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The Volcker Rule: A Comparison

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On December 10 2013, the final regulation implementing the Volcker Rule was adopted by the five US federal bank regulatory agencies. This comes over two years after the publication of the proposed regulation. The text below illustrates the differences between the final and proposed texts.

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This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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Text of the ~~Proposed~~Final Common Rules

(All Agencies)

The text of the ~~proposed~~final common rules appears below:

PART []—PROPRIETARY TRADING AND CERTAIN INTERESTS IN AND RELATIONSHIPS WITH COVERED FUNDS

~~Subpart~~SUBPART A— Authority and Definitions

~~Sec.~~

~~—~~Section 1 Authority, purpose, scope, and relationship to other authorities. ~~[Reserved]~~

Section ~~—~~2 Definitions.

SUBPART B Proprietary Trading

Section ~~—~~3 Prohibition on proprietary trading.

Section ~~—~~4 Permitted underwriting and market making-related activities.

Section ~~—~~5 Permitted risk-mitigating hedging activities.

Section ~~—~~6 Other permitted proprietary trading activities.

~~Section~~ ~~—~~7 ~~Reporting and recordkeeping requirements applicable to~~ 7 Limitations on permitted proprietary trading activities.

Section 8 ~~[Reserved]~~

~~—~~8 ~~Limitations on permitted proprietary trading activities.~~ Section ~~—~~9 ~~[Reserved]~~

SUBPART C Covered Fund Activities and Investments

Section ~~—~~10 Prohibition on acquiring or retaining an ownership interest in and having certain relationships with a covered fund.

Section ~~—~~11 Permitted organizing and offering of a covered fund.

Section ~~—~~12 Permitted investment in a covered fund.

Section ~~—~~13 Other permitted covered fund activities and investments.

~~Section 14 Covered fund activities and investments determined to be permissible~~ 14 Limitations on relationships with a covered fund.

Section

~~15 Internal controls, reporting and recordkeeping requirements applicable to covered fund activities and investments.~~

~~16 Limitations on relationships with a covered fund.~~ 17 15 Other limitations on permitted covered fund activities and investments.

Section 16 [Reserved]

Section 17 [Reserved]

Section 18 [Reserved]

Section 19 [Reserved]

SUBPART D Compliance Program Requirement; Violations

Section 20 Program for ~~monitoring~~ compliance; enforcement.

Section 21 Termination of activities or investments; penalties for violations. ~~Subpart A—~~

APPENDIX A Reporting and Recordkeeping Requirements for Covered Trading Activities

APPENDIX B Enhanced Minimum Standards for Programmatic Compliance

SUBPART A – Authority and Definitions

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

[Reserved.]

§ 2.2 Definitions.

Unless otherwise specified, for purposes of this part:

(a) Affiliate has the same meaning as in section 2(k) of the BHC 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 covered banking entity that [Agency] determines~~

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~~are appropriate, that the covered banking entity uses in the ordinary course of its business in preparing its consolidated financial statements.~~

~~(e) BHC Act means the Bank Holding Company Act of 1956 (12 U.S.C. 1841 et seq.).~~ (d) Bank holding company has the same meaning as in section 2 of the ~~BHC~~Bank Holding Company Act of 1956 (12 U.S.C. 1841).

~~(ec) Banking entity means:~~

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

(i) Any insured depository institution;

(2ii) Any company that controls an insured depository institution;

(3iii) 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

(4iv) Any affiliate or subsidiary of any entity described in paragraphs (ec)(1)(i), (2ii), or (3iii) of this section, ~~other than an affiliate or subsidiary that is:~~

(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;

~~(i) A covered fund that is organized, offered and held by a banking entity pursuant to § __.11 and in accordance with the provisions of subpart C of this part, including the provisions governing relationships between a covered fund and a banking entity; or~~ 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

~~(ii) An entity that is controlled by a covered fund described in paragraph (e)(4)(i) of this section.~~ 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.

~~(fd) Board means the Board of Governors of the Federal Reserve System.~~

~~(g) Buy and purchase each include any contract to buy, purchase, or otherwise acquire. 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.~~
e) CFTC means the Commodity Futures Trading Commission.

~~(h) CFTC means the Commodity Futures Trading Commission.~~

~~(i) Commodity~~ f) Dealer has the same meaning as in section 3(a)(5) of the Exchange Act means the Commodity Exchange Act (7(15 U.S.C. 1 et seq. 78c(a)(5)).

~~(j) [Reserved]~~ (k) Depository institution has the same meaning as in section 3(c) of the Federal Deposit Insurance Act (12 U.S.C. 1813(c)).

~~(h)~~ (i) Derivative.

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

~~(A) 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)), and as those terms are further jointly defined by the CFTC and SEC by joint regulation, interpretation, guidance, or other action, in consultation with the Board pursuant to section 712(d) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (15 U.S.C. 8302(d));~~

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

~~(C) 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));~~

~~(D) 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));~~

~~(E) Any agreement, contract, or transactions 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~~

~~(F) 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:

~~(ii) A derivative does not include:~~ (A) 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

~~(B) 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)).~~

~~(m) 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 ~~Federal Deposit Insurance Corporation~~ FDIC.

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

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

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

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

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

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

~~(t)~~ ~~Nonbank~~Primary financial ~~company supervised by the Board~~regulatory agency has the same meaning specified as in section ~~102 of the Financial Stability Act of 2010~~2(12) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (12 U.S.C. ~~5311~~5301(12)).

~~(s)~~u 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) 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)).

~~(t) Resident of the United States means:~~

~~(1) Any natural person resident in the United States;~~

~~(2) Any partnership, corporation or other business entity organized or incorporated under the laws of the United States or any State;~~

~~(3) Any estate of which any executor or administrator is a resident of the United States;~~

~~(4) Any trust of which any trustee, beneficiary or, if the trust is revocable, any settlor is a resident of the United States;~~

~~(5) Any agency or branch of a foreign entity located in the United States;~~

~~(6) Any discretionary or non-discretionary account or similar account (other than an estate or trust) held by a dealer or fiduciary for the benefit or account of a resident of the United States;~~

~~(7) Any discretionary account or similar account (other than an estate or trust) held by a dealer or fiduciary organized or incorporated in the United States, or (if an individual) a resident of the United States; or~~

~~(8) Any person organized or incorporated under the laws of any foreign jurisdiction formed by or for a resident of the United States principally for the purpose of engaging in one or more transactions described in § __.6(d)(1) or § __.13(e)(1).~~

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

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

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

~~(y) Securities Act means the Securities Act of 1933 (15 U.S.C. 77a et seq.).~~ ~~(zbb)~~ Separate account means an account established and maintained by an insurance company ~~subject to regulation by a State insurance regulator or a foreign insurance regulator~~ 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.

(~~aa~~cc) State means any State, ~~territory or possession of~~ the District of Columbia, the Commonwealth of Puerto Rico, Guam, American Samoa, the United States Virgin Islands, and the District of Columbia Commonwealth of the Northern Mariana Islands.

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

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

~~Subpart~~ SUBPART B — Proprietary Trading

§ .3 Prohibition on proprietary trading.

(a) Prohibition. Except as otherwise provided in this subpart, a ~~covered~~ banking entity may not engage in proprietary trading.

~~(b) Definition of “proprietary trading” and related terms. For purposes of this subpart: (1) Proprietary trading means engaging as principal for the trading account of the covered banking entity in any purchase or sale of one or more covered financial positions. Proprietary trading does not include acting solely as agent, broker, or custodian for an unaffiliated third party financial instruments.~~

~~(2) Trading~~ (b) Definition of trading account.

~~(1)~~ (1) Trading account means any account that is used by a ~~covered~~ banking entity to:

~~(A)~~ (A) ~~Acquire~~ Purchase or ~~take~~ sell one or more ~~covered~~ financial ~~positions~~ instruments principally for the purpose of:

~~(1A)~~ (A) Short-term resale;

~~(2B)~~ (B) Benefitting from actual or expected short-term price movements;

~~(3C)~~ (C) Realizing short-term arbitrage profits; or

~~(4D)~~ (D) Hedging one or more positions resulting from the purchases or sales of financial instruments described in paragraphs (b)(~~2~~1)(i)(A)~~(1)~~, (2B), or (3C) of this section;

~~(Bii) Acquire~~Purchase or ~~take~~sell one or more ~~covered financial positions, other than positions that are foreign exchange derivatives, commodity derivatives, or contracts of sale of a commodity for future delivery, that are~~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 ~~covered~~ banking entity, or any affiliate of the ~~covered~~ banking entity ~~that is a, is an insured depository institution, bank holding company, or savings and loan holding company, and~~ calculates risk-based capital ratios under the market risk capital rule ~~as defined in paragraph (e)(8) of this section;~~ or

~~(Ciii) Acquire~~Purchase or ~~take~~sell one or more ~~covered~~ financial position instruments for any purpose, if the ~~covered~~ banking entity ~~is~~:

~~(1) A dealer or municipal securities dealer that is registered with the SEC under the Exchange Act~~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 position instrument is acquiredpurchased or ~~taken~~sold in connection with the activities ~~of the dealer or municipal securities dealer~~ that require ~~it~~the banking entity to be licensed or registered ~~under that Act;~~as such; or

~~(2) A government securities dealer that is registered, or that has filed notice, with an appropriate regulatory agency (as that term is defined in section 3(a)(34) of the Exchange Act (15 U.S.C. 78c(a)(34)), to the extent the position is acquired or taken in connection with the activities of the government securities dealer that require it to be registered, or to file notice, under that Act;~~

~~(3) A swap dealer that is registered with the CFTC under the Commodity Exchange Act, to the extent the position is acquired or taken in connection with the activities of the swap dealer that require it to be registered under that Act;~~

~~(4) A security-based swap dealer that is registered with the SEC under the Exchange Act, to the extent the position is acquired or taken in connection with the activities of the security-based swap dealer that require it to be registered under that Act; or~~

~~(5B) Engaged~~Is engaged in the business of a dealer, swap dealer, or security-based swap dealer outside of the United States, to the extent the position instrument is acquiredpurchased or ~~taken~~sold in connection with the activities of such business.

~~(ii) 2) Rebuttable presumption for certain positions. An account~~purchases and sales. The purchase (or sale) of a financial instrument by a banking entity shall be presumed to be for the trading account ~~if it is used to acquire or take a covered financial position, other than a covered financial~~

~~position described in~~ of the banking entity under paragraph (b)(~~21~~)(i)(~~B~~) or (~~C~~) of this section; ~~that if~~ the ~~covered~~ banking entity holds ~~for a period of sixty days or less~~ the financial instrument for fewer than sixty days or substantially transfers the risk of the financial instrument within sixty days of the purchase (or sale), unless the ~~covered~~ banking entity can demonstrate, based on all ~~the~~ relevant facts and circumstances, that the ~~covered financial position, either individually or as a category, was not acquired or taken~~ banking entity did not purchase (or sell) the financial instrument principally for any of the purposes described in paragraph (b)(~~21~~)(i)(~~A~~) 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

~~An account shall not be deemed a trading account for purposes of paragraph (b)(2)(i) of this section to the extent that such account is used to acquire or take a position in one or more covered~~ 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 does not include:

(1) Any purchase or sale of one or more financial ~~positions:(A) That arise~~ instruments by a banking entity that arises under a repurchase or reverse repurchase agreement pursuant to which the ~~covered~~ 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;

~~(B) That arise~~ (2) Any purchase or sale of one or more financial instruments by a banking entity that arises under a transaction in which the ~~covered~~ 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;

~~(C) For~~ (3) Any purchase or sale of a security by a banking entity for the ~~bona fide~~ purpose of liquidity management ~~and~~ in accordance with a documented liquidity management plan of the ~~covered~~ banking entity that:

~~(4i)~~ (i) Specifically contemplates and authorizes the particular ~~instrument~~ securities to be used for liquidity management purposes, ~~its profile with respect to market, credit and other~~ the amount, types, and risks of these securities that are consistent with liquidity management, and the liquidity circumstances in which the particular ~~instrument~~ securities may or must be used;

~~(2ii)~~ (ii) Requires that any ~~transaction~~ purchase or sale of securities contemplated and authorized by the plan be principally for the purpose of managing the liquidity of the ~~covered~~ 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;

~~(3iii)~~ (iii) Requires that any ~~position taken~~ securities purchased or sold for liquidity management purposes be highly liquid and limited to ~~financial instruments~~ securities the market, credit, and other risks of which the ~~covered~~ banking entity does not reasonably expect to give rise to appreciable profits or losses as a result of short-term price movements;

~~(4iv)~~ (iv) Limits any ~~position taken~~ securities purchased or sold for liquidity management purposes, together with any other ~~positions taken~~ 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; ~~and~~

~~(5v)~~ (v) Includes written policies and procedures, internal controls, analysis, and independent testing to ensure that the purchase and sale of securities 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 (d)(3) of this section; and

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

~~(D) That are acquired or taken~~ (4) Any purchase or sale of one or more financial instruments by a ~~covered~~ banking entity that is a derivatives clearing organization ~~registered under section 5b of the Commodity Exchange Act (7 U.S.C. 7a-1)~~ or a clearing agency ~~registered with the SEC~~

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~~under section 17A of the Exchange Act (15 U.S.C. 78q-1) in connection with clearing derivatives or securities transactions;~~ 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;

~~(3) Covered~~ (6) Any purchase or sale of one or more financial position instruments by a banking entity, so long as:

~~(i) Covered financial position means any position, including any long, short, synthetic or other position, in;~~ 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

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

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

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

~~(ii) A covered financial position does not include any position that is;~~ The purchase (or sale) satisfies an obligation of the banking entity in connection with a judicial, administrative, self-regulatory organization, or arbitration proceeding;

~~(A) A loan;~~

~~(B) A commodity; or~~

(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

~~(C) Foreign exchange or currency.~~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 [Agency].

(ee) 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;

(24) 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))).

~~(3) Exempted security has the same meaning as in section 3(a)(12)(A) of the Exchange Act (15 U.S.C. 78c(a)(12)(A)).~~5) Derivatives clearing organization means:

~~(4) Foreign insurance regulator means the insurance commission, or a similar official or agency, of one or more countries other than the United States that is engaged in the supervision of insurance companies under foreign insurance law.~~

~~(5) General account means, with respect to an insurance company, all of the assets of the insurance company that are not legally segregated and allocated to separate accounts under applicable State or foreign law.~~

(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) Government securities has the same meaning as in section 3(a)(42) of the Exchange Act (15 U.S.C. 78c(a)(42)).~~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) Market risk capital rule covered position means a covered position as that term is defined for purposes of:~~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) 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) 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) Market risk capital rule covered position and trading position means a financial instrument that is both a covered position and a trading position, as those terms are respectively defined:

(i) In the case of a ~~covered~~-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 ~~covered~~-banking entity; and

(ii) In the case of a ~~covered~~-banking entity that is affiliated with a bank holding company or savings and loan holding company, other than a ~~covered~~ 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.

~~(811)~~ Market risk capital rule means the market risk capital rule that is contained in subpart F of 12 CFR 3, Appendix B, 12 CFR 208, Appendix E, 12 CFR 208 and 225, Appendix E, and or 12 CFR 325, Appendix C, 324, as applicable.

~~(9) Municipal securities has the same meaning as in section 3(a)(29) of the Exchange Act (15 U.S.C. 78e(a)(29)).~~ 12) 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.

~~(10) Security-based swap has the meaning specified in section 3(a)(68) of the Exchange Act (15 U.S.C. 78e(a)(68)).~~

~~(11) Swap has the meaning specified in section 1a(47) of the Commodity Exchange Act (7 U.S.C. 1a(47)).~~

~~(12) State insurance regulator means the insurance commission, or a similar official or agency, of a State that is engaged in the supervision of insurance companies under State insurance law.~~ 13) 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.

§ .4 Permitted underwriting and market making-related activities.

(a) Underwriting activities.

(1) Permitted underwriting activities. The prohibition ~~on proprietary trading~~ contained in § .3(a) does not apply to ~~the purchase or sale of a covered financial position by a covered~~a banking entity ~~that is made in connection with the covered banking entity's~~ underwriting activities conducted in accordance with paragraph (a) of this section.

(2) Requirements. ~~For purposes of~~The underwriting activities of a banking entity are permitted under paragraph (a)(1) of this section, ~~a purchase or sale of a covered financial position shall be deemed to be made in connection with a covered banking entity's underwriting activities~~ only if:

(i) ~~The covered 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) 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, and 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 type of security;

(iii) The banking entity has established ~~the~~and implements, maintains, and enforces an internal compliance program required by subpart D ~~of this part~~ that is reasonably designed to ensure the ~~covered~~ banking entity's compliance with the requirements of paragraph (a)~~(2)~~ of this section, including reasonably designed written policies and procedures, internal controls, analysis and independent testing; identifying and addressing;

~~(ii) The covered financial position is a security;~~(A) The products, instruments or exposures each trading desk may purchase, sell, or manage as part of its underwriting activities;

~~(iii) The purchase or sale is effected solely in connection with a distribution of securities for which the covered banking entity is acting as underwriter;~~

~~(iv) The covered banking entity is:~~

~~(A) With respect to a purchase or sale effected in connection with a distribution of one or more covered financial positions that are securities, other than exempted securities, security-based swaps, commercial paper, bankers' acceptances, or commercial bills;~~

~~(1) A dealer that is registered with the SEC under section 15 of the Exchange Act (15 U.S.C. 78 o), or a person that is exempt from registration or excluded from regulation as a dealer thereunder; or~~

~~(2) Engaged in the business of a dealer outside of the United States and subject to substantive regulation of such business in the jurisdiction where the business is located;~~

~~(B) With respect to a purchase or sale effected as part of a distribution of one or more covered financial positions that are municipal securities, a municipal securities dealer that is registered under section 15B of the Exchange Act (15 U.S.C. 78 o 4) or exempt from registration thereunder; or~~

~~(C) With respect to a purchase or sale effected as part of a distribution of one or more covered financial positions that are government securities, a government securities dealer that is registered, or that has filed notice, under section 15C of the Exchange Act (15 U.S.C. 78 o 5) or exempt from registration thereunder;~~

~~(v) The underwriting activities of the covered banking entity with respect to the covered financial position are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties;~~

~~(vi) The underwriting activities of the covered banking entity are designed to generate revenues primarily from fees, commissions, underwriting spreads or other income not attributable to:~~

(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:

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

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

~~(A) Appreciation in the value of covered financial positions related to such activities; or~~ 3) Period of time a security may be held;

~~(B) The hedging of covered financial positions related to such activities; and~~ (C) Internal controls and ongoing monitoring and analysis of each trading desk's compliance with its limits; and

(D) 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;

~~(viiiiv)~~ The compensation arrangements of persons performing ~~underwriting~~ the activities described in paragraph (a) of this section are designed not to reward or incentivize prohibited proprietary ~~risk-taking~~ trading; and

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

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

(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 ~~magnitude of the offering and 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 paragraph (a) of this section, underwriter means:

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

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

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

(C) ~~To manage~~ Manage a distribution of securities for or on behalf of ~~such~~ the issuer or selling security holder; ~~and~~ or

(ii) A person who has ~~an agreement with another person described in paragraph (a)(4)(i) of this section to engage~~ 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 paragraph (a) of this section, 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 paragraph (a) of this 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 paragraph (a) of this section, 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 ~~on proprietary trading~~ contained in § __.3(a) does not apply to ~~the purchase or sale of a covered financial position by a covered~~a banking entity ~~that is made in connection with the covered banking entity's~~ market making-related activities conducted in accordance with paragraph (b) of this section.

(2) Requirements. ~~For purposes of paragraph (b)(1) of this section, a purchase or sale of a covered financial position shall be deemed to be made in connection with a covered banking entity's~~The market making-related activities of a banking entity are permitted under paragraph (b)(1) of this section only if:

(i) ~~The covered~~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-maker inventory are designed not to exceed, on an ongoing basis, the reasonably expected near term demands of clients, customers, or counterparties, based on:

(A) 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) The banking entity has established ~~the~~and implements, maintains, and enforces an internal compliance program required by subpart D that is reasonably designed to ensure the covered banking entity's compliance with the requirements of paragraph (b)(2) of this section, including reasonably designed written policies and procedures, internal controls, analysis and independent testing; identifying and addressing:

~~(ii) The trading desk or other organizational unit that conducts the purchase or sale holds itself out as being willing to buy and sell, including through entering into long and short positions in, the covered financial position for its own account on a regular or continuous basis;~~A) The financial instruments each trading desk stands ready to purchase and sell in accordance with paragraph (b)(2)(i) of this section;

~~(iii) The market making-related activities of the trading desk or other organizational unit that conducts the purchase or sale are, with respect to the covered financial position, designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties;~~

(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; 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 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) 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 the basis for any temporary or permanent increase to a trading desk's limit(s) is consistent with the

requirements of paragraph (b) of this section, and independent review of such demonstrable analysis and approval;

(iv) ~~The covered banking entity is:~~ 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;

~~(A) With respect to a purchase or sale of one or more covered financial positions that are securities, other than exempted securities, security-based swaps, commercial paper, bankers' acceptances, or commercial bills:~~

~~(1) A dealer that is registered with the SEC under section 15 of the Exchange Act (15 U.S.C. 78o), or a person that is exempt from registration or excluded from regulation as a dealer thereunder; or~~

~~(2) Engaged in the business of a dealer outside of the United States and subject to substantive regulation of such business in the jurisdiction where the business is located;~~

~~(B) With respect to a purchase or sale of one or more covered financial positions that are swaps:~~

~~(1) A swap dealer that is registered with the CFTC under the Commodity Exchange Act (7 U.S.C. 1a) or a person that is exempt from registration thereunder; or~~

~~(2) Engaged in the business of a swap dealer outside the United States and subject to substantive regulation of such business in the jurisdiction where the business is located;~~

~~(C) With respect to a purchase or sale of one or more covered financial positions that are security-based swaps:~~

~~(1) A security-based swap dealer that is registered with the SEC under section 15F of the Exchange Act (15 U.S.C. 78 o-10) or a person that is exempt from registration thereunder; or~~

~~(2) Engaged in the business of a security-based swap dealer outside of the United States and subject to substantive regulation of such business in the jurisdiction where the business is located;~~

~~(D) With respect to a purchase or sale of one or more covered financial positions that are municipal securities, a municipal securities dealer that is registered under section 15B of the Exchange Act (15 U.S.C. 78 o-4) or a person that is exempt from registration thereunder; or~~

~~(E) With respect to a purchase or sale of one or more covered financial positions that are government securities, a government securities dealer that is registered, or that has filed notice, under section 15C of the Exchange Act (15 U.S.C. 78 o-5) or a person that is exempt from registration thereunder;~~

~~(v) The market making-related activities of the trading desk or other organizational unit that conducts the purchase or sale are designed to generate revenues primarily from fees, commissions, bid/ask spreads or other income not attributable to:~~

~~(A) Appreciation in the value of covered financial positions it holds in trading accounts; or~~

~~(B) The hedging of covered financial positions it holds in trading accounts;~~

~~(vi) The market making-related activities of the trading desk or other organizational unit that conducts the purchase or sale are consistent with the commentary provided in Appendix B; and (vii) The compensation arrangements of persons performing the market making-related activities described in paragraph (b) of this section are designed not to reward or incentivize prohibited proprietary ~~risk-taking~~ trading; and~~

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

(3) ~~Market making-related hedging~~Definition of client, customer, and counterparty. For purposes of paragraph (b)(1) of this section, ~~a purchase or sale of a covered financial position shall also be deemed to be made in connection with a covered banking entity'~~ 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 activities if services by obtaining such services, responding to quotations, or entering into a continuing relationship with respect to such services, provided that:

(i) ~~The covered financial position is purchased or sold to reduce the specific risks to the covered banking entity in connection with and related to individual or aggregated positions, contracts, or other holdings acquired pursuant to paragraph (b) of this section; and~~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 § __.20(d)(1) of subpart D, 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

~~(ii) The purchase or sale meets all of the requirements described in § __.5(b) and, if applicable, § __.5(c).~~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 paragraph (b) of this 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. For the purposes of paragraph (b) of this section, market-maker inventory 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.

§ __.5 Permitted risk-mitigating hedging activities.

(a) Permitted risk-mitigating hedging activities. The prohibition ~~on proprietary trading~~ contained in § __.3(a) does not apply to the ~~purchase or sale of a covered financial position by a covered~~risk-mitigating hedging activities of a banking entity ~~that is made~~ in connection with and related to individual or aggregated positions, contracts, or other holdings of ~~a covered~~

the banking entity and ~~is~~ designed to reduce the specific risks to the ~~covered~~ banking entity in connection with and related to such positions, contracts, or other holdings.

(b) Requirements. ~~For purposes of~~The risk-mitigating hedging activities of a banking entity are permitted under paragraph (a) of this section, ~~a purchase or sale of a covered financial position shall be deemed to be in connection with and related to individual or aggregated positions, contracts, or other holdings of a covered banking entity and designed to reduce the specific risks to the covered banking entity in connection with and related to such positions, contracts, or other holdings~~ only if:

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

(i) Reasonably designed written policies and procedures regarding the ~~instruments~~positions, techniques and strategies that may be used for hedging, ~~internal~~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) Internal controls and ongoing monitoring, management, and authorization procedures, including relevant escalation procedures; and ~~independent testing~~;

(iii) 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) The ~~purchase or sale~~risk-mitigating hedging activity:

(i) Is ~~made~~conducted in accordance with the written policies, procedures, and internal controls ~~established by the covered banking entity pursuant to subpart D of this part~~required under this section;

(ii) ~~Hedges or otherwise~~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 ~~individual or aggregated~~identified positions, contracts, or other holdings of a ~~covered~~the banking entity; ~~(iii) Is reasonably correlated~~, based upon the facts and circumstances of the identified underlying and hedging positions, contracts or other holdings and the risks and liquidity ~~of those positions, to the risk or risks the purchase or sale is intended to hedge or otherwise mitigate~~thereof;

(~~iv~~iii) Does not give rise, at the inception of the hedge, to any significant exposures that were not already present in the individual or aggregated positions, contracts, or other holdings of a covered banking entity and that are not new or additional risk that is not itself hedged contemporaneously in accordance with this section;

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

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

(B) ~~Maintains a reasonable level of correlation~~ 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 of those positions, to the risk or risks the purchase or sale is intended to hedge or otherwise mitigate thereof; and

(C) ~~Mitigates any significant exposure arising out of the hedge after inception; and~~ 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) of this section and is not prohibited proprietary trading; and

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

(c) Documentation requirement. ~~With~~

(1) A banking entity must comply with the requirements of paragraphs (c)(2) and (c)(3) of this section with respect to any purchase, or sale, or series of purchases or sales conducted by a covered banking entity pursuant to this § 5 of financial instruments made in reliance on this section for risk-mitigating hedging purposes that is ~~established at a level of organization that is different than the level of organization~~;

(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 purchase, sale, or series of purchases or sales are designed to reduce, the covered 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 §

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, document, at the time and contemporaneously with the purchase, or sale, or series of purchases or sales are conducted document:

(4i) The specific, identifiable risk-mitigating purpose of the purchase, sale, or series of purchases or sales; (2s) The risks of the individual or aggregated identified positions, contracts, or other holdings of a covered the banking entity that the purchase, or sale, or series of purchases or sales are is designed to reduce;

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

(3iii) The level of organization 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 paragraph (c) of this section for a period that is no less than

five years in a form that allows the banking entity to promptly produce such records to [Agency] on request, or such longer period as required under other law or this part.

§ 6.6 Other permitted proprietary trading activities.

(a) Permitted trading in domestic government obligations. ~~(1) The prohibition on proprietary trading contained in § 3.3(a) does not apply to the purchase or sale by a covered banking entity of a covered financial position instrument that is:~~

~~(1) An obligation of, or issued or guaranteed by, the United States or any agency thereof;~~

~~(2) An obligation, participation, or other instrument of, or issued by 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.); or~~

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

~~(2) An obligation or other instrument described in paragraphs (a)(1)(i), (ii) or (iii) of this section shall include both general obligations and limited obligations, such as revenue bonds. 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 ~~on behalf of customers.~~ in foreign government obligations.

(1) Affiliates of foreign banking entities in the United States. The prohibition ~~on proprietary trading~~ contained in § __.3(a) does not apply to the purchase or sale of a ~~covered financial position by a covered banking entity on behalf of customers.~~ 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:

~~(2) For purposes of paragraph (b)(1) of this section, a purchase or sale of a covered financial position by a covered banking entity shall be considered to be on behalf of customers if:~~

~~(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 § __.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.

~~(i) The~~1) Fiduciary transactions. The prohibition contained in § __.3(a) does not apply to the purchase or sale:~~(A) Is conducted~~of financial instruments by a ~~covered~~ banking entity acting as ~~investment adviser, commodity trading advisor, trustee, or in a similar fiduciary capacity for a customer;~~ so long as:

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

~~(C) Involves solely covered financial positions of which the customer, and not the covered banking entity or any subsidiary or affiliate of the covered banking entity, is beneficial owner (including as a result of having long or short exposure under the relevant covered~~ii) The banking entity does not have or retain beneficial ownership of the financial ~~position);~~instruments.

~~(ii) The covered~~2) Riskless principal transactions. The prohibition contained in § __.3(a) does not apply to the purchase or sale of financial instruments by a banking entity ~~is~~ acting as riskless principal in a transaction in which the ~~covered~~ banking entity, after receiving an order to purchase (or sell) a ~~covered~~ financial ~~position~~instrument from a customer, purchases (or sells) the ~~covered~~ financial ~~position~~instrument for its own account to offset a contemporaneous sale to (or purchase from) the customer; ~~or.~~

~~(iii) The covered banking entity is an insurance company that purchases or sells a covered financial position for a separate account, if:~~

~~(A) The insurance company is directly engaged in the business of insurance and subject to regulation by a State insurance regulator or foreign insurance regulator;~~

~~(B) The insurance company purchases or sells the covered financial position solely for a separate account established by the insurance company in connection with one or more insurance policies issued by that insurance company;~~

~~(C) All profits and losses arising from the purchase or sale of a covered financial position are allocated to the separate account and inure to the benefit or detriment of the owners of the insurance policies supported by the separate account, and not the insurance company; and~~

~~(D) The purchase or sale is conducted in compliance with, and subject to, the insurance company investment and other laws, regulations, and written guidance of the State or jurisdiction in which such insurance company is domiciled.~~(e) Permitted trading by a regulated insurance company. The prohibition ~~on proprietary trading~~ contained in § __.3(a) does not apply to the purchase or sale of ~~a covered~~ financial ~~position by~~ instruments by a banking entity that is an insurance company or any affiliate of an insurance company if:

(1) The insurance company ~~is directly engaged in the business of insurance and subject to regulation by a State insurance regulator or foreign insurance regulator;~~(2) The insurance company or its affiliate purchases or sells the ~~covered~~ financial ~~position~~ instruments solely for ~~the~~:

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

(3i) 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

(43) 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 ~~(e)~~(32) of this section is insufficient to protect the safety and soundness of the covered banking entity, or ~~of~~ the financial stability of the United States.

~~(d)~~ Permitted trading ~~outside of the United States.~~ activities of foreign banking entities.

(1) The prohibition ~~on proprietary trading~~ contained in § __.3(a) does not apply to the purchase or sale of ~~a covered~~ financial ~~position~~ instruments by a ~~covered~~ banking entity if:

(i) The ~~covered~~ 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~~ any State;

(ii) The purchase or sale ~~is conducted~~ 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 ~~occurs solely outside of the United States~~ meets the requirements of paragraph (e)(3) of this section.

(2) A purchase or sale ~~shall be deemed to be conducted~~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 ~~covered~~ banking entity that is a foreign banking organization, the banking entity ~~is a~~meets the qualifying foreign banking organization ~~and is conducting the purchase or sale in compliance with subpart B~~requirements of section 211.23(a), (c) or (e) of the Board's Regulation K (12 CFR ~~211.20 through 211.30~~)211.23(a), (c) or (e), as applicable; or

(B) With respect to a ~~covered~~ banking entity that is not a foreign banking organization, the ~~covered~~ 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:

(A1) Total assets of the ~~covered~~ banking entity held outside of the United States exceed total assets of the ~~covered~~ banking entity held in the United States;

(B2) Total revenues derived from the business of the ~~covered~~ banking entity outside of the United States exceed total revenues derived from the business of the ~~covered~~ banking entity in the United States; or

(C3) Total net income derived from the business of the ~~covered~~ banking entity outside of the United States exceeds total net income derived from the business of the ~~covered~~ banking entity in the United States.

(3) A purchase or sale ~~shall be deemed to have occurred solely outside of the United States~~by a banking entity is permitted for purposes of paragraph (e) of this section only if:

~~(i) The covered banking entity conducting the purchase or sale is not organized under the laws of the United States or of one or more States;~~

~~(ii) No party to the purchase or sale is a resident of the United States;~~

~~(iii) No personnel of the covered banking entity who is directly involved in the purchase or sale is physically located in the United States; and~~

~~(iv) The purchase or sale is executed wholly outside of the United States.~~

~~§ 2.7 Reporting and recordkeeping requirements applicable to trading activities.~~

~~A covered banking entity engaged in any proprietary trading activity permitted under §§ 2.4 through 2.6 shall comply with:~~

~~(a) The reporting and recordkeeping requirements described in Appendix A to this part, if the covered banking entity has, together with its affiliates and subsidiaries, trading assets and liabilities the average gross sum of which (on a worldwide consolidated basis) is, as measured as of the last day of each of the four prior calendar quarters, equal to or greater than \$1 billion;~~
i) The banking entity engaging as principal in the purchase or sale (including any 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;

(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) The recordkeeping requirements required under § 2.20 and appendix C to this part, as applicable; and~~
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

~~(e) Such other reporting and recordkeeping requirements as [Agency] may impose to evaluate the covered banking entity's compliance with this subpart.~~ 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 paragraph (e) of this section, 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.

(5) For purposes of paragraph (e) of this section, 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 paragraph (e) of this section, 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.

§ ___.87 Limitations on permitted proprietary trading activities.

(a) No transaction, class of transactions, or activity may be deemed permissible under §§ ___.4 through ___.6 if the transaction, class of transactions, or activity would:

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

(2) Result, directly or indirectly, in a material exposure by the ~~covered~~ 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 ~~covered~~ 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 ~~covered~~ banking entity and its clients, customers, or counterparties exists if the ~~covered~~ banking entity engages in any transaction, class of transactions, or activity that would involve or result in the ~~covered~~ 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, ~~unless: (1) Timely and effective disclosure and opportunity to negate or substantially mitigate 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, ~~for which a conflict of interest may arise, the covered~~ the banking entity:

(i) ~~Makes~~ 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

~~(ii)B) Makes such~~ Such disclosure ~~explicitly and effectively, and 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

(2)ii) Information barriers. ~~The covered banking entity has~~ 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 ~~covered~~ 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 ~~covered~~ 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 ~~covered~~ 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 ~~covered~~ banking entity, significantly increase the likelihood that the ~~covered~~ banking entity would incur a substantial financial loss or would ~~fail~~ 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 ~~covered~~ banking entity, significantly increase the likelihood that the ~~covered~~ banking entity would incur a substantial financial loss or would ~~fail~~ pose a threat to the financial stability of the United States.

§ .8 [Reserved]

§ .9 [Reserved]

~~Subpart~~ SUBPART C— Covered Funds Activities and Investments

§ .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 ~~covered~~ 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 [Agency]; 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) ~~Definitions. For purposes~~ Definition of covered fund.

(1) Except as provided in paragraph (c) of this part:~~(1) Covered~~ 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) ~~A~~ Any commodity pool, ~~as defined in~~ 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 4.7 (a)(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 4.7(a)(3); or

(iii) ~~Any issuer, as defined in section 2(a)(22) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(22)), that is organized or offered outside of the United States that would be a covered fund as defined in paragraphs (b)(1)(i), (ii), or (iv) of this section, were it organized or offered under the laws, or offered to one or more residents,~~ 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 one or more States; and 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.

~~(iv) Any such similar fund as~~ (c) Notwithstanding paragraph (b) of this section, unless the appropriate Federal banking agencies, the SEC, and the CFTC ~~may determine, by rule, as provided in section 13(b)(2) of the BHC Act.~~ 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 § .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 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) of this section and the assets or holdings of which are comprised solely of:

(A) Loans as defined in § __.2(s) 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 paragraph (c)(8) of this section, 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 paragraph (c)(8) of this section;

(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 paragraph (c)(8) of this section 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) of this section, 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) of this section, 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 § .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 § .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 [Agency] 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)).

~~(3) Ownership interest.~~ (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 ~~(including, without limitation, a share, equity security, warrant, option, general partnership interest, limited partnership interest, membership interest, trust certificate, or other similar instrument) in a covered fund, whether voting or nonvoting, or any derivative of such 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 (d)(6)(i)(F) of this section.

(ii) Ownership interest does not include, ~~with respect to a covered fund:~~

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

~~(A)~~ The sole purpose and effect of the interest is to allow the ~~covered banking~~ entity (or ~~the affiliate, subsidiary 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

~~covered banking~~ entity (or ~~the affiliate, subsidiary or~~employee or former employee thereof), provided that the ~~covered banking~~ entity (or ~~the affiliate, subsidiary or~~employee or former employee thereof) may be obligated under the terms of such interest to return profits previously received;

(~~2B~~) All such profit, once allocated, is distributed to the ~~covered banking~~ entity (or ~~the affiliate, subsidiary or~~employee or former employee thereof) promptly after being earned or, if not so distributed, ~~the reinvested profit of the covered banking~~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 ~~the affiliate, subsidiary or~~employee or former employee thereof) does not share in the subsequent ~~profits and losses~~investment gains of the covered fund;

(~~3~~The C) Any amounts invested in the covered banking fund, including any amounts paid by the entity (or ~~the affiliate, subsidiary or~~employee or former employee thereof) ~~does not provide funds to the covered fund~~ in connection with ~~acquiring or retaining this interest~~obtaining the restricted profit interest, are within the limits of § .12 of this subpart; and

(~~4D~~) The interest is not transferable by the ~~covered banking~~ entity (or ~~the affiliate, subsidiary or~~employee or former employee thereof) except to ~~another an~~ affiliate ~~or subsidiary~~ 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.

(~~47~~) Prime brokerage transaction means ~~one or more products or services provided by a covered banking entity to a covered fund, such~~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, ~~or~~ financing, or data, operational, and ~~portfolio management~~administrative support.

(~~5~~) ~~Sponsor, with respect to a covered fund, means:~~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 ~~of~~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.

~~(610)~~ Trustee.

(i) For purposes of paragraph (d)(9) of this section and § __.11 of subpart C, a trustee does not include ~~a~~:

(A) A trustee that does not exercise investment discretion with respect to a covered fund, including a ~~directed~~-trustee, as that ~~term is used in~~ 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 ~~covered banking~~-entity that directs a person ~~identified~~described in paragraph ~~(b)(610)~~(i) of this section, or that possesses authority and discretion to manage and control the ~~assets~~investment decisions of a covered fund for which such person ~~identified in paragraph (b)(6)(i) of this section~~ serves as trustee, shall be considered to be a trustee of such covered fund.

§ __.11 Permitted organizing and offering ~~of~~ underwriting, and market making with respect to a covered fund.

~~Section __.10(a) does not prohibit a covered banking entity from~~(a) Organizing and offering a covered fund in general. Notwithstanding § __.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:

~~(a1)~~ The ~~covered~~-banking entity (or an affiliate thereof) provides bona fide trust, fiduciary, investment advisory, or commodity trading advisory services;

~~(b2)~~ 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 ~~covered~~ banking entity (or an affiliate thereof), pursuant to a credible written plan or similar documentation outlining how the ~~covered~~-banking entity or such affiliate intends to provide advisory or similar services to its customers through organizing and offering such fund;

~~(e3)~~ The ~~covered~~-banking entity ~~does~~and its affiliates do not acquire or retain an ownership interest in the covered fund except as permitted under § __.12 of this subpart;

- (~~d~~4) The ~~covered~~-banking entity complies and its affiliates comply with the ~~restrictions under requirements of~~ § ~~__~~.1614 of this subpart;
- (~~e~~5) The ~~covered~~-banking entity does 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;
- (~~f~~6) The covered fund, for corporate, marketing, promotional, or other purposes:
- (~~4~~i) Does not share the same name or a variation of the same name with the ~~covered~~-banking entity (or an affiliate ~~or subsidiary~~ thereof); and
- (~~2~~i) Does not use the word “bank” in its name;
- (~~g~~7) No director or employee of the ~~covered~~-banking entity (or an affiliate thereof) takes or retains an ownership interest in the covered fund, except for any director or employee of the ~~covered~~-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
- (~~h~~8) The ~~covered~~-banking entity:
- (~~4~~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):
- (~~i~~A) That “any losses in [such covered fund] will be borne solely by investors in [the covered fund] and not by [the ~~covered~~-banking entity ~~and~~ or its affiliates ~~or subsidiaries~~]; therefore, [the ~~covered~~-banking entity’s ~~and its affiliates’ or subsidiaries’~~ s] losses in [such covered fund] will be limited to losses attributable to the ownership interests in the covered fund held by [the ~~covered~~ banking entity] and ~~its affiliates or subsidiaries~~ in their any affiliate in its capacity as investor investor in the [covered fund] or as beneficiary of a restricted profit interest held by [the banking entity] or any affiliate”;
- (~~ii~~B) That such investor should read the fund offering documents before investing in the covered fund;
- (~~iii~~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
- (~~iv~~D) The role of the ~~covered~~-banking entity and its affiliates, ~~subsidiaries~~ and employees in sponsoring or providing any services to the covered fund; and
- (~~2~~i) 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 ~~or subsidiaries~~.

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(b) Organizing and offering an issuing entity of asset-backed securities.

(1) Notwithstanding § __.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 (a)(8) of this section.

(2) For purposes of this paragraph (b) of this section, 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. 78o-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.78o-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;

(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; 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 § __.12(a)(2)(ii) and § __.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 § __.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 paragraph (c) of this section, are included in the calculation of all ownership interests under § __.12(a)(2)(iii) and § __.12(d) of this subpart.

§ __.12 Permitted investment in a covered fund.

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

(1) ~~The~~Notwithstanding the prohibition contained in § __.10(a) ~~does not apply with respect to a covered of this subpart, a~~ banking entity acquiring may acquire and ~~retaining any~~retain an ownership interest in a covered fund that the ~~covered~~ banking entity or an affiliate ~~or subsidiary~~ thereof organizes and offers, pursuant to § __.11, for the purposes of:

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

(ii) De minimis investment. Making and retaining an investment in the covered fund ~~that does not exceed 3 percent of the total outstanding ownership interests in the fund~~ subject to the limits contained in paragraphs (a)(2)(ii) and (a)(2)(iii) of this section.

(2) ~~Ownership~~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 ~~covered~~ 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 ~~covered~~ banking entity in any the covered fund ~~under § __.12~~ to the amount permitted in paragraph (a)(2)(i)(B) of this section; and

(B) ~~May not exceed 3 percent of the total amount or value of outstanding ownership interests of the fund not~~ 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; ~~and~~

(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), 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. 78o-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 ~~covered~~ banking entity and its affiliates in all covered funds acquired or retained under ~~§ __.12~~this section may not exceed 3 percent of the tier 1 capital of the ~~covered~~ banking entity, as provided under paragraph (c) of this section, and shall be calculated as of the last day of each calendar quarter.

~~(b) Limitations on investments in a single covered fund. For purposes of determining whether a covered banking entity is in compliance with the limitations and restrictions on permitted investments in covered funds contained in paragraph (a) of this section, a covered banking entity shall calculate its amount and value of a permitted investment in a single covered fund as follows:~~
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. ~~The~~

(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:~~(i) Controlled investments. Any~~
any ownership interest held under § __.12 ~~by any entity that is controlled, directly or indirectly, by the covered banking entity for purposes of this part; and~~directly by the banking entity, including any affiliate of the banking entity.

~~(ii) Noncontrolled investments. The pro rata share of any ownership interest held under § __.12 by any covered fund that is not controlled by the covered banking entity but in which the covered banking entity owns, controls, or holds with the power to vote more than 5 percent of the voting shares.~~
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 § __.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 amount of permitted ownership interests in a single covered fund. ~~For~~Except as provided in paragraph (b)(3) or (4), for purposes of determining whether an investment in a single covered fund ~~does not exceed 3 percent of the total outstanding ownership interests of the fund~~complies with the restrictions on ownership interests under paragraph (a)(2)(i)(B) and (a)(2)(ii)(A) of this section:

~~(i) The aggregate amount of all ownership interests of the covered banking entity shall be the greater of (without regard to committed funds not yet called for investment):~~

~~(A) The value of any investment or capital contribution made with respect to all ownership interests held under § __.12 by the covered banking entity in the covered fund, divided by the value of all investments or capital contributions, respectively, made by all persons in that covered fund; or~~

~~(B) The total number of ownership interests held under § 12 by the covered banking entity in a covered fund divided by the total number of ownership interests held by all persons in that covered fund.~~ 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), 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) Inclusion of certain parallel investments. To the extent that a covered banking entity is contractually obligated to directly invest in, or is found to be acting in concert through knowing participation in a joint activity or parallel action toward a common goal of investing in, one or more investments with a covered fund that is organized and offered by the covered banking entity, whether or not pursuant to an express agreement, such investments shall be included in any calculation required under paragraph (a)(2) of this section.~~
Fund-of-funds investments. If a banking entity organizes and offers a covered fund pursuant to § .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.

~~(3) Timing of single covered fund investment calculation. The aggregate amount of all ownership interests of a covered banking entity in a single covered fund may at no time exceed the limits in this paragraph after the conclusion of the period provided in paragraph (a)(2)(i)(B) of this section.~~

~~(4) Methodology and standards for calculation. For purposes of determining the amount or value of its investment in a covered fund under this paragraph (b), a covered banking entity must calculate its investment in the same manner and according to the same standards utilized by the covered fund for determining the aggregate value of the fund's assets and ownership interests.~~

(c) Aggregate permitted investments in all covered funds.

(1) For purposes of ~~determining the aggregate value of all permitted investments in all covered funds by a covered banking entity under~~ paragraph (a)(2)(~~hiii~~) of this section, the aggregate value of all ownership interests held by ~~that covered~~ a banking entity shall be the sum of ~~the value of each investment in a covered fund held under § 12, as determined in accordance with applicable accounting standards~~ 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 § 10(d)(6)(ii) of this subpart), on a historical cost basis.

(2) Calculation of tier 1 capital. For purposes of ~~determining compliance with~~ paragraph (a)(2)(~~hiii~~) of this section:

(i) Entities that are required to hold and report tier 1 capital. If a ~~covered~~ banking entity is required to calculate and report tier 1 capital, the ~~covered~~ banking entity's tier 1 capital shall be equal to the amount of tier 1 capital ~~calculated by that covered~~ of the banking entity as of the last day of the most recent calendar quarter ~~that has ended~~, as reported to its primary financial regulatory agency, ~~as defined in section 2(12) of the Dodd-Frank Wall Street Reform and Consumer Protection Act~~; and

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

(A) In the case of a ~~covered~~ 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 ~~pursuant to~~ in the manner described in paragraph (c)(2)(i) of this section;

(B) In the case of a ~~covered~~ 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 ~~covered~~ 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, ~~pursuant to~~ 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 ~~covered~~ 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.

~~(3) A covered banking entity's aggregate permitted investment in all covered funds shall be calculated as of the last day of each calendar quarter.~~ 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 (c)(2)(ii) of this section.

(d) Capital treatment for a permitted investment in a covered fund. For purposes of calculating ~~capital pursuant to compliance with~~ the applicable regulatory capital ~~rules~~ requirements, a ~~covered~~ banking entity shall deduct ~~the aggregate value of all permitted investments in all covered funds made or retained by a covered banking entity pursuant to this section (as determined under paragraph (c)(1) of this section)~~ 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 § .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 § .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 ~~covered~~ banking entity, the Board may extend the period ~~of time to meet the requirements~~ under ~~paragraphs~~ paragraph (a)(2)(i) ~~(A) and (B)~~ 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 ~~covered~~ 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)(~~i~~) of this section.

(2) Factors governing 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:

~~(A) Involve or result in material conflicts of interest between the covered banking entity and its clients, customers or counterparties;~~ ~~(B) Result~~ result, directly or indirectly, in a material exposure by the ~~covered~~ banking entity to high-risk assets or high-risk trading strategies;

~~(C) Pose a threat to the safety and soundness of the covered banking entity; or~~

~~(D) Pose a threat to the financial stability of the United States;~~

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

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

~~(v)~~ v 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 ~~covered~~ banking entity and the financial stability of the United States;

~~(vi)~~ vii The cost to the ~~covered~~ banking entity of divesting or disposing of the investment within the applicable period;

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

~~(viii)~~ (vi) The ~~covered~~ 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) Consultation. In the case of a covered 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 approval of an application by the covered banking entity for an extension under paragraph (e)(1) of this section. (4) Authority to impose restrictions on activities or investment during any extension period. (i) 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 ~~covered~~ 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 ~~(12 U.S.C. 1851)~~ and this part.

~~(ii)~~ (4) Consultation. In the case of a ~~covered~~ 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 ~~imposing conditions on the approval of a request by the covered~~ acting on an application by the banking entity for an extension under paragraph (e)(1) of this section.

§ __.13 Other permitted covered fund activities and investments.

(a) Permitted ~~investments in SBICs and related investments~~ Risk-Mitigating Hedging Activities.

(1) The prohibition contained in § __.10(a) of this subpart does not apply with respect to ~~acquiring or retaining~~ an ownership interest in, ~~or acting as sponsor to,~~ a covered fund acquired or retained by a ~~covered banking entity or an affiliate or subsidiary thereof;~~

~~(1) In one or more small business investment companies, as defined in section 102 of the Small Business Investment Act of 1958 (15 U.S.C. 662);~~

~~(2) That is 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~~

~~(3) That is a qualified rehabilitation expenditure with respect to a qualified rehabilitation 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.~~

~~(b) Permitted risk-mitigating hedging activities.~~

~~(1) The prohibition contained in § 1.10(a) does not apply with respect to an ownership interest in a covered fund by a covered banking entity, provided that the acquisition or retention of the ownership interest is:~~
(i) Made 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 and related to individual or aggregated obligations or liabilities of the covered banking entity that are:

~~(A) Taken by the covered 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, or~~
~~(B) Directly connected to 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; ~~and~~
~~(ii) Designed to reduce the specific risks to the covered banking entity in connection with and related to such obligations or liabilities.~~

(2) Requirements. ~~For purposes of paragraph (b)(1) of this section, acquiring or retaining an ownership interest in a covered fund by a covered banking entity shall be a permissible~~ The risk-mitigating hedging activity activities of a banking entity are permitted under paragraph (a) of this section only if:

(i) The ~~covered~~ banking entity has established ~~the~~ and implements, maintains and enforces an internal compliance program required by subpart D that is reasonably designed to ensure the ~~covered~~ banking entity's compliance with the requirements of this ~~paragraph (b)(2) of this section,~~ including ~~reasonably,~~

(A) Reasonably designed written policies and procedures ~~regarding the instruments, techniques and strategies that may be used for hedging, internal; and~~

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

(ii) The acquisition or retention of anthe ownership interest ~~in a covered fund~~:

(A) Is made in accordance with the written policies, procedures and internal controls ~~established by the covered banking entity pursuant to subpart D~~required under this section;

~~(B) Hedges or otherwise mitigates an exposure to a covered fund through an offsetting exposure to the same covered fund and in the same amount of ownership interest in that covered fund that:~~

~~(1) Arises out of a transaction conducted solely to accommodate a specific customer request with respect to, or~~(2) Is directly connected to itsAt 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 in connection with the compensation arrangement with anthe employee that directly provides investment advisory, commodity trading advisory, or other services to, ~~that~~ the covered fund;

(C) Does not give rise, at the inception of the hedge, to any significant ~~exposures that were not already present in individual or aggregated positions, contracts, or other holdings of a covered banking entity and that are not~~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 ~~covered~~ banking entity ~~that~~;

~~(1) Is consistent with its written hedging policies and procedures;~~

~~(2) Maintains a substantially similar offsetting exposure to the same amount and type of ownership interest, based upon the facts and circumstances of the underlying and hedging positions and the risks and liquidity of those positions, to the risk or risks the purchase or sale is intended to hedge or otherwise mitigate; and~~

~~(3) Mitigates any significant exposure arising out of the hedge after inception; and~~

(iii) The compensation ~~arrangements of persons performing the risk mitigating hedging activities are designed not to reward proprietary risk taking.~~(3) Documentation. With respect to any acquisition or retention of an ownership interest in aarrangement relates solely to the covered fund ~~by a covered~~in which the banking entity or any affiliate has acquired an ownership interest

pursuant to this paragraph ~~(b), the covered banking entity must document, at the time the transaction is conducted:~~

~~(i) The risk-mitigating purpose of the acquisition or retention of an ownership interest in a covered fund;~~

~~(ii) The risks of the individual or aggregated obligation or liability of a covered banking entity that the acquisition or retention of an ownership interest in a covered fund is designed to reduce; and~~

~~(iii) The level of organization that is establishing the hedge, 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 § __.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 ~~covered~~ banking entity only if:

(i) The ~~covered~~ 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 ~~conducted~~ pursuant to paragraph (9) or (13) of section 4(c) of the BHC Act;

(iii) No ownership interest in ~~such~~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 ~~shall be considered to be conducted~~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)

(C) With respect to a ~~covered~~ banking entity that is a foreign banking organization, the ~~covered~~ banking entity ~~is a~~ meets the qualifying foreign banking organization ~~and is conducting the activity in compliance with subpart B~~ Requirements of section 211.23(a), (c) or (e) of the Board's Regulation K (12 CFR ~~211.20 et seq.~~ 211.23(a), (c) or (e)), as applicable; or

(B) With respect to a ~~covered~~ banking entity that is not a foreign banking organization, the ~~covered~~ 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:

(A1) Total assets of the ~~covered~~ banking entity held outside of the United States exceed total assets of the ~~covered~~ banking entity held in the United States;

(B2) Total revenues derived from the business of the ~~covered~~ banking entity outside of the United States exceed total revenues derived from the business of the ~~covered~~ banking entity in the United States; or

(C3) Total net income derived from the business of the ~~covered~~ banking entity outside of the United States exceeds total net income derived from the business of the ~~covered~~ banking entity in the United States.

(3) An ~~activity shall be considered to have occurred solely outside of the United States only if:~~ 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 sold or has been sold pursuant to an offering that does not target residents of the United States.

(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 ~~covered banking entity engaging in the activity is not organized under the laws of the United States or of one or more States;~~ 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) ~~No subsidiary, affiliate, or employee of the covered banking entity that is involved in the offer or sale of an ownership interest in the covered fund is incorporated or physically located in the United States or in one or more States; and~~

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

~~(d) Loan securitizations. The prohibition contained in § __.10(a) does not apply with respect to the acquisition or retention by a covered banking entity of any ownership interest in, or acting as sponsor to, a covered fund that is an issuer of asset-backed securities, the assets or holdings of which are solely comprised of:~~

~~(1) Loans;~~

~~(2) Contractual rights or assets directly arising from those loans supporting the asset-backed securities; and~~

~~(3) Interest rate or foreign exchange derivatives that:~~

~~(i) Materially relate to the terms of such loans or contractual rights or assets; and~~

~~(ii) Are used for hedging purposes with respect to the securitization structure.~~

~~§ __.14 Covered fund activities determined to be permissible.~~

~~(a) The prohibition contained in § __.10(a) does not apply to the acquisition or retention by a covered banking entity of any ownership interest in or acting as sponsor to:~~

~~(1) Bank-owned life insurance. A separate account which is used solely for the purpose of allowing a covered banking entity to purchase an insurance policy for which the covered banking entity is the beneficiary, provided that the covered banking entity that purchases the insurance policy:~~

~~(i) Does not control the investment decisions regarding the underlying assets or holdings of the separate account; and~~

~~(ii) Holds its ownership interest in the separate account in compliance with applicable supervisory guidance regarding bank owned life insurance.~~

~~(2) Certain other covered funds. Any of the following entities that would otherwise qualify as a covered fund:~~

~~(i) A joint venture between the covered banking entity or one of its affiliates and any other person, provided that the joint venture:~~

~~(A) Is an operating company; and~~

~~(B) Does not engage in any activity or make any investment that is prohibited under this part;~~

~~(ii) An acquisition vehicle, provided that the sole purpose and effect of such entity is to effectuate a transaction involving the acquisition or merger of one entity with or into the covered banking entity or one of its affiliates;~~

~~(iii) An issuer of an asset backed security, but only with respect to that amount or value of economic interest in a portion of the credit risk for an asset backed security that is retained by a covered banking entity that is a “securitizer” or “originator” in compliance with the minimum requirements of section 15G of the Exchange Act (15 U.S.C. 78 o-11) and any implementing regulations issued thereunder; 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) ~~A wholly owned subsidiary of the covered banking entity that is;~~ 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.

~~(A) Engaged principally in performing bona fide liquidity management activities described in § 3(b)(2)(iii)(C); and~~

~~(B) Carried on the balance sheet of the covered banking entity; and~~

~~(v) A covered fund that is an issuer of asset backed securities described in § 13(d), the assets or holdings of which are solely comprised of:~~

~~(A) Loans;~~

~~(B) Contractual rights or assets directly arising from those loans supporting the asset backed securities; and~~

~~(C) Interest rate or foreign exchange derivatives that:~~

~~(1) Materially relate to the terms of such loans or contractual rights or assets, and~~

~~(2) Are used for hedging purposes with respect to the securitization structure.~~ 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.

~~(b)~~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 ~~a covered banking entity~~an insurance company, or an affiliate thereof, of any ownership interest in, or ~~acting as sponsor to~~the sponsorship of, a covered fund, ~~but only if such ownership interest is acquired or retained by a covered banking entity (or an affiliate or subsidiary thereof)~~ only if:

~~(1) In the ordinary course of collecting a debt previously contracted in good faith, if the covered banking entity divests the ownership interest within applicable time periods provided for by [Agency]; or~~

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) Pursuant to and in compliance with the conformance or extended transition period authorities provided for in subpart E of the Board's rules implementing section 13 of the BHC Act (12 CFR 248.30 through 248.35);~~

~~§ __.15 Internal controls, reporting and recordkeeping requirements applicable to covered fund activities and investments.~~

~~A covered banking entity engaged in any covered fund activity or making or holding any investment permitted under this subpart shall comply with:~~

~~(a) The internal controls, reporting, and recordkeeping requirements required under § __.20 and appendix C to this part, as applicable; and~~

~~(b) Such other reporting and recordkeeping requirements as [Agency] may deem necessary to appropriately evaluate the covered banking entity's compliance with this subpart.~~The acquisition

and retention of the ownership interest 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 (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.

§ ~~___~~.1614 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 ~~covered~~ 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 § ~~___~~.11, ~~.11 of this subpart, or that continues to hold an ownership interest in accordance with §~~ ___.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 ~~covered~~ 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 ~~covered~~ banking entity may:

(i) Acquire and retain any ownership interest in a covered fund in accordance with the requirements of § ___.11, § ___.12, or § ___.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 ~~covered~~ banking entity (or an affiliate ~~or subsidiary~~ thereof) has taken an ownership interest, if:

(A) The ~~covered~~ banking entity is in compliance with each of the limitations set forth in § ___.11 of this subpart with respect to a covered fund organized and offered by such ~~covered~~ banking entity (or an affiliate ~~or subsidiary~~ thereof);

(B) The chief executive officer (or equivalent officer) of the ~~top-tier affiliate of the covered~~ banking entity certifies in writing annually to [Agency] (with a duty to update the certification if the information in the certification materially changes) that the ~~covered~~ 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 ~~covered~~ banking entity.

(b) Restrictions on transactions with covered funds. A ~~covered~~ 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 § ~~_.11~~, .11 of this subpart, or that continues to hold an ownership interest in accordance with § .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 ~~covered~~ 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 ~~covered~~ banking entity.

§ ~~_.17~~.15 Other limitations on permitted covered fund activities.

(a) No transaction, class of transactions, or activity may be deemed permissible under §§ .11 through ~~_.14 and § ~~_.16~~~~ .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 ~~covered~~ banking entity and its clients, customers, or counterparties;

(2) Result, directly or indirectly, in a material exposure by the ~~covered~~ 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 ~~covered~~ 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 ~~covered~~ banking entity and its clients, customers, or counterparties exists if the ~~covered~~ banking entity engages in any transaction, class of transactions, or activity that would involve or result in the ~~covered~~ 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, ~~unless: (1) Timely and effective disclosure and opportunity to negate or substantially mitigate~~ 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, ~~for which a conflict of interest may arise, the covered~~ the banking entity:

(i) ~~Makes~~ 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

(~~ii~~B) ~~Makes such~~Such disclosure ~~explicitly and effectively, and~~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

(~~2~~i) Information barriers. ~~The covered banking entity has~~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 ~~covered~~ 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 ~~covered~~ 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 ~~covered~~ 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 ~~covered~~ banking entity, significantly increase the likelihood that the ~~covered~~ banking entity would incur a substantial financial loss or would ~~fail~~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 ~~covered~~ banking entity, significantly increase the likelihood that the ~~covered~~ banking entity would incur a substantial financial loss or would ~~fail~~pose a threat to the financial stability of the United States.

§ .16 [Reserved]

§ .17 [Reserved]

§ .18 [Reserved]

§ .19 [Reserved]

~~Subpart~~SUBPART D— — Compliance Program Requirement; Violations

§ __.20 Program for ~~monitoring~~ compliance; ~~enforcement~~ reporting

(a) Program requirement. ~~Except as provided in paragraph (d) of this section, each covered~~ Each banking entity 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 such~~ detail of the compliance program shall be appropriate for the types, size, scope and complexity of activities and business structure of the ~~covered~~ banking entity.

(b) Contents of compliance program. ~~The~~ Except as provided in paragraph (f) of this section, the compliance program required by paragraph (a) of this section, at a minimum, shall include:

(1) ~~Internal-written~~ Written policies and procedures reasonably designed to document, describe, ~~and monitor~~ and limit trading activities subject to subpart B ~~of this part~~ (including those permitted under §§ __.3 to __.6 of subpart B), including setting, monitoring and managing required limits set out in § 4 and § 5, and activities and investments with respect to a covered fund subject to subpart C ~~of this part~~ (including those permitted under §§ __.4 through __.6 or §§ __.11 through __.16) __.14 of subpart C) conducted by the banking

entity to ensure that ~~such~~ 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 ~~and identify potential areas of noncompliance~~ compliance with section 13 of the BHC Act and this part ~~in the covered banking entity's trading activities subject to subpart B of this part and activities and investments with respect to a covered fund subject to subpart C of this part (including those permitted under §§ __.4 through __.6 or §§ __.11 through __.16)~~ 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 ~~for~~ and audit of the effectiveness of the compliance program conducted periodically by qualified personnel of the ~~covered~~ 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) ~~Making and keeping records~~ Records sufficient to demonstrate compliance with section 13 of the BHC Act and this part, which a ~~covered~~ banking entity must promptly provide to [Agency]

upon request and retain for a period of no less than 5 years or such longer period as required by [Agency].

(c) Additional ~~standards~~Standards. ~~(1) In the case of any covered banking entity described in addition to the requirements~~ in paragraph ~~(e)(2b)~~ of this section, the compliance program ~~required by paragraph (a) of this section shall also~~of a banking entity must satisfy the requirements and other standards contained in Appendix ~~C to this part.~~(2) A covered banking entity is subject to paragraph (e)(1) of this sectionB, if:

~~(1)~~ (i) The ~~covered~~ banking entity engages in proprietary trading ~~and~~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) [Agency] notifies the banking entity in writing that it must satisfy the requirements and other standards contained in Appendix B.

(d) Reporting requirements under Appendix A.

(1) A banking entity engaged in proprietary trading activity permitted under subpart B shall comply with the reporting requirements described in 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;

~~(A) Is equal to or greater than \$1 billion; or~~

~~(B) Equals 10 percent or more of its total assets;~~

~~(ii) The covered banking entity invests in, or has relationships with, a covered fund and:~~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

~~(A) The covered banking entity has, together with its affiliates and subsidiaries, aggregate investments in one or more covered funds, the average value of which is, as measured as of the last day of each of the four prior calendar quarters, equal to or greater than \$1 billion; or~~

~~(B) Sponsors or advises, together with its affiliates and subsidiaries, one or more covered funds, the average total assets of which are, as measured as of the last day of each of the four prior calendar quarters, equal to or greater than \$1 billion; or~~

~~(iii) [The Agency] deems it appropriate.~~ iii) [Agency] notifies the banking entity in writing that it must satisfy the reporting requirements contained in 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) Frequency of reporting: Unless [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) shall report the information required by 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 quarter unless [Agency] notifies the banking entity in writing that it must report on a different basis.

(e) Additional documentation for covered funds: Any banking entity that has more than \$10 billion in total consolidated assets 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 §§ .10(c)(1), .10(c)(5), .10(c)(8), .10(c)(9), or .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 §§ .10(c)(12)(i) or .10(c)(12)(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 § .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 § .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.

~~(d) No program required for certain~~ f) Simplified programs for less active banking entities. ~~To the extent that a~~

(1) Banking entities with no covered activities. A banking entity that does not engage in activities or investments prohibited or restricted by pursuant to subpart B or subpart C of this part, a covered banking entity will have satisfied (other than trading activities permitted pursuant to § .6(a) of subpart B) may satisfy the requirements of this section if its existing by establishing

~~the required~~ compliance ~~policies and procedures include measures that are designed to prevent the covered banking entity from~~ program prior to becoming engaged in such activities or making such investments ~~and which require the covered banking entity to develop and provide for the compliance program required under paragraph (a) of this section prior to engaging in such activities or making such investments.~~ (other than trading activities permitted pursuant to § __.6(a) of subpart B).

(2) Banking entities with modest activities. 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 § __.6(a) of subpart B) 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.

§ __.21 Termination of activities or investments; penalties for violations.

(a) Any ~~covered~~ 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) ~~After due notice and an opportunity for hearing, if~~ Whenever [Agency] finds reasonable cause to believe any ~~covered~~ banking entity has engaged in an activity or made an investment ~~described in paragraph (a), the [Agency] may, by order, direct~~ 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, [Agency] 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 ~~the activity and, as relevant, any or all activities under this part and~~ dispose of ~~the~~ any investment.

~~(e) [Reserved]~~

Appendix A: ~~to Part []~~—Reporting and Recordkeeping Requirements for Covered Trading Activities

I. Purpose

This appendix sets forth reporting and recordkeeping requirements that certain ~~covered~~ banking entities must satisfy in connection with the restrictions on proprietary trading set forth in subpart B ~~of this part~~ (“proprietary trading restrictions”). Pursuant to § ~~__~~.7, ~~20(d)~~, this appendix generally applies to a ~~covered~~ banking entity that ~~has~~, together with its affiliates and subsidiaries, ~~has significant~~ trading assets and liabilities ~~the average gross sum of which (on a worldwide consolidated basis) is, as measured as of the last day of each of the four prior calendar quarters, equal to or greater than \$1 billion~~. These entities are required to (i) furnish periodic reports to [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 ~~should~~must be incorporated into the ~~covered~~ banking entity’s internal compliance program under § ~~__~~.20 and ~~appendix C to this part~~Appendix B.

The purpose of this appendix is to assist ~~covered~~ banking entities and [Agency] in:

- (i) Better understanding and evaluating the scope, type, and profile of the ~~covered~~ banking entity’s covered trading activities;
- (ii) Monitoring the ~~covered~~ banking entity’s covered trading activities;
- (iii) Identifying covered trading activities that warrant further review or examination by the ~~covered~~ banking entity to verify compliance with the proprietary trading restrictions;
- (iv) Evaluating whether the covered trading activities of trading ~~units~~desks engaged in market making-related activities subject to § ~~__~~.4(b) are consistent with the requirements governing permitted market making-related activities;
- (v) Evaluating whether the covered trading activities of trading ~~units~~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;
- (vi) Identifying the profile of particular covered trading activities of the ~~covered~~ banking entity, and the individual trading ~~units~~desks of the banking entity, to help establish the appropriate frequency and scope of examination by [Agency] of such activities; and
- (vii) Assessing and addressing the risks associated with the ~~covered~~ banking entity’s covered trading activities.

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

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 § __.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.

In addition to the quantitative measurements required in this appendix, a ~~covered~~ 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 and ~~appendix C to this part~~Appendix B. 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 ~~unit~~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, ~~covered~~ 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 ~~covered~~ banking entity, and to monitor and examine for compliance with the proprietary trading restrictions in this part.

On an ongoing basis, ~~covered~~ banking entities ~~should~~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, ~~should~~must be escalated within the banking entity for review, further analysis, explanation to [Agency], and remediation, where appropriate. ~~Many of the~~The quantitative measurements discussed in this appendix ~~will also~~should be helpful to ~~covered~~ 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:

Covered trading activity means ~~proprietary trading, as defined in paragraph (b)(1) of § __.3~~trading conducted by a trading desk under §§ __.4, __.5, __.6(a), or __.6(b). A banking entity may include trading under §§ __.3(d), __.6(c), __.6(d) or __.6(e).

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

~~(i) Each discrete unit that is engaged in the coordinated implementation of a revenue-generation strategy and that participates in the execution of any covered trading activity; [1]~~

~~(ii) Each organizational unit that is used to structure and control the aggregate risk-taking activities and employees of one or more trading units described in paragraph (i); [2]~~

~~(iii) All trading operations, collectively; and~~

~~(iv) Any other unit of organization specified by [Agency] with respect to a particular banking entity.~~

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

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

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.

III. Reporting and Recordkeeping of Quantitative Measurements

A. Scope of Required Reporting

General scope. ~~The quantitative measurements that must be furnished by a covered banking entity depend on the aggregate size of the covered banking entity's trading activities and the activities in which its trading units engage, as follows:~~

~~(i) With respect to any covered banking entity that is engaged in any covered trading activity, and has trading assets and liabilities the average gross sum of which (on a worldwide consolidated basis) is, as measured as of the last day of each of the four prior calendar quarters, equal to or greater than \$5 billion:(a) Each trading unit of the covered banking entity that is engaged in market-making-related activities~~made subject to § -.4(b)~~this part by §~~ .20 must

furnish the following quantitative measurements for each trading desk of the banking entity, calculated in accordance with this appendix:

• Risk and Position Limits and Usage;

• Risk Factor Sensitivities;

~~• Value-at-Risk and Stress VaR; VaR Exceedance; Risk Factor Sensitivities; Risk and Position Limits; Comprehensive Profit and Loss; Portfolio Profit and Loss; Fee Income and Expense; Spread Profit and Loss; Comprehensive Profit and Loss Attribution; Pay-to-Receive Spread Ratio; Unprofitable Trading Days Based on Comprehensive Profit and Loss and Unprofitable Trading Days Based on Portfolio Profit and Loss; Skewness of Portfolio Profit and Loss and Kurtosis of Portfolio Profit and Loss; Volatility of Comprehensive Profit and Loss and Volatility of Portfolio Profit and Loss; Comprehensive Profit and Loss to Volatility Ratio and Portfolio Profit and Loss to Volatility Ratio; Inventory Risk Turnover; Inventory Aging; and Customer-facing Trade Ratio; and (b) Each trading unit of the covered banking entity that is engaged in permitted trading activity subject to §§ 4(a), 5, or 6(a) must furnish the following quantitative measurements, calculated in accordance with this appendix:~~

~~Value at Risk and Stress VaR; Risk Factor Sensitivities; Risk and Position Limits; Comprehensive Profit and Loss; and~~

~~• Comprehensive Profit and Loss Attribution; and (ii) With respect to any covered banking entity that is engaged in any covered trading activity, and has trading assets and liabilities the average gross sum of which (on a worldwide consolidated basis) is, as measured as of the last day of each of the four prior calendar quarters, equal to or greater than \$1 billion and less than \$5 billion, each trading unit of the covered banking entity that is engaged in market making related activities under § 4(b) must furnish the following quantitative measurement, calculated in accordance with this appendix:~~

• Inventory Turnover;

• Inventory Aging; and

• Customer-Facing Trade Ratio

~~Comprehensive Profit and Loss; Portfolio Profit and Loss; Fee Income and Expense; Spread Profit and Loss; Value at Risk; Comprehensive Profit and Loss Attribution; Volatility of Comprehensive Profit and Loss and Volatility of Portfolio Profit and Loss; and Comprehensive Profit and Loss to Volatility Ratio and Portfolio Profit and Loss to Volatility Ratio. B. Frequency of Required Calculation and Reporting~~

A ~~covered~~ banking entity must calculate any applicable quantitative measurement for each trading day. A ~~covered~~ banking entity must report each applicable quantitative measurement to [Agency] on ~~a monthly basis, or on any other~~ the reporting schedule established in § .20 unless otherwise requested by [Agency]. All quantitative measurements for any calendar month must be reported ~~to [Agency] no later than 30 days after the end of that calendar month or on any other time basis requested by [Agency].~~ [3] within the time period required by § .20.

C. Recordkeeping

A ~~covered~~ banking entity must, for any quantitative measurement furnished to [Agency] pursuant to this appendix and § ~~7.20(d)~~, create and maintain records documenting the preparation and content of these reports, as well as such information as is necessary to permit [Agency] to verify the accuracy of such reports, for a period of 5 years from the end of the calendar year for which the measurement was taken.

IV. Quantitative Measurements

A. Risk-Management Measurements

1. ~~Value at Risk and Stress Value at Risk~~ Risk and Position Limits and Usage

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 portfolio over a specified 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 portfolio over a specified period of time, based on market conditions during a period of significant financial stress.~~ Risk and Position Limits are the constraints that define the amount of risk 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 of the trading desk’s limits that are accounted for by the current activity of the desk. Risk and position limits and their usage are key 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, including “Risk Factor Sensitivities” and “Value-at-Risk and Stress 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) and § .5(b)(1)(i) must meet the applicable requirements under § .4(b)(2)(iii) and § .5(b)(1)(i) 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 are 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.

General Calculation Guidance: ~~Banking entities should compute and report VaR and Stress VaR by employing generally accepted standards and methods of calculation. VaR should reflect a loss in a trading unit 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 should be computed and reported in a manner that is consistent with such regulatory capital requirements. In cases where a trading unit does not have a standalone VaR or Stress VaR calculation but is part of a larger portfolio for which a VaR or Stress VaR calculation is performed, a VaR or Stress VaR calculation that includes only the trading unit's holdings should be performed consistent with the VaR or Stress VaR model and methodology used by the larger portfolio.~~ 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.

Calculation Period: One trading day.

Measurement Frequency: Daily.

2. ~~VaR Exceedance~~

~~Description: For purposes of this appendix, VaR Exceedance is the difference between VaR and Portfolio Profit and Loss, exclusive of Spread Profit and Loss, for a trading unit for any given calculation period.~~

~~Calculation Period: One trading day.~~ 3. Risk Factor Sensitivities

Description: For purposes of this appendix, Risk Factor Sensitivities are changes in a trading ~~unit's Portfolio~~ desk's Comprehensive Profit and Loss, ~~exclusive of Spread Profit and Loss~~, that are expected to occur in the event of a change in ~~a trading unit's "risk factors"~~ (i.e., one or more underlying ~~market~~ variables that are significant sources of the trading ~~unit's~~ desk's profitability and risk).

General Calculation Guidance: A ~~covered~~ banking entity ~~should~~ must report the Risk Factor Sensitivities that are monitored and managed as part of the trading ~~unit's~~ desk's overall risk management policy. The underlying data and methods used to compute a trading ~~unit's~~ desk's Risk Factor Sensitivities ~~should~~ will depend on the specific function of the trading ~~unit's~~ desk and the internal risk management models employed. The number and type of Risk Factor Sensitivities that are monitored and managed by a trading ~~unit's~~ desk, and furnished to [Agency], ~~should~~ will

depend on the explicit risks assumed by the trading ~~unit~~desk. In general, however, reported Risk Factor Sensitivities ~~should be sufficient~~must be sufficiently

granular to account for a preponderance of the expected price variation in the trading ~~unit~~desk's holdings.

Trading ~~units should~~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: ~~sensitivities~~risk factors with respect to the related ~~commodity type (e.g., precious metals, oil and petroleum or agricultural products)~~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: ~~sensitivities~~risk factors with respect to credit ~~spread factors~~spreads that are sufficiently granular to account for specific credit sectors and market segments, the maturity profile of the positions, and ~~sensitivities~~risk factors with respect to interest rates ~~at~~of all relevant maturities;
- Credit-related derivative positions: ~~credit positions~~risk factor sensitivities ~~and, 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 positions: ~~sensitivity to~~risk factors for equity prices and ~~sensitivities~~risk factors that differentiate between important equity market sectors and segments, such as a small capitalization equities and international equities;
- Equity derivative positions: ~~equity position~~risk factor sensitivities ~~and~~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;
- Foreign exchange derivative positions: ~~sensitivities~~risk factors with respect to major currency pairs and maturities, ~~sensitivity~~exposure to interest rates at relevant maturities, ~~and~~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: ~~sensitivities~~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.

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

Calculation Period: One trading day.

~~4. Risk and Position Limits~~

Measurement Frequency: Daily.

3. Value-at-Risk and Stress Value-at-Risk

Description: For purposes of this appendix, ~~Risk and Position Limits are the constraints that define the amount of risk that a trading unit is permitted to take at a point in time, as defined by the covered banking entity for a specific trading unit.~~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 aggregated positions over a specified 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.

General Calculation Guidance: ~~Risk and Position Limits should be reported in the format used by the covered banking entity for the purposes of risk management of each trading unit. 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 should be reported.~~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.

Calculation Period: One trading day.

Measurement Frequency: Daily.

B. Source-of-Revenue Measurements

~~1. Comprehensive Profit and Loss~~

~~Description: For purposes of this appendix, Comprehensive Profit and Loss is the net profit or loss of a trading unit's material sources of trading revenue, including, for example, dividend and interest income and expense, over a specific period of time. A trading unit's Comprehensive Profit and Loss for any given calculation period should generally equal the sum of the trading unit's (i) Portfolio Profit and Loss and (ii) Fee Income.~~

~~General Calculation Guidance: Comprehensive Profit and Loss generally should be computed using data on the value of a trading unit's underlying holdings, the prices at which those holdings were bought and sold, and the value of any fees, commissions, sales credits, spreads, dividends, interest income and expense, or other sources of income from trading activities, whether realized or unrealized. Comprehensive Profit and Loss should not include: (i) compensation costs or other costs required to operate the unit, such as information technology costs; or (ii) charges and adjustments made for internal reporting and management purposes, such as accounting reserves.~~

~~Calculation Period: One trading day.~~

~~2. Portfolio Profit and Loss~~

~~Description: For purposes of this appendix, Portfolio Profit and Loss is a trading unit's net profit or loss on its underlying holdings over a specific period of time, whether realized or unrealized. Portfolio Profit and Loss should generally include any increase or decrease in the market value of a trading unit's holdings, including, for example, any dividend, interest income, or expense of a trading unit's holdings. Portfolio Profit and Loss should not include direct fees, commissions, sales credits, or other sources of trading revenue that are not directly related to the market value of the trading unit's holdings.~~

~~General Calculation Guidance: In general, Portfolio Profit and Loss should be computed using data on a trading unit's underlying holdings and the prices at which those holdings are marked for valuation purposes. Portfolio Profit and Loss should not include: compensation costs or other costs required to operate the trading unit, such as information technology costs; or charges and adjustments made for internal reporting and management purposes, such as accounting reserves.~~

~~Calculation Period: One trading day.~~

~~3. Fee Income and Expense~~

~~Description: For purposes of this appendix, Fee Income and Expense generally includes direct fees, commissions and other distinct income for services provided by or to a trading unit over a specific period of time.~~

~~General Calculation Guidance: Fee Income and Expense should be computed using data on direct fees that are earned by the trading unit for services it provides to clients, customers, or counterparties, such as fees earned for structured transactions or sales commissions and credits earned for fulfilling a customer request, whether realized or unrealized, and similar fees paid by the trading unit to other service providers.~~

~~Calculation Period: One trading day.~~

~~4. Spread Comprehensive Profit and Loss Attribution~~

~~Description: For purposes of this appendix, Spread Profit and Loss is the portion of Portfolio Profit and Loss that generally includes revenue generated by a trading unit from charging higher prices to buyers than the trading unit pays to sellers of comparable instruments over the same period of time (i.e., charging a “spread,” such as the bid-ask spread).~~

~~General Calculation Guidance: Spread Profit and Loss generally should be computed using data on the prices at which comparable instruments are either bought or sold by the trading unit, as well as the turnover of these instruments. Spread Profit and Loss should be measured with respect to both the purchase and the sale of any position, and should include both (i) the spreads that are earned by the trading unit to execute transactions (expressed as positive amounts), and (ii) the spreads that are paid by the trading unit to initiate transactions (expressed as negative amounts). Spread Profit and Loss should be computed by calculating the difference between the bid price or the ask price (whichever is paid or received) and the mid-market price. The mid-market price is the average of bid and ask.~~

~~For some asset classes in which a trading unit is engaged in market-making-related activities, bid-ask or similar spreads are widely disseminated, constantly updated, and readily available, or~~

~~otherwise reasonably ascertainable. For purposes of calculating the Spread Profit and Loss attributable to a transaction in such asset classes, the trading unit should utilize the prevailing bid-ask or similar spread on the relevant position at the time the purchase or sale is completed.~~

~~For other asset classes in which a trading unit is engaged in market making related activities, bid-ask or similar spreads may not be widely disseminated on a consistent basis or otherwise reasonably ascertainable. A covered banking entity must identify any trading unit engaged in market making related activities in an asset class for which the covered banking entity believes bid-ask or similar spreads are not widely disseminated on a consistent basis or are not otherwise reasonably ascertainable and must be able to demonstrate that bid-ask or similar spreads for the asset class are not reasonably ascertainable. In such cases, the trading unit should calculate the Spread Profit and Loss for the relevant purchase or sale of a position in a particular asset class by using whichever of the following three alternatives the banking entity believes more accurately reflects prevailing bid-ask or similar spreads for transactions in that asset class:~~

~~(i) End of Day Spread Proxy: A proxy based on the bid-ask or similar spread that is used to estimate, or is otherwise implied by, the market price at which the trading entity marks (or in the case of a sale, would have marked) the position for accounting purposes at the close of business on the day it executes the purchase or sale (“End of Day Spread Proxy”);~~

~~(ii) Historical Data Spread Proxy: A proxy based on historical bid-ask or similar spread data in similar market conditions (“Historical Data Spread Proxy”); or~~

~~(iii) Any other proxy that the banking entity can demonstrate accurately reflects prevailing bid-ask or similar spreads for transactions in the specific asset class.~~

~~A covered banking entity selecting any of these alternatives should be able to demonstrate that the alternative it has chosen most accurately reflects prevailing bid-ask or similar spreads for the relevant asset class. If a covered banking entity chooses to calculate Spread Profit and Loss for a particular trading unit using the End of Day Spread Proxy, then the banking entity should separately identify the portion of Spread Profit and Loss that is attributable to positions acquired and disposed of on the same trading day. If a banking entity chooses to calculate Spread Profit and Loss for a particular trading unit using the Historical Data Spread Proxy, the covered banking entity should be able to demonstrate that the Historical Data Proxy is appropriate and~~

~~continually monitor market conditions and adjust, as necessary, the Historical Data Proxy to reflect any changes.~~

~~Calculation Period: One trading day.~~

~~5. Comprehensive Profit and Loss Attribution~~

~~Description: For purposes of this appendix, Comprehensive Profit and Loss Attribution is an attribution analysis that divides the trading unit's Comprehensive Profit and Loss into the separate sources of risk and revenue that have caused any observed variation in Comprehensive Profit and Loss. This attribution analysis should attribute Comprehensive Profit and Loss to specific market and risk factors that can be accurately and consistently measured over time. Any component of Comprehensive Profit and Loss that cannot be specifically identified in the attribution analysis should be identified as an unexplained portion of the Comprehensive Profit and Loss.~~

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 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) 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.

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 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.

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.

The portion of comprehensive profit and loss that cannot be specifically attributed to known sources 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.

General Calculation Guidance: The specific ~~market and risk factors~~ categories used by a trading ~~unit~~ 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 ~~unit~~. ~~These factors should~~ 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. ~~The attribution analysis should also identify any significant factors that have a consistent and regular influence on Comprehensive Profit and Loss, such as Risk Factor Sensitivities that have a significant influence on portfolio income, customer spreads, bid-ask spreads, or commissions that are earned. Factors that influence Comprehensive Profit and Loss across different trading units should be measured and included in the attribution analysis in a comparable fashion.~~

Calculation Period: One trading day.

Measurement Frequency: Daily.

C. ~~Revenue-Relative-to-Risk~~ Customer-Facing Activity Measurements

~~1. Volatility of Comprehensive Profit and Loss and Volatility of Portfolio Profit and Loss~~

~~Description: For purposes of this appendix, Volatility of Comprehensive Profit and Loss generally is the standard deviation of the trading unit's Comprehensive Profit and Loss estimated over a given calculation period. For purposes of this appendix, Volatility of Portfolio Profit and Loss generally is the standard deviation of the trading unit's Portfolio Profit and Loss, exclusive of Spread Profit and Loss, estimated over a given calculation period.~~

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

~~2. Comprehensive Profit and Loss to Volatility Ratio and Portfolio Profit and Loss to Volatility Ratio~~

~~Description: For purposes of this appendix, Comprehensive Profit and Loss to Volatility Ratio is a ratio of Comprehensive Profit and Loss to the Volatility of Comprehensive Profit and Loss for a trading unit over a given calculation period. For purposes of this appendix, Portfolio Profit and Loss to Volatility Ratio is a ratio of Portfolio Profit and Loss, exclusive of Spread Profit and Loss, to the Volatility of Portfolio Profit and Loss, exclusive of Spread Profit and Loss, for a trading unit over a given calculation period.~~

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

~~3. Unprofitable Trading Days Based on Comprehensive Profit and Loss and Unprofitable Trading Days Based on Portfolio Profit and Loss~~

~~Description: For purposes of this appendix, Unprofitable Trading Days Based on Comprehensive Profit and Loss is the number or proportion of trading days on which a trading unit's Comprehensive Profit and Loss is less than zero over a given calculation period. For purposes of this appendix, Unprofitable Trading Days Based on Portfolio Profit and Loss, exclusive of Spread Profit and Loss, is the number or proportion of trading days on which a trading unit's Portfolio Profit and Loss, exclusive of Spread Profit and Loss, is less than zero over a given calculation period.~~

~~Calculation Period: 30 days, 90 days, and 360 days.~~

~~4. Skewness of Portfolio Profit and Loss and Kurtosis of Portfolio Profit and Loss~~

~~Description: Skewness of Portfolio Profit and Loss and Kurtosis of Portfolio Profit and Loss should be calculated using standard statistical methods with respect to Portfolio Profit and Loss, exclusive of Spread Profit and Loss.~~

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

~~D. Customer-Facing Activity Measurements~~

~~1.5. Inventory Risk Turnover~~

Description: For purposes of this appendix, Inventory ~~Risk~~ Turnover is a ratio that measures the ~~amount~~turnover of ~~risk associated with~~ a trading ~~unit's inventory, as measured by Risk Factor Sensitivities, that is turned over by the trading unit over a specific period of time. For each Risk Factor Sensitivity, the~~ desk's inventory. The numerator of the ~~Inventory Risk Turnover~~ ratio generally ~~should be~~is the absolute value of ~~the Risk Factor Sensitivity associated with each transaction~~all transactions over the ~~calculation~~reporting period. The denominator of the ~~Inventory Risk Turnover~~ ratio generally ~~should be~~is the value of ~~each Risk Factor Sensitivity for all of the trading unit's holdings~~desk's inventory at the beginning of the ~~calculation~~reporting period.

General Calculation Guidance: ~~As a general matter, a trading unit should measure and report the Inventory Risk Turnover ratio for each of the Risk Factor Sensitivities calculated and furnished for that trading unit.~~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.

Calculation Period: 30 days, 60 days, and 90 days.

Measurement Frequency: Daily.

~~2.6. Inventory Aging~~

Description: For purposes of this appendix, Inventory Aging generally describes a schedule of the trading ~~unit's~~desk's aggregate assets and liabilities and the amount of time that those assets and liabilities have been held ~~for the following periods: 0-30 days; 30-60 days; 60-90 days; 90-180 days; 80-360 days; and greater than 360 days.~~ Inventory Aging should measure the age profile of the trading ~~unit's~~desk's assets and liabilities.

General Calculation Guidance: In general, Inventory Aging ~~should~~must be computed using a trading ~~unit's~~desk's trading activity data and ~~should~~must identify the value of a trading unit's aggregate assets and liabilities. ~~In addition,~~ Inventory Aging ~~should~~must include two schedules, an asset-aging schedule and a liability-aging schedule. ~~The asset-aging~~Each schedule ~~should~~must record the value of ~~the trading unit's assets that have been held for: 0-30 days; 30-60 days; 60-90 days; 90-180 days; 180-360 days; and greater than 360 days.~~ The liability-aging schedule should record the value of the trading unit's liabilities that have been held for: 0-30 days; 30-60 days; 60-90 days; 90-180 days; 180-360 days; and more than 360 daysassets 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.

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

~~3. Customer Facing Trade Ratio~~

~~Description: For purposes of this appendix, the Customer Facing Trade Ratio is a ratio comparing the number of transactions involving a counterparty that is a customer of the trading unit to the number of transactions involving a counterparty that is not a customer of the trading unit. For purposes of calculating the Customer Facing Trade Ratio, a counterparty is considered to be a customer of the trading unit if the counterparty is neither a counterparty to a transaction executed on a designated contract market registered under the Commodity Exchange Act or national securities exchange registered under the Exchange Act, nor a broker-dealer, swap dealer, security-based swap dealer, any other entity engaged in market-making related activities, or any affiliate thereof. A broker-dealer, swap dealer, or security-based swap dealer, any other entity engaged in market-making related activities, or any affiliate thereof may be considered a customer of the trading unit for these purposes if the covered banking entity treats that entity as a customer and has documented how and why the entity is treated as such.~~

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

~~E. Payment of Fees, Commissions, and Spreads Measurement~~

~~1. Pay-to-Receive Spread Ratio~~

~~Description: For purposes of this appendix, the Pay-to-Receive Spread Ratio is a ratio comparing the amount of Spread Profit and Loss and Fee Income that is earned by a trading unit to the amount of Spread Profit and Loss and Fee Income that is paid by the trading unit.~~

~~General Calculation Guidance: The Pay-to-Receive Spread Ratio will depend on the amount of Spread Profit and Loss and Fee Income that is earned by the trading unit for facilitating buy and sell orders and the amount of Spread Profit and Loss that is paid by a trading unit as it initiates buy and sell orders. The Pay-to-Receive Spread Ratio generally should be computed using the calculation of Spread Profit and Loss described in this appendix, except that spread paid should include the aggregate Spread Profit and Loss of all transactions producing a negative Spread Profit and Loss, and spread received should include the aggregate Spread Profit and Loss of all transactions producing a positive Spread Profit and Loss.~~

~~Calculation Period: One trading day.~~

~~Appendix B: Commentary Regarding Identification of Permitted Market Making-Related Activities~~

~~I. Purpose~~

~~This appendix provides commentary describing the features of permitted market making-related activities and distinctions between permitted market making-related activities and prohibited proprietary trading. The appendix applies to all covered banking entities that are engaged in market making-related activities in reliance on § 4(b). The following commentary must be incorporated into the covered banking entity's internal compliance program under § 20, as applicable.~~

~~II. Definitions~~

~~The terms used in this appendix have the same meanings as those set forth in §§ 2 and 3 and Appendix A.~~

~~III. Commentary~~

~~Section 13 of the BHC Act and § 3 prohibit any covered banking entity from engaging in proprietary trading, which is generally defined as engaging as principal for the trading account of the covered banking entity in any transaction to purchase or sell a covered financial position. However, section 13(d)(1)(B) of the BHC Act and § 4(b) permit a covered banking entity to engage in proprietary trading that would otherwise be prohibited if the activity is conducted in connection with the covered banking entity's market making-related activities, to the extent that such activities are designed not to exceed the reasonably expected near-term demands of clients, customers, and counterparties. This commentary is intended to assist covered banking entities in identifying permitted market making-related activities and distinguishing such activities from trading activities that, even if conducted in the context of the covered banking entity's market making operations, would constitute prohibited proprietary trading.~~

~~A. Overview of Market Making-Related Activities~~

Measurement Frequency: Daily.

7. Customer-Facing Trade Ratio – Trade Count Based and Value Based

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.

~~In the context of trading activities in which a covered banking entity acts as principal, market making-related activities generally involve the covered banking entity either (i) in the case of market making in a security that is executed on an organized trading facility or exchange, passively providing liquidity by submitting resting orders that interact with the orders of others on an organized trading facility or exchange and acting as a registered market maker, where such exchange or organized trading facility provides the ability to register as a market maker, [1] or (ii) in other cases, providing an intermediation service to its customers by assuming the role of a counterparty that stands ready to buy or sell a position that the customer wishes to sell or buy. A market maker's "customers" generally vary depending on the asset class and market in which the market maker is providing intermediation services. In the context of market making in a security that is executed on an organized trading facility or an exchange, a "customer" is any person on behalf of whom a buy or sell order has been submitted by a broker-dealer or any other market participant. In the context of market making in a covered financial position in an over-the-counter market, a "customer" generally would be a market participant that makes use of the market maker's intermediation services, either by requesting such services or entering into a continuing relationship with the market maker with respect to such services. [2]~~ 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 § __.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

The primary purpose of market making related activities is to intermediate between buyers and sellers of similar positions, for which service market makers are compensated, resulting in more liquid markets and less volatile prices. The purpose of such activities is not to earn profits as a result of movements in the price of positions and risks acquired or retained; rather, a market maker generally manages and limits the extent to which it is exposed to movements in the price of principal positions and risks that it acquires or retains, or in the price of one or more material elements of those positions. To the extent that it can, a market maker will eliminate some or all of the price risks to which it is exposed. However, in some cases, the risks posed by one or more positions may be sufficiently complex or specific that the risk cannot be fully hedged. In other cases, although it may be possible to hedge the risks posed by one or more positions, the cost of doing so may be so high as to effectively make market making in those positions uneconomic if complete hedges were acquired. In such cases, in order to provide effective intermediation services, market makers are required to retain at least some risk for at least some period of time with respect to price movements of retained principal positions and risks. The size and type of risk that must be retained in such cases may vary widely depending on the type and size of the positions, the liquidity of the specific market, and the market's structure. As the liquidity of positions increases, the frequency with which a market maker must take or retain risk in order to make a market in those positions generally decreases.

The profitability of market making related activities relies on forms of revenue that reflect the value of the intermediation services that are provided to the market maker's customers. These revenues typically take the form of explicit fees and commissions or, in markets where no such fees or commission are charged, a bid-ask or similar spread that is generated by charging higher prices to buyers than is paid to sellers of comparable instruments. In the case of a derivative contract, these revenues reflect the difference between the cost of entering into the derivative contract and the cost of hedging incremental, residual risks arising from the contract. These types of "customer revenues" provide the primary source of a market maker's profitability. Typically, a market maker holds at least some risk with respect to price movements of retained principal positions and risks. As a result, the market maker also incurs losses or generates profits as price movements actually occur, but such losses or profits are incidental to customer revenues and significantly limited by the banking entity's hedging activities. Customer revenues, not revenues from price movements, predominate. The appropriate proportion of "customer revenues" to profits and losses resulting from price movements of retained principal positions and risks varies depending on the type of positions involved, the typical fees, commissions, and spreads payable for transactions in those positions, and the risks of those positions. As a general matter, the proportion of "customer revenues" generated when making a market in certain positions

~~increases as the fees, commissions, or spreads payable for those positions increase, the volatility of those positions' prices decrease, and the prices for those positions are less transparent.~~

~~Because a market maker's business model entails managing and limiting the extent to which it is exposed to movements in the prices of retained principal positions and risks while generating customer revenues that are earned, regardless of movements in the price of retained principal positions and risks, a market maker typically generates significant revenue relative to the risks that it retains. Accordingly, a market maker will typically demonstrate consistent profitability and low earnings volatility under normal market conditions. The appropriate extent to which a market maker will demonstrate consistent profitability and low earnings volatility varies depending on the type of positions involved, the liquidity of the positions, the price transparency of the positions, and the volatility of the positions' prices. As a general matter, consistent profitability will decrease and earnings volatility will increase as the liquidity of the positions decrease, the volatility of the positions' prices increase, and the prices for the positions are less transparent.~~

~~As the primary purpose of market making related activities is to provide intermediation services to its customers, market makers focus their activities on servicing customer demands and typically only engage in transactions with non-customers to the extent that these transactions directly facilitate or support customer transactions. In particular, a market maker generally only transacts with non-customers to the extent necessary to hedge or otherwise manage the risks of its market making related activities, including managing its risk with respect to movements of the price of retained principal positions and risks, to acquire positions in amounts consistent with reasonably expected near term demand of its customers, or to sell positions acquired from its customers. The appropriate proportion of a market maker's transactions that are with customers versus non-customers varies depending on the type of positions involved and the extent to which the positions are typically hedged in non-customer transactions. In the case of a derivatives market maker that engages in dynamic hedging, the number of non-customer transactions significantly outweighs the number of customer transactions, as the derivatives market maker must constantly enter into transactions to appropriately manage its retained principal positions and risks as market prices for the positions and risks move and additional transactions with customers change the risk profile of the market maker's retained principal positions.~~

~~Because a market maker generates revenues primarily by transacting with, and providing intermediation services to, customers, a market maker typically engages in transactions that earn fees, commissions, or spreads as payment for its services. Transactions in which the market maker pays fees, commissions, or spreads—i.e., where it pays another market maker for providing it with liquidity services—are much less frequent, although in some cases obtaining~~

~~liquidity services from another market maker and paying fees, commissions, or spreads may be necessary to prudently manage its risk with respect to price movements of retained principal positions and risks. The appropriate proportion of a market maker's transactions that earn, rather than pay, fees, commissions or spreads varies depending on the type of positions involved, the liquidity of the positions, and the extent to which market trends increase the volatility of its risk with respect to price movements of retained principal positions and risks. As a general matter, the proportion of a market maker's transactions that earn rather than pay fees, commissions or spreads decreases as the liquidity of the positions decreases, and the extent to which the price volatility of retained principal positions and risks increases.~~

~~Finally, because the primary purpose of market making related activities is to provide intermediation services to its customers, a market maker does not provide compensation incentives to its personnel that primarily reward proprietary risk taking. Although a market maker may take into account revenues resulting from movements in the price of retained principal positions and risks to the extent that such revenues reflect the effectiveness with which personnel have effectively managed the risk of movements in the price of retained principal positions and risks, a market maker that provides compensation incentives relating to revenues generally does so through incentives that primarily reward customer revenues and effective customer service.~~

~~B. Overview of Prohibited Proprietary Trading Activities~~

~~Like permitted market making related activities, prohibited proprietary trading involves the taking of principal positions by a covered banking entity. Unlike permitted market making related activities, the purpose of prohibited proprietary trading is to generate profits as a result of, or otherwise benefit from, changes in the price of positions and risks taken. Whereas a market maker attempts to eliminate some or all of the price risks inherent in its retained principal positions and risks by hedging or otherwise managing those risks in a reasonable period of time after positions are acquired or risks arise, a proprietary trader seeks to capitalize on those risks, and generally only hedges or manages a portion of those risks when doing so would improve the potential profitability of the risk it retains. A proprietary trader does not have "customers" because a proprietary trader simply seeks to obtain the best price and execution in purchasing or selling its proprietary positions. A proprietary trader generates few if any fees, commissions, or spreads from its trading activities because it is not providing an intermediation service to any customer or other third party. Instead, a proprietary trader is likely to pay fees, commissions, or spreads to other market makers when obtaining their liquidity services is beneficial to execution of its trading strategy. Because a proprietary trader seeks to generate profits from changes in the price of positions taken, a proprietary trader typically provides compensation incentives to its personnel that primarily reward successful proprietary risk taking.~~

~~C. Distinguishing Permitted Market Making-Related Activities From Prohibited Proprietary Trading~~

~~Because both permitted market making-related activities and prohibited proprietary trading involve the taking of principal positions, certain challenges arise in distinguishing permitted market making-related activities and prohibited proprietary trading, particularly in cases where both of these activities occur in the context of a market making operation. Particularly during periods of significant market disruption, it may be difficult to distinguish between retained principal positions and risks that appropriately support market making-related activities and positions taken, or positions or risks not hedged, for proprietary purposes.~~

~~In connection with these challenges, [Agency] will apply the following factors in distinguishing permitted market making-related activities from trading activities that, even if conducted in the context of the covered banking entity's market making operations, would constitute prohibited proprietary trading. The particular types of trading activity described in this appendix may involve the aggregate trading activities of a single trading unit, a significant number or series of transactions occurring at one or more trading units, or a single significant transaction, among other potential scenarios. In addition to meeting the terms of this appendix, any transaction or activity for which a covered banking entity intends to rely on the market making exemption in § 2.4(b) must also satisfy all the requirements specified in § 2.4(b), as well as the other applicable requirements and conditions of this part.~~

~~1. Risk Management~~

~~Absent explanatory facts and circumstances, particular trading activity in which a trading unit retains risk in excess of the size and type required to provide intermediation services to customers will be considered to be prohibited proprietary trading, and not permitted market making-related activity.~~

~~[The Agency] will base a determination of whether a trading unit retains risk in excess of the size and type required for these purposes on all available facts and circumstances, including a comparison of retained principal risk to: The amount of risk that is generally required to execute a particular market making function; hedging options that are available in the market and permissible under the covered banking entity's hedging policy at the time the particular trading activity occurred; the trading unit's prior levels of retained risk and its hedging practices with respect to similar positions; and the levels of retained risk and the hedging practices of other trading units with respect to similar positions.~~

~~To help assess the extent to which a trading unit's risks are potentially being retained in excess of amounts required to provide intermediation services to customers, [Agency] will utilize the VaR and Stress VaR, VaR Exceedance, and Risk Factor Sensitivities quantitative measurements, as applicable, among other risk measurements described in appendix A to this part and any other relevant factor. This assessment will focus primarily on the risk measurements relative to: The risk required for conducting market making related activities, and any significant changes in the risk over time and across similarly situated trading units and banking entities.~~

~~Explanatory facts and circumstances might include, among other things, market wide changes in risk, changes in the specific composition of market making related activities, temporary market disruptions, or other market changes that result in previously used hedging or other risk management techniques no longer being possible or cost effective.~~

~~2. Source of Revenues~~

~~Absent explanatory facts and circumstances, particular trading activity in which a trading unit primarily generates revenues from price movements of retained principal positions and risks, rather than customer revenues, will be considered to be prohibited proprietary trading, and not permitted market making related activity.~~

~~[The Agency] will base a determination of whether a trading activity primarily generates revenues from price movements of retained principal positions and risks, rather than customer revenues, on all available facts and circumstances, including: an evaluation of the revenues derived from price movements of retained principal positions and risks relative to its customer revenues; and a comparison of these revenue figures to the trading unit's prior revenues with respect to similar positions, and the revenues of other covered banking entities' trading units with respect to similar positions.~~

~~To help assess the extent to which a trading unit's revenues are potentially derived from movements in the price of retained principal positions and risks, [Agency] will utilize the Comprehensive Profit and Loss, Portfolio Profit and Loss, Fee Income and Expense, and Spread Profit and Loss quantitative measurements, as applicable, both individually and in combination with one another (e.g., by comparing the ratio of Spread Profit and Loss to Portfolio Profit and Loss), and any other relevant factor.~~

~~Explanatory facts and circumstances might include, among other things: general upward or downward price trends in the broader markets in which the trading unit is making a market, provided revenues from price movements in retained principal positions and risks are consistent; sudden market disruptions or other changes causing significant, unanticipated alterations in the price of retained principal positions and risks; sudden and/or temporary changes in the market (e.g., narrowing of bid/ask spreads) that cause significant, unanticipated reductions in customer revenues; or efforts to expand or contract a trading unit's market share.~~

~~3. Revenues Relative to Risk~~

~~Absent explanatory facts and circumstances, particular trading activity will be considered to be prohibited proprietary trading, and not permitted market making related activity, if the trading unit: generates only very small or very large amounts of revenue per unit of risk taken; does not demonstrate consistent profitability; or demonstrates high earnings volatility.~~

~~[The Agency] will base such a determination on all available facts and circumstances, including: an evaluation of the amount of revenue per unit of risk taken, earnings volatility, profitability, exposure to risks, and overall level of risk taking for the particular trading activities; and a comparison of these figures to the trading unit's prior results with respect to similar positions, and the results of other covered banking entities' trading units with respect to similar positions.~~

~~To help assess the riskiness of revenues and the amount of revenue per unit of risk taken, [Agency] will utilize the Volatility of Comprehensive Profit and Loss and Volatility of Portfolio Profit and Loss, Comprehensive Profit and Loss to Volatility Ratio and Portfolio Profit and Loss to Volatility Ratio, and Comprehensive Profit and Loss Attribution quantitative measurements, as applicable, and any other relevant factor.~~

~~To help assess the extent to which a trading unit demonstrates consistent profitability, [Agency] will utilize the Unprofitable Trading Days Based on Comprehensive Profit and Loss and Unprofitable Trading Days Based on Portfolio Profit and Loss quantitative measurements, as applicable, and any other relevant factor.~~

~~To help assess the extent to which a trading unit is exposed to outsized risk, [Agency] will utilize the Skewness of Portfolio Profit and Loss and Kurtosis of Profit and Loss quantitative measurements, as applicable, and any other relevant factor.~~

~~Explanatory facts and circumstances might include, among other things: market disruptions or other changes causing significant, unanticipated increases in a trading unit's risk with respect to movements in the price of retained principal positions and risks; market disruptions or other changes causing significant, unanticipated increases in the volatility of positions in which the trading unit makes a market; sudden and/or temporary changes in the market (e.g., narrowing of bid-ask spreads) that cause significant, unanticipated reductions in customer revenues and decrease overall profitability; or efforts to expand or contract a trading unit's market share.~~

~~4. Customer Facing Activity~~

~~Absent explanatory facts and circumstances, particular trading activity will be considered to be prohibited proprietary trading, and not permitted market making related activity, if the trading unit: does not transact through a trading system that interacts with orders of others or primarily with customers of the banking entity's market making desk to provide liquidity services; or retains principal positions and risks in excess of reasonably expected near term customer demands.~~

~~[The Agency] will base such a determination on all available facts and circumstances, including, among other things: An evaluation of the extent to which a trading unit's transactions are with customers versus non-customers and the frequency with which the trading unit's retained principal positions and risks turn over; and a comparison of these figures to the trading unit's prior results with respect to similar positions and market situations, and the results of other covered banking entities' trading units with respect to similar positions.~~

~~To help assess the extent to which a trading unit's transactions are with customers versus non-customers, [Agency] will utilize the Customer Facing Trade Ratio quantitative measurement, as applicable, and any other relevant factor. To help assess the frequency with which the trading unit's retained principal positions and risks turn over, [Agency] will utilize the Inventory Risk Turnover and Inventory Aging quantitative measurements, as applicable, and any other relevant factor.~~

~~With respect to a particular trading activity in which a trading unit either does not transact through a trading system that interacts with orders of others or primarily with customers of the banking entity's market making desk to provide liquidity services, explanatory facts and circumstances might include, among other things: sudden market disruptions or other changes causing significant increases in a trading unit's hedging transactions with non-customers; or substantial intermediary trading required to satisfy customer demands and hedging management. With respect to particular trading activity in which a trading unit retains principal positions and risks in excess of reasonably expected near term customer demands, explanatory facts and circumstances might include, among other things: sudden market disruptions or other changes causing a significant reduction in actual customer demand relative to expected customer demand; documented and reasonable expectations for temporary increases in customer demand in the near term; and sudden market disruptions or other changes causing a significant reduction in the value of retained principal positions and risks, such that it would be imprudent for the trading unit to dispose of the positions in the near term.~~

~~5. Payment of Fees, Commissions, and Spreads~~

~~Absent explanatory facts and circumstances, particular trading activity in which a trading unit routinely pays rather than earns fees, commissions, or spreads will be considered to be prohibited proprietary trading, and not permitted market making related activity.~~

~~[The Agency] will base such a determination on all available facts and circumstances, including, among other things: An evaluation of the frequency with which the trading unit pay fees, commissions, or spreads and the relative amount of fees, commissions, or spreads that is paid versus earned; and a comparison of these figures to the trading unit's prior results with respect to similar positions, and the results of other covered banking entities' trading units with respect to similar positions.~~

~~To help assess the extent to which a trading unit is paying versus earning fees, commissions, and spreads, [Agency] will utilize the Pay to Receive Spread Ratio quantitative measurement, as applicable, and any other relevant factor.~~

~~Explanatory facts and circumstances might include, among other things, sudden market disruptions or other changes causing significant, increases in a trading unit's hedging transactions with non-customers for which it must pay fees, commissions, or spreads, sudden, unanticipated customer demand for liquidity that requires the trading unit itself to pay fees, commissions, or spreads to other market makers for liquidity services to obtain the inventory needed to meet that~~

~~customer demand, or significant, unanticipated reductions in fees, commissions, or spreads earned by the trading unit. Explanatory facts and circumstances might also include a trading unit's efforts to expand or contract its market share.~~

~~6. Compensation Incentives~~

~~Absent explanatory facts and circumstances, the trading activity of a trading unit that provides compensation incentives to employees that primarily reward proprietary risk taking will be considered to be prohibited proprietary trading, and not permitted market making related activity.~~

~~[The Agency] will base such a determination on all available facts and circumstances, including, among other things, an evaluation of: the extent to which compensation incentives are provided to trading unit personnel that reward revenues from movements in the price of retained principal positions and risks; the extent to which compensation incentives are provided to trading unit personnel that reward customer revenues; and the compensation incentives provided by other covered banking entities to similarly situated personnel.~~

~~* * * * *~~

~~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.~~

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

~~Measurement Frequency: Daily.~~

~~Appendix ~~C~~B: Enhanced Minimum Standards for ~~Programmatic~~ Compliance Programs~~

~~I. Overview~~

~~A. Purpose~~

~~This appendix sets forth the minimum standards with respect to the establishment, maintenance, and enforcement by banking entities of internal compliance programs for ensuring and~~

~~monitoring compliance with the prohibitions and restrictions on proprietary trading and covered fund activities or investments set forth in section 13 of the BHC Act and this part.~~

~~This appendix~~Section 20(c) requires ~~that certain~~ banking entities to establish, maintain, and enforce an ~~effective~~enhanced compliance program, ~~consisting of that includes the requirements and standards in this Appendix as well as the minimum~~ written policies and procedures, internal controls, ~~a~~ management framework, independent testing, training, and recordkeeping, ~~that provisions outlined in § 20. This Appendix sets forth additional minimum standards with respect to the establishment, oversight, maintenance, and enforcement by these banking entities of an enhanced internal compliance program for ensuring and monitoring 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.~~

This compliance program must:

~~Is~~• Be reasonably designed to ~~clearly identify~~, document, ~~describe, and~~ monitor, and report the ~~covered~~permitted trading and covered fund activities ~~or and~~ investments ~~and the risks~~ of the ~~covered~~ banking entity ~~related to such~~; identify, monitor and promptly address the risks of these covered activities ~~or and~~ investments, ~~identify and~~ potential areas of noncompliance; and prevent activities or investments prohibited by, or that do not comply with, section 13 of the BHC Act and this part; ~~Specifically addresses the varying nature of~~

• Establish and enforce appropriate limits on the covered activities ~~or and~~ investments ~~conducted by different units~~ of the ~~covered~~ banking entity's ~~organization~~, including limits on the size, scope, complexity, and risks of the individual activities or investments consistent with the requirements of section 13 of the BHC Act and this part; ~~Subjects~~

• Subject the effectiveness of the compliance program to periodic independent review and testing, and ensure that the entity's internal audit, corporate compliance and internal control functions involved in review and testing are effective and independent; ~~Makes~~

• Make senior management, ~~and intermediate managers~~ others as appropriate, accountable for the effective implementation of the compliance program, and ~~ensures~~ensure that the board of directors and ~~CEO~~chief executive officer (or equivalent) of the banking entity review the effectiveness of the compliance program; and ~~Facilitates supervision and examination of the covered banking entity's covered trading and covered fund activities or investments by the Agencies.~~ **B. Definitions**

~~The terms used in this Appendix have the same meanings as set forth in §§ 2, 3, and 10. In addition, for purposes of this appendix, the following definitions apply:~~

~~Asset management unit means any unit of organization of a covered banking entity that makes investments in, or acts as sponsor to, covered funds, or has relationships with covered funds, that~~

~~the covered banking entity (or an affiliate or subsidiary thereof) has sponsored, organized and offered, or in which a covered fund sponsored or advised by the covered banking entity invests.~~

~~Compliance program means the internal compliance program established by a covered banking entity in accordance with § __.20 and this appendix.~~

~~Covered fund activity or investment means sponsoring any covered fund or making investments in, or otherwise having relationships with, any covered fund for which the covered banking entity (or an affiliate or subsidiary thereof) acts as sponsor or organizes and offers.~~

~~Covered fund restrictions means the restrictions on covered fund activities or investments set forth in subpart C.~~

~~Covered trading activity means proprietary trading, as defined in § __.3(b)(1).~~

~~Trading unit means each of the following units of organization of a covered banking entity:~~

~~(i) Each discrete unit that is engaged in the coordinated implementation of a revenue generation strategy and that participates in the execution of any covered trading activity; [1]~~

~~(ii) Each organizational unit that is used to structure and control the aggregate risk-taking activities and employees of one or more trading units described in paragraph (i); [2]~~

~~(iii) All trading operations, collectively; and~~

~~(iv) Any other unit of organization specified by [Agency] with respect to a particular banking entity.~~

C. Required Elements

~~Section __.20 requires that covered banking entities establish, maintain, and enforce a compliance program reasonably designed to ensure and monitor compliance with the prohibitions and restrictions on proprietary trading and covered fund activities or investments that effectively implements, at a minimum, the six elements required under paragraph (b) of § __.20.~~

D. Compliance Program Structure

~~Each covered banking entity subject to § __.20(c) must be governed by a compliance program meeting the requirements of this appendix. A covered banking entity may establish a compliance program on an enterprise-wide basis to satisfy the requirements of § __.20 and this appendix with respect to the covered banking entity and all of its affiliates and subsidiaries collectively, provided that: the program is clearly applicable, both by its terms and in operation, to all such affiliates and subsidiaries; the program specifically addresses the requirements set forth in this appendix; the program takes into account and addresses the consolidated organization's business structure, size, and complexity, as well as the particular activities, risks, and applicable legal requirements of each subsidiary and affiliate; and the program is determined through periodic independent testing to be effective for the covered banking entity and all of its subsidiaries and affiliates. An enterprise-wide program established pursuant to this Appendix will be subject to supervisory review and examination by any Agency vested with rulewriting authority under section 13 of the BHC Act with respect to the compliance program and the activities or investments of any banking entity for which the Agency has such authority. Further, such Agency will have access to all records related to the enterprise-wide compliance program pertaining to any banking entity that is supervised by the Agency vested with such rulewriting authority.~~

E. Applicability

~~This appendix applies only to covered banking entities described in § __.20(c)(2). In addition, [Agency] may require any covered banking entity to comply with all or portions of this appendix if [Agency] deems it appropriate for purposes the covered banking entity's compliance with this part.~~

~~Nothing in this appendix limits the authority of [Agency] under any other provision of law or regulation to take supervisory, examination, or enforcement action, including action to address unsafe or unsound practices or conditions, deficient capital levels, or violations of law.~~

• Facilitate supervision and examination by the Agencies of the banking entity's permitted trading and covered fund activities and investments.

II. ~~Internal Policies and Procedures~~ Enhanced Compliance Program

A. ~~Covered~~ Proprietary Trading Activities

A ~~covered~~ banking entity must establish, maintain, and enforce a compliance program that includes written policies and procedures ~~reasonably designed to document, describe, and monitor the covered banking entity's covered trading activities and the risks taken in these activities, as follows: [3]~~ that are appropriate for the types, size, and complexity

of, and risks associated with, its permitted trading activities. The compliance program may be tailored to the types of trading activities conducted by the banking entity, and must include a detailed description of controls established by the banking entity to reasonably ensure that its trading activities are conducted in accordance with the requirements and limitations applicable to those trading activities under section 13 of the BHC Act and this part, and provide for appropriate revision of the compliance program before expansion of the trading activities of the banking entity. A banking entity must devote adequate resources and use knowledgeable personnel in conducting, supervising and managing its trading activities, and promote consistency, independence and rigor in implementing its risk controls and compliance efforts. The compliance program must be updated with a frequency sufficient to account for changes in the activities of the banking entity, results of independent testing of the program, identification of weaknesses in the program, and changes in legal, regulatory or other requirements.

~~Identification of trading accounts~~ Trading Desks: The ~~covered~~ banking entity's ~~policies and procedures must specify how the banking entity evaluates the covered financial positions it acquires or takes and determines which of its accounts are trading accounts for purposes of subpart B of this part.~~ Identification of trading units and organization structure: The ~~covered banking entity's~~ must have written policies and procedures ~~must identify and document each trading unit within the organization and map each trading unit~~ governing each trading desk that include a description of:

• The process for identifying, authorizing and documenting financial instruments each trading desk may purchase or sell, with separate documentation for market making-related activities conducted in reliance on § __.4(b) and for hedging activity conducted in reliance on § __.5;

• A mapping for each trading desk to the division, business line, or other organizational structure that ~~the covered banking entity uses to manage or oversee~~ is responsible for managing and overseeing the trading ~~unit~~ desk's activities;

~~Description of missions and strategies:~~ The ~~covered banking entity's~~ written policies and procedures for each trading unit must clearly articulate and document a comprehensive

~~description of the mission (i.e., the nature of the business conducted) and strategy (i.e., business model for the generation of revenues) of the trading unit, and include a description of:~~

~~How revenues are intended to be generated by the trading unit.~~• The mission (i.e., the type of trading activity, such as market-making, trading in sovereign debt, etc.) and strategy (i.e., methods for conducting authorized trading activities) of each trading desk;

• The activities that the trading ~~unit~~desk is authorized to conduct, including (i) authorized instruments and products, and (ii) authorized hedging strategies, techniques and instruments;~~The expected~~

• The types and amount of risks allocated by the banking entity to each trading desk to implement the mission and strategy of the trading desk, including an enumeration of material risks resulting from the activities in which the trading desk is authorized to engage (including but not limited to price risks, such as basis, volatility and correlation risks, as well as counterparty credit risk). Risk assessments must take into account both the risks inherent in the trading activity and the strength and effectiveness of controls designed to mitigate those risks;

• How the risks allocated to each trading desk will be measured;

• Why the allocated risks levels are appropriate to the activities authorized for the trading desk;

• The limits on the holding period of, and the ~~market~~risk associated with, ~~covered financial positions in its trading account;~~financial instruments under the responsibility of the trading desk;

• The process for setting new or revised limits, as well as escalation procedures for granting exceptions to any limits or to any policies or procedures governing the desk, the analysis that will be required to support revising limits or granting exceptions, and the process for independently reviewing and documenting those exceptions and the underlying analysis;

• The process for identifying, documenting and approving new products, trading strategies, and hedging strategies;

• The types of clients, customers, and counterparties with whom ~~trading is conducted by the trading unit;~~ ~~How the trading unit, if engaged in market making related activity under § __.4(b) of this part, identifies its customers for purposes of computing the Customer Facing Trade Ratio, if applicable, including documentation explaining when, how, and why a broker-dealer, swap dealer, security-based swap dealer, any other entity engaged in market making related activities, or any affiliate thereof is considered to be a customer of the trading unit for those purposes;~~ and ~~The compensation structure of the~~the trading desk may trade; and

• The compensation arrangements, including incentive arrangements, for employees associated with the trading unit. ~~Trader mandates: The covered banking entity must establish, maintain, document, and enforce trader mandates for each trading unit. At a minimum, trader mandates~~

~~must~~ desk, which may not be designed to reward or incentivize prohibited proprietary trading or excessive or imprudent risk-taking.

~~Clearly inform each trader of the prohibitions and requirements set forth in section 13 of the BHC Act and this part and his or her responsibilities for compliance with such requirements; Set forth appropriate parameters for each trader engaged in covered trading activities, including: ○ The conditions for relying on the applicable exemptions in §§ 4 through 6;~~

~~○ The financial contracts, products, and underlying assets that the trader is permitted to trade pursuant to the covered banking entity's internal controls;~~

~~○ The risk limits of the trader's trading unit, and the types and levels of risk that may be taken; and~~

~~○ The applicable trading unit's hedging policy.~~

Description of risks and risk management processes: The ~~written policies and procedures for each trading unit must clearly articulate and document~~ compliance program for the banking entity must include a comprehensive description of the ~~risks associated with the trading unit. Such descriptions~~ risk management program for the trading activity of the banking entity. The compliance program must also include a description of the governance, approval, reporting, escalation, review and other processes the banking entity will use to reasonably ensure that trading activity is conducted in compliance with section 13 of the BHC Act and this part. Trading activity in similar financial instruments should be subject to similar governance, limits, testing, controls, and review, unless the banking entity specifically determines to establish different limits or processes and documents those differences. Descriptions must include, at a minimum, the following elements:

• A description of the supervisory and risk management structure governing the all trading units activity, including a description of processes for initial and senior-level review of new products and new strategies; ~~A description of the types of risks that may be taken to implement the mission and strategy of the trading unit, including an enumeration of material risks resulting from the activities in which the trading unit is engaged (including but not limited to all significant price risks, such as basis, volatility and correlation risks, as well as any significant counterparty credit risk associated with the trading activity); An articulation of the amount of risk allocated by the covered banking entity to such trading unit to implement the documented mission and strategy of the trading unit; An explanation of how the risks allocated to such~~

~~trading unit will be measured; and An explanation of why the allocated risk levels are appropriate to the mission and strategy of the trading unit.~~

• A description of the process for developing, documenting, testing, approving and reviewing all models used for valuing, identifying and monitoring the risks of trading activity and related positions, including the process for periodic independent testing of the reliability and accuracy of those models;

• A description of the process for developing, documenting, testing, approving and reviewing the limits established for each trading desk;

• A description of the process by which a security may be purchased or sold pursuant to the liquidity management plan, including the process for authorizing and monitoring such activity to ensure compliance with the banking entity's liquidity management plan and the restrictions on liquidity management activities in this part;

• A description of the management review process, including escalation procedures, for approving any temporary exceptions or permanent adjustments to limits on the activities, positions, strategies, or risks associated with each trading desk; and

• The role of the audit, compliance, risk management and other relevant units for conducting independent testing of trading and hedging activities, techniques and strategies.

Authorized risks, instruments, and products. The banking entity must implement and enforce limits and internal controls for each trading desk that are reasonably designed to ensure that trading activity is conducted in conformance with section 13 of the BHC Act and this part and with the banking entity's written policies and procedures. The banking entity must establish and enforce risk limits appropriate for the activity of each trading desk. These limits should be based on probabilistic and non-probabilistic measures of potential loss (e.g., Value-at-Risk and notional exposure, respectively), and measured under normal and stress market conditions. At a minimum, these internal controls must monitor, establish and enforce limits on:

• The financial instruments (including, at a minimum, by type and exposure) that the trading desk may trade;

• The types and levels of risks that may be taken by each trading desk; and

• The types of hedging instruments used, hedging strategies employed, and the amount of risk effectively hedged.

Hedging policies and procedures. The ~~covered~~ banking entity must establish, maintain, and enforce written policies and procedures ~~for all of its trading units~~ regarding the use of risk-mitigating hedging instruments and strategies. ~~At that, at~~ a minimum, ~~these hedging policies and procedures must articulate the following~~ describe:

~~The manner in which the covered banking entity will determine that the risks generated by each trading unit have been properly and effectively hedged; The instruments, techniques and strategies the covered entity will~~

~~• The positions, techniques and strategies that each trading desk may use to hedge the risk of the positions or portfolios; The level of the organization at which hedging activity and management will occur; The manner in which hedging strategies will be monitored; The risk management processes used to control unhedged or residual risks; and The independent testing of hedging techniques and strategies. Explanation of compliance. The covered banking entity's written policies and procedures must clearly articulate and document a comprehensive explanation of how the mission and strategy of each trading unit, and its related risk levels, comply with this part. Such explanation must:~~its positions;

• The manner in which the banking entity will identify the risks arising in connection with and related to the individual or aggregated positions, contracts or other holdings of the banking entity that are to be hedged and determine that those risks have been properly and effectively hedged;

• The level of the organization at which hedging activity and management will occur;

• The manner in which hedging strategies will be monitored and the personnel responsible for such monitoring;

• The risk management processes used to control unhedged or residual risks; and

• The process for developing, documenting, testing, approving and reviewing all hedging positions, techniques and strategies permitted for each trading desk and for the banking entity in reliance on § __.5.

Analysis and quantitative measurements. The banking entity must perform robust analysis and quantitative measurement of its trading activities that is reasonably designed to ensure that the trading activity of each trading desk is consistent with the banking entity's compliance program; monitor and assist in the identification of potential and actual prohibited proprietary trading activity; and prevent the occurrence of prohibited proprietary trading. Analysis and models used to determine, measure and limit risk must be rigorously tested and be reviewed by management responsible for trading activity to ensure that trading activities, limits, strategies, and hedging activities do not understate the risk and exposure to the banking entity or allow prohibited proprietary trading. This review should include periodic and independent back-testing and revision of activities, limits, strategies and hedging as appropriate to contain risk and ensure compliance. In addition to the quantitative measurements reported by any banking entity subject to Appendix A to this part, each banking entity must develop and implement, to the extent appropriate to facilitate compliance with this part, additional quantitative measurements specifically tailored to the particular risks, practices, and strategies of its trading desks. The

banking entity's analysis and quantitative measurements must incorporate the quantitative measurements reported by the banking entity pursuant to Appendix A (if applicable) and include, at a minimum, the following:

- Internal controls and written policies and procedures reasonably designed to ensure the accuracy and integrity of quantitative measurements;

- Ongoing, timely monitoring and review of calculated quantitative measurements;

- The establishment of numerical thresholds and appropriate trading measures for each trading desk and heightened review of trading activity not consistent with those thresholds to ensure compliance with section 13 of the BHC Act and this part, including analysis of the measurement results or other information, appropriate escalation procedures, and documentation related to the review; and

- Immediate review and compliance investigation of the trading desk's activities, escalation to senior management with oversight responsibilities for the applicable trading desk, timely notification to [Agency], appropriate remedial action (e.g., divesting of impermissible positions, cessation of impermissible activity, disciplinary actions), and documentation of the investigation findings and remedial action taken when quantitative measurements or other information, considered together with the facts and circumstances, or findings of internal audit, independent testing or other review suggest a reasonable likelihood that the trading desk has violated any part of section 13 of the BHC Act or this part.

Other Compliance Matters. In addition to the requirements specified above, the banking entity's compliance program must:

~~Identify which portions of the risk-taking activity of the trading unit would or would not constitute covered trading activity;~~ • Identify activities of ~~the~~each trading ~~unit~~desk that will be conducted in reliance on exemptions contained in §§ ___.4 through ___.6, including an explanation of:

- o How and where in the organization the activity occurs; and

- o Which exemption is being relied on and how the activity meets the specific requirements for reliance on the applicable exemption;

- Include an explanation of the process for documenting, approving and reviewing actions taken pursuant to the liquidity management plan, where in the organization this activity occurs, the securities permissible for liquidity management, the process for ensuring that liquidity management activities are not conducted for the purpose of prohibited proprietary trading, and the process for ensuring that securities purchased as part of the liquidity management plan are highly liquid and conform to the requirements of this part;

• Describe how the ~~covered~~ banking entity monitors for and prohibits potential or actual material exposure to high-risk assets or high-risk trading strategies presented by each trading ~~unit~~desk that relies on the exemptions contained in §§ .3(d)(3), and .4 through .6, which must take into account potential or actual exposure to:

o Assets whose values cannot be externally priced or, where valuation is reliant on pricing models, whose model inputs cannot be externally validated;

o Assets whose changes in ~~values~~value cannot be adequately mitigated by effective hedging;

o New products with rapid growth, including those that do not have a market history;

o Assets or strategies that include significant embedded leverage;

o Assets or strategies that have demonstrated significant historical volatility;

o Assets or strategies for which the application of capital and liquidity standards would not adequately account for the risk; and

o Assets or strategies that result in large and significant concentrations to sectors, risk factors, or counterparties;

~~Explain how each trading unit will comply~~• Establish responsibility for compliance with the reporting and recordkeeping requirements of subpart B and § .7 and Appendix A; ~~Describe how the covered banking entity monitors~~20; and

• Establish policies for monitoring and ~~prohibits~~prohibiting potential or actual material conflicts of interest between the ~~covered~~ banking entity and its clients, customers, or counterparties ~~present in each trading unit~~; and ~~Describe how the covered banking entity monitors for and prohibits potential or actual transactions or activities that may threaten the safety and soundness of the covered banking entity.~~

Remediation of violations. The ~~covered banking entity's written policies and procedures must require the covered banking entity~~banking entity's compliance program must be reasonably designed and established to effectively monitor and identify for further analysis any trading

activity that may indicate potential violations of section 13 of the BHC Act and this part and to prevent actual violations of section 13 of the BHC Act and this part. The compliance program must describe procedures for identifying and remedying violations of section 13 of the BHC Act and this part, and must include, at a minimum, a requirement to promptly document, address and remedy any violation of section 13 of the BHC Act or this part, and document all proposed and actual remediation efforts. ~~Further, such policies and procedures~~The compliance program must include specific written policies and procedures that are reasonably designed to ~~implement and monitor any required remediation and that~~ assess the extent to which any ~~violation~~activity indicates that modification to the ~~covered~~ banking entity's compliance program is warranted.

and to ensure that appropriate modifications are implemented. The written policies and procedures must provide for prompt notification to appropriate management, including senior management and the board of directors, of any material weakness or significant deficiencies in the design or implementation of the compliance program of the banking entity.

~~With respect to any trading unit that is either used by the covered banking entity to structure and control the aggregate risk-taking activities and employees of one or more other trading units, or comprised of the entire trading operation of the covered banking entity, the description of missions and strategies, description of risks and risk management processes, and explanation of compliance for such trading units may incorporate by reference the policies and procedures of the underlying trading units that the trading unit oversees and manages in the aggregate.~~

B. Covered Fund Activities or Investments

~~A covered~~ banking entity must establish, maintain, and enforce a compliance program that includes written policies and procedures that are ~~reasonably designed to document, describe, and monitor the covered banking entity's covered fund activities or investments and the risks taken in these~~ appropriate for the types, size, complexity and risks of the covered fund and related activities or conducted and investments, as follows made, by the banking entity.

Identification of covered funds: ~~The covered banking entity's policies and procedures must specify how the covered banking entity identifies~~ banking entity's compliance program must provide a process, which must include appropriate management review and independent testing, for identifying and documenting covered funds that each unit within the covered banking entity's organization sponsors, or organizes and offers, or in which covered banking entity invests and covered funds in which each such unit invests. In addition to the documentation requirements for covered funds, as specified under § .20(e), the documentation must include information that identifies all pools that the banking entity sponsors or has an interest in and the type of exemption from the Commodity Exchange Act (whether or not the pool relies on section 4.7 of the regulations under the Commodity Exchange Act), and the amount of ownership interest the banking entity has in those pools.

Identification of ~~asset management units and organization structure: The covered~~ covered fund activities and investments. The banking entity's ~~written policies and procedures's~~ compliance program must identify ~~and~~ document each asset management and map each unit within the organization that is permitted to acquire or hold an interest in any covered fund or sponsor any covered fund and map each ~~asset management~~ unit to the division, business line, or other organizational structure that ~~the covered banking entity uses to manage or oversee the asset management unit's activities or will be responsible for managing and overseeing that unit's~~ activities and investments.

~~Description of sponsorship activities related to covered funds: The covered banking entity's written policies and procedures for each asset management unit must clearly articulate and document a comprehensive description of the mission (i.e., the nature of the business conducted) and strategy (i.e., business model for the generation of revenues) of the asset management unit related to its sponsorship or organizing and offering of covered funds, including a description of how such activities comply with this part and, in particular:~~

~~The activities that the asset management unit is authorized to conduct, including the nature of any trust, fiduciary, investment advisory, or commodity trading advisory services offered to customers of the covered banking entity; The types of customers to whom the asset management unit provides such services and to whom ownership interests in covered funds are sold; The extent of any co-investment activities of the covered banking entity (including its directors or employees) in covered funds offered to such customers; and How the asset management unit complies with the requirements of subpart C of this part. Description of investment activities of covered funds: The covered banking entity's written policies and procedures for each asset management unit must clearly articulate and document a comprehensive description of the mission (i.e., the nature of the business conducted) and strategy (i.e., business model for the generation of revenues) of the asset management unit related to its investments in covered funds, including a description of how such activities comply with this part and, in particular:~~

Explanation of compliance. The banking entity's compliance program must explain how:

~~• The asset management unit's practices with respect to seed capital investments in covered funds, including how the asset management unit reduces its investments in covered funds to amounts that are permitted de minimis investments within the required period of time; The asset management unit's practices with respect to co-investments in covered funds, including certain parallel investments as identified in § __.12; How the asset management unit complies with the requirements of § __.12 with respect to individual and aggregate investments in covered funds; With respect to other permitted covered fund activities or investment, how the asset management unit complies with the requirements of §§ __.13 and __.14; How the asset management unit complies with the limitations on relationships with a covered fund under § __.16; How the covered banking entity monitors for and prohibits potential or actual material conflicts of interest between the covered banking entity and its clients, customers, or counterparties related to the asset management unit; How the its covered fund activities and investments;~~

~~• The banking entity monitors for and prohibits potential or actual transactions or activities that may threaten the safety and soundness of the covered banking entity related to the asset management unit; and How the its covered fund activities and investments; and~~

~~• The banking entity monitors for and prohibits potential or actual material exposure to high-risk assets or high-risk trading strategies presented by each asset management unit. Remediation of violations. The covered banking entity's written policies and procedures must require the covered~~

~~banking entity to promptly document, address and remedy any violation of section 13 of the BHC Act or this part, and document all proposed and actual remediation efforts. Further, such policies and procedures must include specific procedures that are designed to implement, monitor, and enforce any required remediation and that assess the extent to which any violation indicates that modification to the covered banking entity's compliance program is warranted.~~its

covered fund activities and investments, taking into account potential or actual exposure to:

o Assets whose values cannot be externally priced or, where valuation is reliant on pricing models, whose model inputs cannot be externally validated;

o Assets whose changes in values cannot be adequately mitigated by effective hedging;

o New products with rapid growth, including those that do not have a market history;

o Assets or strategies that include significant embedded leverage;

o Assets or strategies that have demonstrated significant historical volatility;

o Assets or strategies for which the application of capital and liquidity standards would not adequately account for the risk; and

o Assets or strategies that expose the banking entity to large and significant concentrations with respect to sectors, risk factors, or counterparties;

Description and documentation of covered fund activities and investments. For each organizational unit engaged in covered fund activities and investments, the banking entity's compliance program must document:

o The covered fund activities and investments that the unit is authorized to conduct;

o The banking entity's plan for actively seeking unaffiliated investors to ensure that any investment by the banking entity conforms to the limits contained in § __.12 or registered in compliance with the securities laws and thereby exempt from those limits within the time periods allotted in § __.12; and

o How it complies with the requirements of subpart C.

~~III. Internal Controls~~ Internal Controls. A banking entity must establish, maintain, and enforce internal controls that are reasonably designed to ensure that its covered fund activities or investments comply with the requirements of section 13 of the BHC Act and this part and are appropriate given the limits on risk established by the banking entity. These written internal controls must be reasonably designed and established to effectively monitor and identify for further analysis any covered fund activity or investment that may indicate potential violations of section 13 of the BHC Act or this part.

~~A. Covered Trading Activities~~

~~A covered banking entity must establish, maintain, and enforce written internal controls that are reasonably designed to ensure that the trading activity of each trading unit is appropriate and consistent with the description of mission, strategy, and risk mitigation for each trading unit contained in its written policies and procedures. These written internal controls must also be reasonably designed and established to effectively monitor and identify for further analysis any covered trading activity that may indicate potential violations of section 13 of the BHC Act and this part and to prevent actual violations of section 13 of the BHC Act and this part. Further, the internal controls must describe procedures for remedying violations of section 13 of the BHC Act and this part. The written internal controls must include, at a minimum, the following:~~

~~Authorized risks, instruments, and products. The covered banking entity must implement and enforce internal controls for each trading unit that are reasonably designed to ensure that trading activity is conducted in conformance with the trading unit's authorized risks, instruments, and products, as documented in the covered banking entity's written policies and procedures and trader mandates. At a minimum, these internal controls must monitor and govern:~~

~~The types and levels of risks that may be taken by each trading unit, consistent with the covered banking entity's written policies and procedures; The type of hedging instruments used, hedging strategies employed, and the amount of risk effectively hedged, consistent with the covered banking entity's written policies and procedures; and The financial contracts, products and underlying assets that the trading unit may trade, consistent with covered banking entity's written policies and procedures. Risk limits. The covered banking entity must establish and enforce risk limits appropriate for each trading unit, which shall include limits based on probabilistic and non-probabilistic measures of potential loss (e.g., Value at Risk and notional exposure, respectively), measured under normal and stress market conditions.~~

~~Analysis and quantitative measurements. The covered banking entity must perform robust analysis and quantitative measurement of its covered trading activities that is reasonably designed to ensure that the trading activity of each trading unit is consistent with its mission, strategy and risk management process, as documented in the covered banking entity's written policies and procedures; monitor and assist in the identification of potential and actual prohibited proprietary trading activity; and prevent the occurrence of prohibited proprietary trading. In addition to the quantitative measurements reported by the covered banking entity to [Agency] pursuant to appendix A to this part, each covered banking must develop and implement, to the extent necessary to facilitate compliance with this part, additional quantitative measurements specifically tailored to the particular risks, practices, and strategies of its trading units. The~~

~~covered banking entity's analysis and quantitative measurement must incorporate the quantitative measurements reported by the covered banking entity to [Agency] pursuant to Appendix A and include, at minimum, the following:~~

~~Internal controls and written policies and procedures reasonably designed to ensure the accuracy and integrity of quantitative measurements; Ongoing, timely monitoring and review of calculated quantitative measurements; Heightened review of a quantitative measurement when such quantitative measurement raises any question regarding compliance with section 13 of the BHC Act and this part, which shall include in-depth analysis, appropriate escalation procedures, and documentation related to the review, including the establishment of numerical thresholds for each trading unit for purposes of triggering such heightened review; and Immediate review and compliance investigation of the trading unit's activities, escalation to senior management with oversight responsibilities for the applicable trading unit, timely notification to [Agency], appropriate remedial action (e.g., divesting of impermissible positions, cessation of impermissible activity, disciplinary actions), and documentation of the investigation findings and remedial action taken when the quantitative measurement, considered together with the facts and circumstances, suggests a reasonable likelihood that the trading unit has violated any part of section 13 of the BHC Act and this part. Surveillance of compliance program effectiveness. The covered banking entity must regularly monitor the effectiveness of its compliance program and take prompt action to address and remedy any deficiencies identified. Any actions taken to remedy deficiencies and violations shall be documented and maintained as a record of the banking entity.~~

~~B. Covered Fund Activities~~

~~A covered banking entity must establish, maintain, and enforce internal controls that are reasonably designed to ensure that the covered fund activities or investments of its asset management units are appropriate and consistent with the description of the asset management unit's mission, strategy, and risk management process contained in the covered banking entity's written policies and procedures. The internal controls must, at a minimum, be designed to ensure that the covered banking entity complies with the requirements of § __.11 for any covered fund in which it invests, acts as sponsor, or organizes and offers, as well as the following:~~

~~The internal controls must, at a minimum require:~~

~~Monitoring investments in a covered fund. The covered banking entity must implement and enforce internal controls in a way that monitors and limits the covered~~ Monitoring and limiting the ~~banking entity's~~ banking entity's individual and aggregate investments in covered funds. ~~At a minimum, the covered banking entity shall establish, maintain, and enforce internal controls reasonably~~

~~designed to ensure that such investments are in compliance with section 13 of the BHC Act and this part at all times, including:~~

- ~~• Monitoring the amount and timing of seed capital investments for compliance with the limitations under subpart C (including but not limited to the redemption, sale or disposition requirements) of § ~~_.12~~ .12, and the effectiveness of efforts to seek unaffiliated investors to ensure compliance with those limits;~~
- ~~• Calculating the individual and aggregate levels of ownership interests in one or more covered funds fund required by § _.12; ~~Describing procedures for remedying violations of section 13 of the BHC Act and this part;~~~~
- ~~• Attributing the appropriate instruments to the individual and aggregate ownership interest calculations above; ~~and~~~~
- ~~• Making ~~the appropriate required~~ disclosures, in writing, to prospective and actual investors in any covered fund organized and offered or sponsored by the ~~covered~~ banking entity, as provided under § _.11(h). ~~Monitoring relationships with a covered fund. The covered banking entity must implement and enforce internal controls in a way that monitors and limits the covered banking entity's sponsorship of, and relationships with, covered funds. At a minimum, the covered banking entity shall establish, maintain, and enforce internal controls reasonably designed to ensure that such activities and relationships are in compliance with section 13 of the BHC Act and this part at all times, including monitoring for and preventing any relationship or transaction between the covered banking entity and a covered fund that is prohibited under § _.16. .11(a)(8);~~~~

~~Surveillance of compliance program effectiveness. The covered banking entity must regularly monitor the effectiveness of its compliance program and take prompt action to address and remedy any deficiencies identified. Any actions taken to remedy deficiencies and violations shall be documented and maintained as a record of the covered banking entity.~~

- ~~• Monitoring for and preventing any relationship or transaction between the banking entity and a covered fund that is prohibited under § _.14, including where the banking entity has been designated as the sponsor, investment manager, investment adviser, or commodity trading advisor to a covered fund by another banking entity; and~~
- ~~• Appropriate management review and supervision across legal entities of the banking entity to ensure that services and products provided by all affiliated entities comply with the limitation on services and products contained in § _.14.~~

~~Remediation of violations. The banking entity's compliance program must be reasonably designed and established to effectively monitor and identify for further analysis any covered fund activity or investment that may indicate potential violations of section 13 of the BHC Act or this part and to prevent actual violations of section 13 of the BHC Act and this part. The banking~~

entity's compliance program must describe procedures for identifying and remedying violations of section 13 of the BHC Act and this part, and must include, at a minimum, a requirement to promptly document, address and remedy any violation of section 13 of the BHC Act or this part, including § .21, and document all proposed and actual remediation efforts. The compliance program must include specific written policies and procedures that are reasonably designed to assess the extent to which any activity or investment indicates that modification to the banking entity's compliance program is warranted and to ensure that appropriate modifications are implemented. The written policies and procedures must provide for prompt notification to appropriate management, including senior management and the board of directors, of any material weakness or significant deficiencies in the design or implementation of the compliance program of the banking entity.

IVIII. Responsibility and Accountability for the Compliance Program

A ~~covered~~ banking entity must establish, maintain, and enforce a governance and management framework to manage its business and employees with a view to preventing violations of section 13 of the BHC Act and this part. A ~~covered~~ banking entity must have an appropriate management framework reasonably designed to ensure that: appropriate personnel are ~~made~~ responsible and accountable for the effective implementation and enforcement of the compliance program; a clear reporting line with a chain of responsibility is delineated; and the compliance program is reviewed periodically by senior management. The board of directors; ~~(or similar corporate body, and CEO reviews and approves the compliance program. This management framework must include, at a minimum:~~equivalent governance body) and senior management should have the appropriate authority and access to personnel and information within the organizations as well as appropriate resources to conduct their oversight activities effectively.

Corporate governance. The ~~covered~~ banking entity must ~~ensure that its~~adopt a written compliance program ~~is reduced to writing,~~ approved by the board of directors ~~or similar corporate body, and noted in the minutes,~~ an appropriate committee of the board, or equivalent governance body, and senior management.

~~Trader mandates. The covered banking entity must establish, maintain, and enforce the trader mandates required by this appendix to clearly inform each trader within a trading unit of his or her responsibilities for compliance with section 13 of the BHC Act and this part.~~

Management procedures. The ~~covered~~ banking entity must establish, maintain, and enforce ~~management procedures~~a governance framework that ~~are~~is reasonably designed to achieve compliance with section 13 of the BHC Act and this part, which, at a minimum, ~~provide~~provides for:

- The designation of ~~at least one person~~appropriate senior management or committee of senior management with authority to carry out the management responsibilities of the ~~covered~~

banking entity for each trading ~~unit~~desk and for each organizational unit engaged in covered fund activities;

• Written procedures addressing the management of the activities of the ~~covered~~ banking entity that are reasonably designed to achieve compliance with section 13 of the BHC Act and this part, including: ~~o Procedures for the review by a manager of activities of the trading unit and the quantitative measurements pursuant to appendix A and any other quantitative measurements developed and tailored to the particular risks, practices, and strategies of the covered banking entity's trading units;~~

~~o~~ A description of the management system, including the titles, qualifications, and locations of managers and the specific responsibilities of each person with respect to the ~~covered~~ banking entity's ~~trading units~~'s activities governed by section 13 of the BHC Act and this part; and

~~o~~ Procedures for determining compensation arrangements for traders engaged in underwriting or market making-related activities under § __.4 or risk-mitigating hedging activities under § __.5 so that such compensation arrangements are designed not to reward or incentivize prohibited proprietary ~~risk-taking~~trading and appropriately balance risk and financial results in a manner that does not encourage employees to expose the banking entity to excessive or imprudent risk.

Business line managers. Managers with responsibility for one or more trading ~~units or asset management units~~desks of the ~~covered~~ banking entity ~~engaged in covered trading activities or covered fund activities or investments~~ are accountable for the effective implementation and enforcement of the compliance program with respect to the applicable trading ~~unit or asset management unit~~desk(s).

Board of directors, or similar corporate body, and senior management. The board of directors, or similar corporate body, and senior management are responsible for setting and communicating an appropriate culture of compliance with section 13 of the BHC Act and this part and ensuring that appropriate policies regarding the management of trading activities and covered fund activities or investments are adopted to comply with section 13 of the BHC Act and this part. The board of directors or similar corporate body (such as a designated committee of the board or an equivalent governance body) must ensure that senior management is fully capable, qualified, and properly motivated to manage compliance with this part in light of the organization's business activities and the expectations of the board of directors. The board of directors or similar corporate body must also ensure that senior management has established appropriate incentives and adequate resources to support compliance with this part, including the implementation of a compliance program meeting the requirements of this appendix into management goals and compensation structures across the banking entity.

Senior management. Senior management is responsible for ~~communicating and reinforcing the culture of compliance with section 13 of the BHC Act and this part, as established by the board of directors or similar corporate body, and~~ implementing and enforcing the approved compliance

program. Senior management must also ensure that effective corrective action is taken when failures in compliance with section 13 of the BHC Act and this part are identified. ~~[4]~~ Senior management and control personnel charged with overseeing compliance with section 13 of the BHC Act and this part should review the compliance program for the banking entity periodically and report to the board, or an appropriate committee thereof, on the effectiveness of the compliance program and compliance matters with a frequency appropriate to the size, scope, and risk profile of the ~~covered~~ banking entity's ~~covered's~~ trading activities and covered fund activities or investments, which shall be at least ~~once every twelve months~~ annually.

~~Board of directors, or similar corporate body, and CEO. The board of directors, or similar corporate body, and CEO are responsible for setting an appropriate culture of compliance with this part and establishing clear policies regarding the management of covered trading activities and covered fund activities or investments in compliance with section 13 of the BHC Act and this part. The board of directors or similar corporate body must ensure that senior management is fully capable, qualified, and properly motivated to manage compliance with this part in light of the organization's business activities. The board of directors or similar corporate body must also ensure that senior management has established appropriate incentives to support compliance with this part, including the implementation of a compliance program meeting the requirements of this appendix into management goals and compensation structures across the covered banking entity.~~

CEO attestation. Based on a review by the CEO of the banking entity, the CEO of the banking entity must, annually, attest in writing to [Agency] that the banking entity has in place

processes to establish, maintain, enforce, review, test and modify the compliance program established under this Appendix and § __.20 of this part 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 United States operations of the foreign banking entity who is located in the United States.

IV. Independent Testing

~~A covered banking entity must ensure that independent testing is conducted by a qualified independent party, such as the covered banking entity's internal audit department, outside auditors, consultants, or other qualified independent parties, regarding the effectiveness of the covered banking entity's compliance program established pursuant to this appendix and § __.20 and the covered banking entity's compliance with this part. A banking entity must take appropriate action to remedy any concerns identified by the independent testing (e.g., remedying deficiencies in its written policies and procedures and internal controls, etc.).~~

~~The required independent~~Independent testing must occur with a frequency appropriate to the size, scope, and risk profile of the ~~covered~~ banking entity's ~~covered~~ trading and covered fund activities or investments, which shall be ~~no less than once every twelve months~~at least annually. This independent testing must include an evaluation of:

- The overall adequacy and effectiveness of the ~~covered~~ banking entity's compliance program, including an analysis of the extent to which the program contains all the required elements of this appendix;
- The effectiveness of the ~~covered~~ banking entity's ~~written policies and procedures~~; ~~The effectiveness of the covered banking entity's~~ internal controls, including an analysis and documentation of instances in which such internal controls have been breached, and how such breaches were addressed and resolved; and
- The effectiveness of the ~~covered~~ banking entity's management procedures. ~~VI. Training~~

A banking entity must ensure that independent testing regarding the effectiveness of the banking entity's compliance program is conducted by a qualified independent party, such as the banking entity's internal audit department, compliance personnel or risk managers independent of the organizational unit being tested, outside auditors, consultants, or other qualified independent parties. A banking entity must promptly take appropriate action to remedy any significant deficiencies or material weaknesses in its compliance program and to terminate any violations of section 13 of the BHC Act or this part.

V. Training

~~Covered banking~~Banking entities must provide adequate training to ~~trading~~ personnel and managers of the ~~covered~~ banking entity engaged in activities or investments governed by section 13 of the BHC Act or this part, as well as other appropriate supervisory, risk, independent testing, and audit personnel, ~~as determined by the covered banking entity~~, in order to effectively implement and enforce the compliance program. This training should occur with a frequency appropriate to the size and the risk profile of the ~~covered~~ banking entity's ~~covered~~ trading activities and covered fund activities or investments. ~~The training may be conducted by internal personnel or independent parties deemed appropriate by the covered banking entity based on its size and risk profile.~~

~~VI~~VII. Recordkeeping

~~Covered banking~~Banking entities must create and retain records sufficient to demonstrate compliance and support the operations and effectiveness of the compliance program. A ~~covered~~ banking entity must retain these records for a period that is no less than 5 years or such longer period as required by [Agency] in a form that allows it to promptly produce such records to [Agency] on request.

SHEARMAN & STERLING_{LLP}

~~END OF COMMON RULE~~

~~[END OF COMMON TEXT]~~