

## US

Morrison &amp; Foerster

**Proprietary trading**

It seems like soon there will be no proprietary trading. It appears likely that some form of “activities” restrictions will part of the future for financial institutions. Maybe not the full Volcker Rule limitations, but restrictions nonetheless. There are various possible permutations of the proposed activities restrictions to choose from – the original (Volcker Rule), the Obama administration’s proposal, the activities restrictions included in the Wall Street Reform and Consumer Protection Act, or House bill (HR 4173), and now the version included in the new bill proposed by Senator Dodd.

The House bill authorises the Federal Reserve to prohibit systemically important companies from engaging in proprietary trading. The House bill also authorises the proposed Financial Services Oversight Council to require a financial institution to terminate certain activities or to divest itself of businesses if these pose a grave threat to the economy.



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The administration’s proposal goes further; it prohibits proprietary trading by regulated institutions, subject to a few narrow exceptions. It also would prohibit regulated institutions from sponsoring and investing in hedge funds and private equity funds. Shortly after the administration released its version of legislative language, Senators Merkley and Levin introduced the PROP Trading Act that would expand upon these prohibited activities. The Merkley-Levin bill would extend restrictions to certain non-bank affiliates. The bill would also include restrictions on banking activities related to asset-backed securities, although these were not well articulated.

The new Dodd bill includes a formulation of these activities restrictions. The bill would require regulatory agencies to issue rules for banks, bank holding companies and their affiliates to prohibit

proprietary trading and to restrict hedge fund and private-equity fund sponsorship. For non-banks under its supervision, the Federal Reserve would be required to adopt similar restrictions. All of these measures seem to be based on the notion that firms that benefit from the federal safety net should not be permitted to engage in speculative transactions that do not provide any public benefit. Of course, many would have differing views about the validity of this premise.

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