized under the laws of a foreign sovereign and is not directly or indirectly controlled by a top-tier banking entity that is organized under the laws of the United States;

(ii) The financial instrument is an obligation of, or issued or guaranteed by, the foreign sovereign under the laws of which the foreign banking entity referred to in paragraph (b)(1)(i) of this section is organized (including any multinational central bank of which the foreign sovereign is a member), or any agency or political subdivision of that foreign sovereign; and

(iii) The purchase or sale as principal is not made by an insured depository institution.

(2) *Foreign affiliates of a U.S. banking entity.* The prohibition contained in § 248.3(a) does not apply to the purchase or sale of a financial instrument that is an obligation of, or issued or guaranteed by, a foreign sovereign (including any multinational central bank of which the foreign sovereign is a member), or any agency or political subdivision of that foreign sovereign, by a foreign entity that is owned or controlled by a banking entity organized or established under the laws of the United States or any State, so long as:

(i) The foreign entity is a foreign bank, as defined in section 211.2(j) of the Board's Regulation K (12 CFR 211.2(j)), or is regulated by the foreign sovereign as a securities dealer;

(ii) The financial instrument is an obligation of, or issued or guaranteed by, the foreign sovereign under the laws of which the foreign entity is organized (including any multinational central bank of which the foreign sovereign is a member), or any agency or political subdivision of that foreign sovereign; and

(iii) The financial instrument is owned by the foreign entity and is not financed by an affiliate that is located in the United States or organized under the laws of the United States or of any State.

(c) *Permitted trading on behalf of customers*—(1) *Fiduciary transactions.* The prohibition contained in § 248.3(a) does not apply to the purchase or sale of financial instruments by a banking entity acting as trustee or in a similar fiduciary capacity, so long as:

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

(ii) The banking entity does not have or retain beneficial ownership of the financial instruments.

(2) *Riskless principal transactions.* The prohibition contained in § 248.3(a) does not apply to the purchase or sale of financial instruments by a banking entity acting as riskless principal in a transaction in which the banking entity, after receiving an order to purchase (or sell) a financial instrument from a customer, purchases (or sells) the financial instrument for its own account to offset a contemporaneous sale to (or purchase from) the customer.

(d) *Permitted trading by a regulated insurance company.* The prohibition contained in § 248.3(a) does not apply to the purchase or sale of financial instruments by a banking entity that is an insurance company or an affiliate of an insurance company if:

(1) The insurance company or its affiliate purchases or sells the financial instruments solely for:

(i) The general account of the insurance company; or

(ii) A separate account established by the insurance company;

(2) The purchase or sale is conducted in compliance with, and subject to, the insurance company investment laws, regulations, and written guidance 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, regulation, or written guidance described in paragraph (d)(2) of this section is insufficient to protect the safety and soundness of the covered banking entity, or the financial stability of the United States.

(e) *Permitted trading activities of foreign banking entities.* (1) The prohibition contained in § 248.3(a) does not apply to the purchase or sale of financial instruments by a banking entity 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 any State;

(ii) The purchase or sale by the banking entity is made pursuant to paragraph (9) or (13) of section 4(c) of the BHC Act; and

(iii) The purchase or sale meets the requirements of paragraph (e)(3) of this section.

(2) A purchase or sale of financial instruments by a banking entity is made pursuant to paragraph (9) or (13) of section 4(c) of the BHC Act for purposes of paragraph (e)(1)(ii) of this section only if:

(i) The purchase or sale is conducted in accordance with the requirements of paragraph (e) 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 any State 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) A purchase or sale by a banking entity is permitted for purposes of this paragraph (e) if:

(i) The banking entity engaging as principal in the purchase or sale (including relevant personnel) is not 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 purchase or sell as principal is not located in the United States or organized under the laws of the United States or of any State; and

(iii) The purchase or sale, including any transaction arising from risk- mitigating hedging related to the instruments purchased or sold, is not accounted for as principal directly or 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.

~~(4)For purposes of this paragraph (e), a U.S. entity is any entity that is, or is controlled by, or is acting on behalf of, or at the direction of, any other entity that is, located in the United States or organized under the laws of the United States or of any State.~~

(4)~~(5)~~ For purposes of this paragraph (e), a U.S. branch, agency, or subsidiary of a foreign banking entity is considered to be 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.

§ 248.7 Limitations on permitted proprietary trading activities.

(a) No transaction, class of transactions, or activity may be deemed permissible under §§

248.4 through 248.6 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.

§§ 248.8-248.9 [Reserved]

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;

(B) Is authorized to offer and sell ownership interests to retail investors in the issuer's home jurisdiction; and

(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 of such entities.

(iii) For purposes of paragraph (c)(1)(i)(C) 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;

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

(C) 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 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 ~~supervisory guidance~~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 solely of:

(A) Loans as defined in §__.2(~~u~~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 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.

(ii) *Impermissible assets.* For purposes of this paragraph (c)(8), 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 paragraph (c)(8)(iii) 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 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 derivative directly relate to the loans, the asset-backed securities, or the contractual rights of 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 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

(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.

(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) ~~(1)~~*Asset-backed security* has the meaning specified in Section 3(a)(79) of the Exchange Act (15 U.S.C. 78c(a)(79).

(3) ~~(2)~~*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) ~~(3)~~*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) ~~(4)~~*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) ~~(5)~~*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);

(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)(~~5~~6)(i)(A) through (F) of this section.

(ii) *Ownership interest* does not include: *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) 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) 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;

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

(D) 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.

(7) ~~(6)~~*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) ~~(7)~~*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) ~~(8)~~*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) ~~(9)~~*Trustee.* (i) For purposes of paragraph (d)(~~8~~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)(~~9~~10)(i)(A) of this section;

(ii) Any entity that directs a person described in paragraph (d)(~~9~~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 §___.10(a) of this subpart 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 §__.4(a) or §__.4(b) of subpart 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 §__.12(a)(2)(ii); §__.12(a)(2)(iii), and §__.12(d) of this subpart.

§ 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 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 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.

(c) *Aggregate permitted investments in all covered funds.* (1) 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)(~~5~~6)(ii) of this subpart), on a historical cost basis.

(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) 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)(~~5~~6)(ii) of subpart C), on a historical cost basis, plus any earnings received; and

(2) 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)(~~5~~6)(ii) of subpart C), if the banking entity accounts for the profits (or losses) of the fund investment in its financial statements.

(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:

(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) 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) *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) *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) *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 §___.10(a) of this subpart 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~~.~~; and

(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 §__.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~~, and written guidance~~ 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~~, or written guidance~~ 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.

§ 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 [Agency] (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.

(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 transactions.* A prime brokerage transaction permitted under paragraph (a)(2)(ii) 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.

§§ 248.17-248.19 [Reserved]

Subpart D—Compliance Program Requirement; Violations

§ 248.20 Program for compliance; reporting.

(a) *Program requirement.* Each banking entity (other than a banking entity with limited trading assets and liabilities) shall develop and provide for the continued administration of a compliance program reasonably designed to ensure and monitor compliance with the prohibitions and restrictions on proprietary trading and covered fund activities and investments set forth in section 13 of the BHC Act and this part. The terms, scope, and detail of the compliance program shall be appropriate for the types, size, scope, and complexity of activities

and business structure of the banking entity.

(b) *Banking entities with significant trading assets and liabilities.* With respect to a banking entity with significant trading assets and liabilities, the compliance program required by paragraph (a) of this section, at a minimum, shall include:

(1) Written policies and procedures reasonably designed to document, describe, monitor and limit trading activities subject to subpart B (including those permitted under §§ 248.3 to 248.6 of subpart B), including setting, monitoring and managing required limits set out in §§ 248.4 and 248.5, and activities and investments with respect to a covered fund subject to subpart C (including those permitted under §§ 248.11 through 248.14 of subpart C) conducted by the banking entity to ensure that all activities and investments conducted by the banking entity that are subject to section 13 of the BHC Act and this part comply with section 13 of the BHC Act and this part;

(2) A system of internal controls reasonably designed to monitor compliance with section 13 of the BHC Act and this part and to prevent the occurrence of activities or investments that are prohibited by section 13 of the BHC Act and this part;

(3) A management framework that clearly delineates responsibility and accountability for compliance with section 13 of the BHC Act and this part and includes appropriate management review of trading limits, strategies, hedging activities, investments, incentive compensation and other matters identified in this part or by management as requiring attention;

(4) Independent testing and audit of the effectiveness of the compliance program conducted periodically by qualified personnel of the banking entity or by a qualified outside party;

(5) Training for trading personnel and managers, as well as other appropriate personnel, to effectively implement and enforce the compliance program; and

(6) Records sufficient to demonstrate compliance with section 13 of the BHC Act and this part, which a banking entity must promptly provide to the Board upon request and retain for a period of no less than 5 years or such longer period as required by the Board.

(c) *CEO attestation.* The CEO of a banking entity ~~described in paragraph (2)~~that has significant trading assets and liabilities must, based on a review by the CEO of the banking entity, attest in writing to the [Agency], each year no later than March 31, that the banking entity has in place processes to establish, maintain, enforce, review, test and modify the compliance program required by paragraph (b) of this section in a manner reasonably designed to achieve compliance with section 13 of the BHC Act and this part. In the case of a U.S. branch or agency of a foreign banking entity, the attestation may be provided for the entire U.S. operations of the foreign banking entity by the senior management officer of the U.S. operations of the foreign banking entity who is located in the United States.

~~(2)The requirements of paragraph (c)(1) of this section apply to a banking entity if:~~

~~(i)The banking entity does not have limited trading assets and liabilities; or~~

~~(ii)The [Agency] notifies the banking entity in writing that it must satisfy the requirements~~

~~contained in paragraph (c)(1) of this section.~~

(d) *Reporting requirements under the Appendix to this part.* (1) A banking entity engaged in proprietary trading activity permitted under subpart B shall comply with the reporting requirements described in the Appendix, if:

(i) The banking entity has significant trading assets and liabilities; or

(ii) The [Agency] notifies the banking entity in writing that it must satisfy the reporting requirements contained in the Appendix.

(2) Frequency of reporting: Unless the [Agency] notifies the banking entity in writing that it must report on a different basis, a banking entity ~~with $50 billion or more in trading assets and liabilities (as calculated in accordance with the methodology described in the definition of "significant trading assets and liabilities" contained in § .2 of this part of this part [sic]) shall report the information required by the Appendix for each calendar month within 20 days of the end of each calendar month. Any other banking entity~~subject to the Appendix shall report the information required by the Appendix for each ~~calendar~~quarter within 30 days of the end of ~~that calendar~~the quarter~~unless the [Agency] notifies the banking entity in writing that it must report on a different basis~~.

(e) *Additional documentation for covered funds.* A banking entity with significant trading assets and liabilities shall maintain records that include:

(1) Documentation of the exclusions or exemptions other than sections 3(c)(1) and 3(c)(7) of the Investment Company Act of 1940 relied on by each fund sponsored by the banking entity (including all subsidiaries and affiliates) in determining that such fund is not a covered fund;

(2) For each fund sponsored by the banking entity (including all subsidiaries and affiliates) for which the banking entity relies on one or more of the exclusions from the definition of covered fund provided by §§ 248.10(c)(1), 248.10(c)(5), 248.10(c)(8), 248.10(c)(9), or 248.10(c)(10) of subpart C, documentation supporting the banking entity's determination that the fund is not a covered fund pursuant to one or more of those exclusions;

(3) For each seeding vehicle described in § 248.10(c)(12)(i) or (iii) of subpart C that will become a registered investment company or SEC-regulated business development company, a written plan documenting the banking entity's determination that the seeding vehicle will become a registered investment company or SEC-regulated business development company; the period of time during which the vehicle will operate as a seeding vehicle; and the banking entity's plan to market the vehicle to third-party investors and convert it into a registered investment company or SEC-regulated business development company within the time period specified in § 248.12(a)(2)(i)(B) of subpart C;

(4) 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, if the aggregate amount of ownership interests in foreign public funds that are described in § 248.10(c)(1) of subpart C owned by such banking entity (including ownership interests owned by any affiliate that 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) exceeds $50 million at the end

of two or more consecutive calendar quarters, beginning with the next succeeding calendar quarter, documentation of the value of the ownership interests owned by the banking entity (and such affiliates) in each foreign public fund and each jurisdiction in which any such foreign public fund is organized, calculated as of the end of each calendar quarter, which documentation must continue until the banking entity's aggregate amount of ownership interests in foreign public funds is below $50 million for two consecutive calendar quarters; and

(5) For purposes of paragraph (e)(4) 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.

(f) *Simplified programs for less active banking entities*—(1) *Banking entities with no covered activities.* A banking entity that does not engage in activities or investments pursuant to subpart B or subpart C (other than trading activities permitted pursuant to § 248.6(a) of subpart B) may satisfy the requirements of this section by establishing the required compliance program prior to becoming engaged in such activities or making such investments (other than trading activities permitted pursuant to § 248.6(a) of subpart B).

(2) *Banking entities with moderate trading assets and liabilities.* A banking entity with moderate trading assets and liabilities may satisfy the requirements of this section by including in its existing compliance policies and procedures appropriate references to the requirements of section 13 of the BHC Act and this part and adjustments as appropriate given the activities, size, scope, and complexity of the banking entity.

(g) Rebuttable presumption of compliance for banking entities with limited trading assets and liabilities.

(1) *Rebuttable presumption.* Except as otherwise provided in this paragraph, a banking entity with limited trading assets and liabilities shall be presumed to be compliant with subpart B and subpart C and shall have no obligation to demonstrate compliance with this part on an ongoing basis.

(2) *Rebuttal of presumption.* If upon examination or audit, the [Agency] determines that the banking entity has engaged in proprietary trading or covered fund activities that are otherwise prohibited under subpart B or subpart C, the [Agency] may require the banking entity to be treated under this part as if it did not have limited trading assets and liabilities. The [Agency]'s rebuttal of the presumption in this paragraph must be made in accordance with the notice and response procedures in paragraph (i) of this Subpart.

(h) Reservation of authority. Notwithstanding any other provision of this part, the [Agency] retains its authority to require a banking entity without significant trading assets and liabilities to apply any requirements of this part that would otherwise apply if the banking entity had significant or moderate trading assets and liabilities if the [Agency] determines that the size or complexity of the banking entity's trading or investment activities, or the risk of evasion of subpart B or subpart C, does not warrant a presumption of compliance under paragraph (g) of this section or treatment as a banking entity with moderate trading assets and liabilities, as applicable. The [Agency]'s exercise of this reservation of authority must be made in accordance with the notice and response procedures in paragraph (i) of this Subpart.

~~(ii)~~(i) Notice and Response Procedures.

(1) ~~(A)~~Notice. The [Agency] will notify the banking entity in writing of any determination ~~pursuant to paragraph (g)(2)(i) of this section to rebut the presumption described in this paragraph (g)~~requiring notice under this part and will provide an explanation of the determination.

(2) ~~(B)~~Response.~~(1)~~ The banking entity may respond to any or all items in the notice described in paragraph (~~g~~i)(~~2)(ii)(A~~1) of this section. The response should include any matters that the banking entity would have the [Agency] consider in deciding whether to make the ~~banking entity has engaged in proprietary trading or covered fund activities prohibited under subpart B or subpart C~~determination. The response must be in writing and delivered to the designated [Agency] official within 30 days after the date on which the banking entity received the notice. The [Agency] may shorten the time period when, in the opinion of the [Agency], the activities or condition of the banking entity so requires, provided that the banking entity is informed ~~promptly~~of the~~new~~ time period at the time of notice, or with the consent of the banking entity. In its discretion, the [Agency] may extend the time period for good cause.

~~(2)~~(3) Failure to respond within 30 days or such other time period as may be specified by the [Agency] shall constitute a waiver of any objections to the [Agency~~]'s determination.~~

~~(C)After the close of banking entity's response period, the [Agency] will decide, based on a review of the banking entity's response and other information concerning the banking entity, whether to maintain the [Agency~~]'s] determination~~that banking entity has engaged in proprietary trading or covered fund activities prohibited under subpart B or subpart C~~.

(4) The [Agency] will notify the banking entity~~will be notified~~ of the decision in writing. The notice will include an explanation of the decision.

~~(h)Reservation of authority. Notwithstanding any other provision of this part, the [Agency] retains its authority to require a banking entity without significant trading assets and liabilities to apply any requirements of this part that would otherwise apply if the banking entity had significant or moderate trading assets and liabilities if the [Agency] determines that the size or complexity of the banking entity's trading or investment activities, or the risk of evasion of subpart B or subpart C, does not warrant a presumption of compliance under paragraph (g) of this section or treatment as a banking entity with moderate trading assets and liabilities, as applicable.~~

§ 248.21 Termination of activities or investments; penalties for violations.

(a) Any banking entity that engages in an activity or makes an investment in violation of section 13 of the BHC Act or this part, or acts in a manner that functions as an evasion of the requirements of section 13 of the BHC Act or this part, including through an abuse of any activity or investment permitted under subparts B or C, or otherwise violates the restrictions and requirements of section 13 of the BHC Act or this part, shall, upon discovery, promptly terminate the activity and, as relevant, dispose of the investment.

(b) Whenever the Board finds reasonable cause to believe any banking entity has engaged in an activity or made an investment in violation of section 13 of the BHC Act or this

part, or engaged in any activity or made any investment that functions as an evasion of the requirements of section 13 of the BHC Act or this part, the Board may take any action permitted by law to enforce compliance with section 13 of the BHC Act and this part, including directing the banking entity to restrict, limit, or terminate any or all activities under this part and dispose of any investment.

Appendix to Part__—Reporting and Recordkeeping Requirements for Covered Trading Activities

I. PURPOSE

a. This appendix sets forth reporting and recordkeeping requirements that certain banking entities must satisfy in connection with the restrictions on proprietary trading set forth in subpart B ("proprietary trading restrictions"). Pursuant to §__.20(d), this appendix applies to a banking entity that, together with its affiliates and subsidiaries, has significant trading assets and liabilities. These entities are required to (i) furnish periodic reports to the [Agency] regarding a variety of quantitative measurements of their covered trading activities, which vary depending on the scope and size of covered trading activities, and (ii) create and maintain records documenting the preparation and content of these reports. The requirements of this appendix must be incorporated into the banking entity's internal compliance program under §__.20.

b. The purpose of this appendix is to assist banking entities and the [Agency] in:

(1) ~~(i)~~Better understanding and evaluating the scope, type, and profile of the banking entity's covered trading activities;

(2) ~~(ii)~~Monitoring the banking entity's covered trading activities;

(3) ~~(iii)~~Identifying covered trading activities that warrant further review or examination by the banking entity to verify compliance with the proprietary trading restrictions;

(4) ~~(iv)~~Evaluating whether the covered trading activities of trading desks engaged in market making-related activities subject to § .4(b) are consistent with the requirements governing permitted market making-related activities;

(5) ~~(v)~~Evaluating whether the covered trading activities of trading desks that are engaged in permitted trading activity subject to ~~§§~~§ __.4,__.5, or__.6(a)-(b) (i.e., underwriting and market making-~~related~~related activity, risk-mitigating hedging, or trading in certain government obligations) are consistent with the requirement that such activity not result, directly or indirectly, in a material exposure to high-risk assets or high-risk trading strategies;

(6) ~~(vi)~~Identifying the profile of particular covered trading activities of the banking entity, and the individual trading desks of the banking entity, to help establish the appropriate frequency and scope of examination by ~~the~~[Agency] of such activities; and

(7) ~~(vii)~~Assessing and addressing the risks associated with the banking entity~~'~~'s covered trading activities.

c. Information that must be furnished pursuant to this appendix is not intended to serve as a dispositive tool for the identification of permissible or impermissible activities.

d. In addition to the quantitative measurements required in this appendix, a banking entity may need to develop and implement other quantitative measurements in order to effectively monitor its covered trading activities for compliance with section 13 of the BHC Act and this part and to have an effective compliance program, as required by §__.20. The effectiveness of particular quantitative measurements may differ based on the profile of the banking entity's businesses in general and, more specifically, of the particular trading desk, including types of instruments traded, trading activities and strategies, and history and experience (e.g., whether the trading desk is an established, successful market maker or a new entrant to a competitive market). In all cases, banking entities must ensure that they have robust measures in place to identify and monitor the risks taken in their trading activities, to ensure that the activities are within risk tolerances established by the banking entity, and to monitor and examine for compliance with the proprietary trading restrictions in this part.

e. On an ongoing basis, banking entities must carefully monitor, review, and evaluate all furnished quantitative measurements, as well as any others that they choose to utilize in order to maintain compliance with section 13 of the BHC Act and this part. All measurement results that indicate a heightened risk of impermissible proprietary trading, including with respect to otherwise- permitted activities under §§§__.4 through __.6(a)-(b), or that result in a material exposure to high- risk assets or high-risk trading strategies, must be escalated within the banking entity for review, further analysis, explanation to the [Agency], and remediation, where appropriate. The quantitative measurements discussed in this appendix should be helpful to banking entities in identifying and managing the risks related to their covered trading activities.

II. DEFINITIONS

The terms used in this appendix have the same meanings as set forth in §§§__.2 and __§____.3. In addition, for purposes of this appendix, the following definitions apply:

Applicability identifies the trading desks for which a banking entity is required to calculate and report a particular quantitative measurement based on the type of covered trading activity conducted by the trading desk.

Calculation period means the period of time for which a particular quantitative measurement must be calculated.

Comprehensive profit and loss means the net profit or loss of a trading desk's material sources of trading revenue over a specific period of time, including, for example, any increase or decrease in the market value of a trading desk's holdings, dividend income, and interest income and expense.

Covered trading activity means trading conducted by a trading desk under §§§__.4, __.5, ___.6(a), or___.6(b). A banking entity may include in its covered trading activity trading conducted under §§ __§__.3(ed),_____.6(c),____.6(d), or_____.6(e).

Measurement frequency means the frequency with which a particular quantitative metric must be calculated and recorded.

Trading day means a calendar day on which a trading desk is open for trading.

III. REPORTING AND RECORDKEEPING

a. Scope of Required Reporting

1. Quantitative measurements. Each banking entity made subject to this appendix by § _____.20 must furnish the following quantitative measurements, as applicable, for each trading desk of the banking entity engaged in covered trading activities and calculate these quantitative measurements in accordance with this appendix:

i. ~~Risk and Position~~Internal Limits and Usage;

~~ii.Risk Factor Sensitivities;~~

~~iii~~ii. Value-at-Risk~~and Stressed Value-at-Risk~~;

~~iv~~iii. Comprehensive Profit and Loss Attribution;

~~v~~iv. Positions; and

~~vi~~v. Transaction Volumes~~; and~~

~~vii.Securities Inventory Aging~~.

2. Trading desk information. Each banking entity made subject to this appendix by § _____.20 must provide certain descriptive information, as further described in this appendix, regarding each trading desk engaged in covered trading activities.

3. Quantitative measurements identifying information. Each banking entity made subject to this appendix by § _.20 must provide certain identifying and descriptive information, as further described in this appendix, regarding its quantitative measurements.

4. Narrative statement. Each A [sic] banking entity made subject to this appendix by § _.20 ~~must~~may provide ~~a separate~~an optional narrative statement, as further described in this appendix.

5. File identifying information. Each banking entity made subject to this appendix by § .20 must provide file identifying information in each submission to the [Agency] pursuant to this appendix, including the name of the banking entity, the RSSD ID assigned to the top-tier banking entity by the Board, and identification of the reporting period and creation date and time.

b. Trading Desk Information

1. Each banking entity must provide descriptive information regarding each trading desk engaged in covered trading activities, including:

i. ~~1.~~Name of the trading desk used internally by the banking entity and a unique identification label for the trading desk;

ii. ~~2.~~Identification of each type of covered trading activity in which the trading desk is engaged;

iii. ~~3.~~Brief description of the general strategy of the trading desk;

v. ~~4.~~[sic] A list ~~of~~identifying each Agency receiving the ~~types of financial instruments and other products purchased and sold by~~submission of the trading desk;~~an indication of which of these are the main financial instruments or products purchased and sold by the trading desk; and, for trading desks engaged in market making-related activities under § .4(b), specification of whether each type of financial instrument is included in market-maker positions or not included in market- maker positions. In addition, indicate whether the trading desk is including in its quantitative measurements products excluded from the definition of "financial instrument" under § .3(d)(2) and, if so, identify such products;~~

~~5.Identification by complete name of each legal entity that serves as a booking entity for covered trading activities conducted by the trading desk; and indication of which of the identified legal entities are the main booking entities for covered trading activities of the trading desk;~~

~~6.For each legal entity that serves as a booking entity for covered trading activities, specification of any of the following applicable entity types for that legal entity:~~

~~A.National bank, Federal branch or Federal agency of a foreign bank, Federal savings association, Federal savings bank;~~

~~B.State nonmember bank, foreign bank having an insured branch, State savings association;~~

~~C.U.S.-registered broker-dealer, U.S.-registered security-based swap dealer, U.S.-registered major security-based swap participant;~~

~~D.Swap dealer, major swap participant, derivatives clearing organization, futures commission merchant, commodity pool operator, commodity trading advisor, introducing broker, floor trader, retail foreign exchange dealer;~~

~~E.State member bank;~~

~~F.Bank holding company, savings and loan holding company;~~

~~G.Foreign banking organization as defined in 12 CFR 211.21(o);~~

~~H.Uninsured State-licensed branch or agency of a foreign bank; or~~

~~I.Other entity type not listed above, including a subsidiary of a legal entity described above where the subsidiary itself is not an entity type listed above;~~

2. Indication of whether each calendar date is a trading day or not a trading day for the trading desk; and

3. Currency reported and daily currency conversion rate.

c. Quantitative Measurements Identifying Information

Each banking entity must provide the following information regarding the quantitative measurements:

~~i~~1.~~A Risk and Position~~An Internal Limits Information Schedule that provides identifying and descriptive information for each limit reported pursuant to the ~~Risk and Position~~Internal Limits and Usage quantitative measurement, including the name of the limit, a unique identification label for the limit, a description of the limit, ~~whether the limit is intraday or end-of-day,~~the unit of measurement for the limit, ~~whether~~the ~~limit measures risk on a net or gross basis, and the~~type of limit~~;~~

~~ii.A Risk Factor Sensitivities Information Schedule that provides identifying and descriptive information for each risk factor sensitivity reported pursuant to the Risk Factor Sensitivities quantitative measurement, including the name of the sensitivity, a unique~~, and identification ~~label for the sensitivity, a description~~of the corresponding risk factor attribution in the particular case that the limit type is a limit on a risk factor sensitivity~~,~~ and profit and loss attribution to the ~~sensitivity's~~same risk factor ~~change unit~~is reported; and

~~iii~~2. A Risk Factor Attribution Information Schedule that provides identifying and descriptive information for each risk factor attribution reported pursuant to the Comprehensive Profit and Loss Attribution quantitative measurement, including the name of the risk factor or other factor, a unique identification label for the risk factor or other factor, a description of the risk factor or other factor, and the risk factor or other factor's change unit~~;~~

~~4.A Limit/Sensitivity Cross-Reference Schedule that cross-references, by unique identification label, limits identified in the Risk and Position Limits Information Schedule to associated risk factor sensitivities identified in the Risk Factor Sensitivities Information Schedule; and~~

~~5.A Risk Factor Sensitivity/Attribution Cross-Reference Schedule that cross- references, by unique identification label, risk factor sensitivities identified in the Risk Factor Sensitivities Information Schedule to associated risk factor attributions identified in the Risk Factor Attribution Information Schedule.~~.

d. Narrative Statement

Each banking entity made subject to this appendix by §__.20 ~~must~~may submit in a separate electronic document a Narrative Statement to the [Agency] ~~describing~~with any information the banking entity views as relevant for assessing the information reported. The Narrative Statement may include further description of or changes ~~in~~to calculation methods~~used~~, ~~a~~identification of material events, description of and reasons for changes in the banking entity's trading desk structure or trading desk strategies, and when any such changes occurred. ~~The Narrative Statement must include any information the banking entity views as relevant for assessing the information reported, such as further description of calculation methods used.~~

~~If a banking entity does not have any information to report in a Narrative Statement, the banking entity must submit an electronic document stating that it does not have any information to report in a Narrative Statement.~~

e. Frequency and Method of Required Calculation and Reporting

A banking entity must calculate any applicable quantitative measurement for each trading

day.

A banking entity must report~~the Narrative Statement,~~ the Trading Desk Information, the Quantitative Measurements Identifying Information, and each applicable quantitative measurement electronically to ~~the~~[Agency] on the reporting schedule established in §__.20 unless otherwise requested by ~~the~~[Agency]. A banking entity must report the Trading Desk Information, the Quantitative Measurements Identifying Information, and each applicable quantitative measurement to the [Agency] in accordance with the XML Schema specified and published on the [Agency~~]~~'s] website.

f. Recordkeeping

A banking entity must, for any quantitative measurement furnished to ~~the~~[Agency] pursuant to this appendix and §____.20(d), create and maintain records documenting the preparation and content of these reports, as well as such information as is necessary to permit~~the~~ [Agency] to verify the accuracy of such reports, for a period of five years from the end of the calendar year for which the measurement was taken. A banking entity must retain the Narrative Statement, the Trading Desk Information, and the Quantitative Measurements Identifying Information for a period of five years from the end of the calendar year for which the information was reported to the [Agency].

IV. QUANTITATIVE MEASUREMENTS

a. Risk-Management Measurements

1. ~~Risk and Position~~Internal Limits and Usage

i. *Description:* For purposes of this appendix, ~~Risk and Position~~Internal Limits are the constraints that define the amount of risk and the positions that a trading desk is permitted to take at a point in time, as defined by the banking entity for a specific trading desk. Usage represents the value of the trading desk~~'~~'s risk or positions that are accounted for by the current activity of the desk. ~~Risk and position~~Internal limits and their usage are key compliance and risk management tools used to control and monitor risk taking and include, but are not limited to, the limits set out in §_____.4 and §___.5. A ~~number of the metrics that are described below,~~trading desk's risk limits, commonly including ~~"Risk Factor Sensitivities" and~~a limit on "Value-at-Risk," ~~relate to a trading desk's risk and position limits and~~are useful in ~~evaluating and setting these limits in~~the broader context of the trading desk~~'~~'s overall activities, particularly for the market making activities under §_ _____.4(b) and hedging activity under §_____.5. Accordingly, the limits required under § _____.4(b)(2)(iii)(C) and §_____ .5(b)(1)(i)(A) must meet the applicable requirements under §___.4(b)(2)(iii)(C) and §____ _____.5(b)(1)(i)(A) and also must include appropriate metrics for the trading desk limits including, at a minimum, ~~the "Risk Factor Sensitivities" and~~"Value-at-Risk"~~metrics~~ except to the extent ~~any of~~the "~~Risk Factor Sensitivities" or "~~Value-at- Risk" metric~~sare~~ is demonstrably ineffective for measuring and monitoring the risks of a trading desk based on the types of positions traded by, and risk exposures of, that desk.

A. A banking entity must provide the following information for each limit reported pursuant to this quantitative measurement: ~~T~~the unique identification label for the limit reported in the ~~Risk and Position~~Internal Limits Information Schedule, the limit size (distinguishing between an upper and a lower limit), and the value of usage of the limit.

ii.*Calculation Period*: One trading day.

iii.*Measurement Frequency*: Daily.

iv.*Applicability*:All trading desks engaged in covered trading activities.

~~2.Risk Factor Sensitivities~~

~~i. *Description*: For purposes of this appendix, Risk Factor Sensitivities are changes in a trading desk's Comprehensive Profit and Loss that are expected to occur in the event of a change in one or more underlying variables that are significant sources of the trading desk's profitability and risk. A banking entity must report the risk factor sensitivities that are monitored and managed as part of the trading desk's overall risk management policy. Reported risk factor sensitivities must be sufficiently granular to account for a preponderance of the expected price variation in the trading desk's holdings. A banking entity must provide the following information for each sensitivity that is reported pursuant to this quantitative measurement: The unique identification label for the risk factor sensitivity listed in the Risk Factor Sensitivities Information Schedule, the change in risk factor used to determine the risk factor sensitivity, and the aggregate change in value across all positions of the desk given the change in risk factor. ii. *Calculation Period*: One trading day.~~

~~iii.*Measurement Frequency*: Daily.~~

~~iv.*Applicability*: All trading desks engaged in covered trading activities.~~

2. Value-at-Risk~~and Stressed Value-at-Risk~~

i. *Description:* For purposes of this appendix, Value-at-Risk ("VaR") is the measurement of the risk of future financial loss in the value of a trading desk's aggregated positions at the ninety-nine percent confidence level over a one-day period, based on current market conditions. ~~For purposes of this appendix, Stressed Value-at-Risk ("Stressed VaR") is the measurement of the risk of future financial loss in the value of a trading desk's aggregated positions at the ninety-nine percent confidence level over a one-day period, based on market conditions during a period of significant financial stress~~

ii. *Calculation Period:* One trading day.

iii. *Measurement Frequency:* Daily.

iv. *Applicability*: All trading desks engaged in covered trading activities.~~For VaR, all trading desks engaged in covered trading activities. For Stressed VaR, all trading desks engaged in covered trading activities, except trading desks whose covered trading activity is conducted exclusively to hedge products excluded from the definition of "financial instrument" under § .3(d)(2).~~

b. Source-of-Revenue Measurements

1. Comprehensive Profit and Loss Attribution

i. *Description:* For purposes of this appendix, Comprehensive Profit and Loss Attribution is an analysis that attributes the daily fluctuation in the value of a trading desk's positions to various sources. First, the daily profit and loss of the aggregated positions is divided into

~~three~~two categories: (i) profit and loss attributable to a trading desk's existing positions that were also positions held by the trading desk as of the end of the prior day ("existing positions");~~(ii)~~ and (ii) profit and loss attributable to new positions resulting from the current day~~'~~'s trading activity ("new positions")~~; and (iii) residual profit and loss that cannot be specifically attributed to existing positions or new positions. The sum of (i), (ii), and (iii) must equal the trading desk's comprehensive profit and loss at each point in time~~.

A. The comprehensive profit and loss associated with existing positions must reflect changes in the value of these positions on the applicable day. The comprehensive profit and loss from existing positions must be further attributed, as applicable, to (i) changes in ~~(i)~~the specific risk factors and other factors that are monitored and managed as part of the trading desk's overall risk management policies and procedures; and (ii) any other applicable elements, such as cash flows, carry, changes in reserves, and the correction, cancellation, or exercise of a trade.

B. For the attribution of comprehensive profit and loss from existing positions to specific risk factors and other factors, a banking entity must provide the following information for the factors that explain the preponderance of the profit or loss changes due to risk factor changes: ~~T~~the unique identification label for the risk factor or other factor listed in the Risk Factor Attribution Information Schedule, and the profit or loss due to the risk factor or other factor change.

C. The comprehensive profit and loss attributed to new positions must reflect commissions and fee income or expense and market gains or losses associated with transactions executed on the applicable day. New positions include purchases and sales of financial instruments and other assets/liabilities and negotiated amendments to existing positions. The comprehensive profit and loss from new positions may be reported in the aggregate and does not need to be further attributed to specific sources.

D. The portion of comprehensive profit and loss from existing positions that ~~cannot be specifically~~is not attributed to ~~known sources~~changes in specific risk factors and other factors must be allocated to a residual category~~identified as an unexplained portion of the comprehensive profit and loss~~. Significant unexplained profit and loss must be escalated for further investigation and analysis.

ii.*Calculation Period*: One trading day.

iii.*Measurement Frequency:*Daily.

iv.*Applicability:*All trading desks engaged in covered trading activities.

c. Positions~~,~~ and Transaction Volumes~~, and Securities Inventory Aging~~ Measurements

1. Positions

i. *Description:* For purposes of this appendix, Positions is the value of securities and derivatives positions managed by the trading desk. For purposes of the Positions quantitative measurement, do not include in the Positions calculation for "securities" those securities that are also "derivatives," as those terms are defined under subpart A; instead, report those

securities that are also derivatives as "derivatives."[2] A banking entity must separately report the trading desk's market value of long securities positions, ~~market value of~~short securities positions, ~~market value of~~derivatives receivables, ~~market value of~~and derivatives payables~~, notional value of derivatives receivables, and notional value of derivatives payables~~.

ii. *Calculation Period:* One trading day.

iii. *Measurement Frequency:* Daily.

iv. *Applicability:* All trading desks that rely on § .4(a) or § .4(b) to conduct underwriting activity or market-making-related activity, respectively.

2. Transaction Volumes

i. *Description:* For purposes of this appendix, Transaction Volumes measures ~~four~~three exclusive categories of covered trading activity conducted by a trading desk. A banking entity is required to report the value and number of security and derivative transactions conducted by the trading desk with: (i) ~~C~~customers, excluding internal transactions; (ii) non- customers, excluding internal transactions; and (iii) trading desks and other organizational units where the transaction is booked ~~in~~into either the same banking entity~~; and (iv) trading desks and other organizational units where the transaction is booked into~~ or an affiliated banking entity. For securities, value means gross market value. For derivatives, value means gross notional value. For purposes of calculating the Transaction Volumes quantitative measurement, do not include in the Transaction Volumes calculation for "securities" those securities that are also "derivatives," as those terms are defined under subpart A; instead, report those securities that are also derivatives as "derivatives."[3] Further, for purposes of the Transaction Volumes quantitative measurement, a customer of a trading desk that relies on § .4(a) to conduct underwriting activity is a market participant identified in § .4(a)(7), and a customer of a trading desk that relies on § .4(b) to conduct market making-related activity is a market participant identified in § .4(b)(3).

ii. *Calculation Period:* One trading day.

iii. *Measurement Frequency:* Daily.

iv. *Applicability:* All trading desks that rely on § .4(a) or § .4(b) to conduct underwriting activity or market-making-related activity, respectively.

~~3.Securities Inventory Aging~~

~~i. *Description*: For purposes of this appendix, Securities Inventory Aging generally describes a schedule of the market value of the trading desk's securities positions and the amount of time that those securities positions have been held. Securities Inventory Aging must measure the age profile of a trading desk's securities positions for the following periods: 0-30 Calendar days; 31- 60 calendar days; 61-90 calendar days; 91-180 calendar~~

[2] See §§.2(~~i~~h), (~~bb~~aa). For example, under this part, a security-based swap is both a "security" and a "derivative." For purposes of the Positions quantitative measurement, security-based swaps are reported as derivatives rather than securities.

[3] See §§.2(~~i~~h), (~~bb~~aa).

days; 181- 360 calendar days; and greater than 360 calendar days. Securities Inventory Aging includes two schedules, a security asset- aging schedule, and a security liability-aging schedule. For purposes of the Securities Inventory Aging quantitative measurement, do not include securities that are also "derivatives," as those terms are defined under subpart A.[4]

ii. *Calculation Period*: One trading day.

iii. *Measurement Frequency*: Daily.

iv. *Applicability*: All trading desks that rely on § .4(a) or § .4(b) to conduct underwriting activity or market-making related activity, respectively.

[4] See §§.2(i), (bb).