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February 18, 2014

The Honorable Tim Johnson
Chairman
The Honorable Mike Crapo
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Jeb Hensarling
Chairman
The Honorable Maxine Waters
Ranking Member
Committee on Financial Services
House of Representatives

Subject: *Department of the Treasury, Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Securities and Exchange Commission: Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds*

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Department of the Treasury, Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (the Board), Federal Deposit Insurance Corporation (FDIC), and Securities and Exchange Commission (SEC) (collectively, the agencies) entitled “Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds” (RINS: 1557-AD44, 7100 AD82; 3064-AD85; 3235-AL07). We received the rule on December 27, 2013, from SEC; on January 30, 2014, from the Board; on January 30, 2014, from FDIC; and on January 31, 2014, from OCC. It was published in the *Federal Register* as a final rule on January 31, 2014, with an effective date of April 1, 2014. 79 Fed. Reg. 5536.

The final rule implements section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act¹ (Dodd-Frank Act) which contains certain prohibitions and restrictions on the ability of banking entities and nonbank financial companies supervised by the Board to engage in proprietary trading and on the ability to have certain interests in, or relationships with, hedge funds or private equity funds. Specifically, the rule prohibits banking entities from engaging in proprietary trading or acquiring or retaining an ownership interest in, or having certain relationships with, a covered fund, while permitting banking entities to continue to provide, and to manage and limit the risks associated with providing, client-oriented financial services that

¹ 12 U.S.C. § 1851.

are critical to capital generation for businesses, households, and individuals, and that facilitate liquid markets. These client-oriented financial services include underwriting, market making, and asset management services. The final rule includes a framework describing the key characteristics of both prohibited and permitted activities. The final rule also requires banking entities to establish a comprehensive compliance program designed to ensure compliance with the requirements of the statute and rule in a way that takes into account and reflects the banking entity's activities, size, scope, and complexity. With respect to proprietary trading, the final rule also requires the large firms that are active participants in trading activities to calculate and report meaningful quantitative data that will assist both the banking entities and the agencies in identifying a particular activity that warrants additional scrutiny to distinguish prohibited proprietary trading from otherwise permissible activities.

Enclosed is our assessment of the agencies' compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. Our review of the procedural steps taken indicates that the agencies complied with the applicable requirements. It should be noted that in the final rule the agencies state that a costs and benefits analysis is not required, although they do discuss some costs and benefits as raised in the public comments. Additionally, OCC indicated in its submission to us that it had prepared an analysis of the costs and benefits, although it did not include any such analysis beyond the text of the final rule in its submission to us.²

If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to the subject matter of the rule, please contact Shirley A. Jones, Assistant General Counsel, at (202) 512-8156.

signed

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Enclosure

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² As part of their submission to us, agencies are required to include a complete copy of the cost-benefit analysis of rules, if any. 5 U.S.C. § 801(a)(1)(B)(i).

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON A MAJOR RULE
ISSUED BY THE
DEPARTMENT OF THE TREASURY,
OFFICE OF THE COMPTROLLER OF THE CURRENCY,
BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
FEDERAL DEPOSIT INSURANCE CORPORATION,
SECURITIES AND EXCHANGE COMMISSION
ENTITLED
"PROHIBITIONS AND RESTRICTIONS ON PROPRIETARY TRADING
AND CERTAIN INTERESTS IN, AND RELATIONSHIPS WITH,
HEDGE FUNDS AND PRIVATE EQUITY FUNDS"
(RINS: 1557-AD44, 7100 AD82; 3064-AD85; 3235-AL07)

(i) Cost-benefit analysis

In the final rule, the agencies state that a costs and benefits analysis is not required. 79 Fed. Reg. 5541. However, the agencies noted that they found certain of the information submitted by commenters concerning costs and benefits and economic effects to be relevant to consideration of the rule, and so considered this information as appropriate. For example, in the final rule's discussion of the scope of the market-making exemption to the general prohibition on proprietary trading, the agencies described the commenters' views on market making and liquidity. Several commenters stated that the proposed rule would impact a banking entity's ability to engage in market making-related activity, with corresponding reductions in market liquidity. Some commenters identified possible benefits associated with reduced liquidity while other commenters identified negative market impacts. 79 Fed. Reg. 5583.

In their submission to us, the Board and SEC indicated that the preparation of an analysis of the costs and benefits of this final rule was not applicable. FDIC indicated that it had not prepared an analysis of the costs and benefits of this final rule. OCC indicated that it had prepared an analysis of the costs and benefits of this final rule but did not include any information other than the text of the final rule as its submission.

(ii) Agency actions relevant to the Regulatory Flexibility Act (RFA), 5 U.S.C. §§ 603-605, 607, and 609

The agencies certified that, for the banking entities subject to their jurisdictions, this final rule will not result in a significant economic impact on a substantial number of small entities.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

The OCC determined that this final rule qualifies as a significant regulatory action under the Act because its federal mandates may result in expenditures by the private sector in excess of \$100 million or more (adjusted for inflation) in any one year. As independent regulatory agencies, the Board, FDIC, and SEC are not subject to the Act.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 et seq.

OCC, the Board, FDIC, and SEC promulgated a joint notice of proposed rulemaking for this rule. 76 Fed. Reg. 68,846 (Nov. 7, 2011).³ The initial comment period was extended for an additional 30 days. 77 Fed. Reg. 23 (Jan. 3, 2012). The agencies received over 18,000 comments on the proposed rule. To improve understanding of the issues raised by commenters, the agencies met with a number of these commenters to discuss issues related to the proposed rule. The agencies responded to comments in the final rule.

Paperwork Reduction Act (PRA), 44 U.S.C. §§ 3501-3520

The agencies determined that this final rule contains information collection requirements under the Act. OCC, the Board, and FDIC have submitted the requirements contained on the form entitled “Reporting, Recordkeeping, and Disclosure Requirements Associated with Proprietary Trading and Certain Interests in and Relationships with Covered Funds” to the Office of Management and Budget (OMB) for review. OCC estimates that of the entities under its jurisdiction, there will be 381 respondents with a total estimated annual burden of 28,016 hours (14,386 hours for initial setup and 13,630 hours for ongoing compliance). The Board estimates that of the entities under its jurisdiction, there will be 5,027 respondents with a total estimated annual burden of 2,336,190 hours (968,488 hours for initial setup and 1,367,702 hours for ongoing compliance). FDIC estimates that of the entities under its jurisdiction, there will be 797 respondents with a total estimated annual burden of 28,234 hours (14,165 hours for initial setup and 14,069 hours for ongoing compliance).

Statutory authorization for the rule

The agencies promulgated this final rule under the authority of section 619 of the Dodd-Frank Act, among others. 12 U.S.C. § 1851.

Executive Order No. 12,866 (Regulatory Planning and Review)

As independent regulatory agencies, the Board, FDIC, and SEC, are not subject to the Order. Although OCC is not an independent regulatory agency, it did not discuss the Order in the final rule.

³ CFTC also promulgated a proposed rule on proprietary trading. 77 Fed. Reg. 8332 (Feb. 14, 2012). The rule was finalized on January 31, 2014. 79 Fed. Reg. 5808.