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August 17, 2020

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

The Honorable Maxine Waters
Chairwoman
The Honorable Patrick McHenry
Ranking Member
Committee on Financial Services
House of Representatives

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

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Department of the Treasury, Office of the Comptroller of the Currency (OCC); Board of Governors of the Federal Reserve System (Board); Federal Deposit Insurance Corporation (FDIC); Securities and Exchange Commission (SEC); and Commodity Futures Trading Commission (CFTC) (together, the agencies) entitled “Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds” (RINs: 1557-AE67; 7100-AF70; 3064-AF17; 3038-AE93; 3235-AM70). We received the rule on July 15, 2020. It was published in the *Federal Register* as a final rule on July 31, 2020. 85 Fed. Reg. 46422. The effective date of the rule is October 1, 2020.

According to the agencies, the final rule improves and streamlines the regulations implementing section 13 of the Bank Holding Company Act (BHCA), May 9, 1956, ch. 240, 70 Stat. 133, *classified at* 12 U.S.C. § 1841 *et seq.*, by modifying and clarifying requirements related to the covered fund provisions of the regulations. Section 13 of BHCA contains certain restrictions on the ability of a banking entity or nonbank financial company supervised by the Board to engage in proprietary trading and have certain interests in, or relationships with, a hedge fund or private equity fund (covered funds).

Enclosed is our assessment of the agencies’ compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to

the subject matter of the rule, please contact Shari Brewster, Assistant General Counsel, at (202) 512-6398.

A handwritten signature in black ink that reads "Shirley A. Jones". The signature is written in a cursive, flowing style.

Shirley A. Jones
Managing Associate General Counsel

Enclosure

cc: Shaquita Merritt
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Robert N. Sidman
Deputy Secretary
Commodity Futures Trading Commission

Vanessa A. Countryman
Secretary, Securities and Exchange Commission

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON A MAJOR RULE
ISSUED BY THE
DEPARTMENT OF THE TREASURY,
OFFICE OF THE COMPTROLLER OF THE CURRENCY;
FEDERAL RESERVE SYSTEM;
FEDERAL DEPOSIT INSURANCE CORPORATION;
SECURITIES AND EXCHANGE COMMISSION;
COMMODITY FUTURES TRADING COMMISSION (CFTC).
ENTITLED
“PROHIBITIONS AND RESTRICTIONS ON PROPRIETARY TRADING
AND CERTAIN INTERESTS IN, AND RELATIONSHIPS WITH,
HEDGE FUNDS AND PRIVATE EQUITY FUNDS”
(RINS: 1557-AE67; 7100-AF70; 3064-AF17; 3038-AE93; 3235-AM70)

(i) Cost-benefit analysis

The Securities and Exchange Commission (SEC) stated the final rule would (1) reduce the scope of entities that may be treated as covered funds (e.g., credit funds, venture capital funds, family wealth management vehicles, and customer facilitation vehicles), (2) modify existing covered fund exclusions under the implementing regulations (e.g., foreign public funds, public welfare funds, and small business investment companies), and (3) affect the types of permitted activities between certain banking entities and certain covered funds (e.g., restrictions on relationships between banking entities and covered funds, definition of “ownership interest,” and treatment of loan securitizations).

SEC estimated these provisions would reduce the burden on affected banking entities by codifying an existing policy statement by the federal banking agencies that addresses the potential issues related to a foreign banking entity controlling a qualifying foreign excluded fund and adopting a rule of construction to provide clarity regarding a banking entity’s permissible investments alongside a covered fund. SEC further estimated the final rule may enhance the beneficial economic impacts of the implementing regulations to the extent that it directly changes the scope of permissible covered fund activities, and indirectly reduces costs to banking entities and covered funds by reducing uncertainty regarding the scope of permissible activities.

According to SEC, the final rule may promote the ability of the capital markets to intermediate between suppliers and users of capital through, for example, increased ability and willingness of banking entities and investors in “covered funds” to facilitate capital formation through sponsorship and participation in certain types of funds and to transact with certain groups of counterparties. SEC also stated the final rule may benefit banking entities by providing clarity and removing certain constraints around potentially profitable business opportunities and by reducing compliance costs, and may benefit excluded funds and their banking entity sponsors and advisers by increasing the spectrum of available counterparties and improving the quality or cost of financial services available to customers. SEC further stated the final rule, however, may also facilitate risk mitigation as well as risk taking activities of banking entities. SEC also stated the final rule may also impact competition, allocative efficiency, and capital formation.

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

The Board of Governors of the Federal Reserve System (Board) stated the final rule is not expected to have a significant economic impact on a substantial number of small entities. The Department of the Treasury, Office of the Comptroller of the Currency (OCC), Federal Deposit Insurance Corporation (FDIC), and SEC each certified the final rule would not have a significant economic impact on a substantial number of small entities. The Commodity Futures Trading Commission (CFTC) stated it believed the final rule would not have a significant economic impact on a small number of small entities.

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

OCC determined the final rule does not impose any new mandates so did not prepare an analysis under the Act.

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

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

On February 28, 2020, the agencies issued a proposed rule. 85 Fed. Reg. 12120. The agencies collectively received approximately 40 unique comments from banking entities and industry groups, public interest groups, and other organizations and individuals. In addition, the agencies received six letters related to the subject matter considered in the 2020 proposal prior to the formal comment period. The agencies responded to the comments in the final rule.

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

The agencies determined the final rule has information collection requirements (ICRs) under the Act. Each agency outlined its title, Office of Management and Budget (OMB) control number, and its estimated annual burden hours. OCC and FDIC, submitted the ICRs to OMB for review, and the Board reviewed its ICR under authority delegated to it by OMB. The ICRs are associated with OMB control numbers 1557-0309, 7100-0360, and 3064-0184.

Statutory authorization for the rule

The agencies promulgated the final rule pursuant to sections 27 *et seq.* of title 7; sections 1, 24, 92a, 93a, 161, 221 *et seq.*, 1461, 1462a, 1463, 1464, 1467a, 1811 *et seq.*, 1841 *et seq.*, 3101, 3102, 3108, and 5412 of title 12, United States Code.

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

As independent regulatory agencies, the agencies are not subject to the Order.

Executive Order No. 13,132 (Federalism)

As independent regulatory agencies, the agencies are not subject to the Order.