

ADVISORY | Dodd-Frank

January 13, 2012

VOLCKER RULE: CFTC PROPOSAL

On January 11, 2012, the U.S. Commodity Futures Trading Commission adopted proposed rules (the “CFTC Proposal”) implementing section 619 of the Dodd-Frank Act, commonly referred to as the “Volcker Rule.”¹ The CFTC Proposal is relevant to entities that will be subject to the Volcker Rule for whom the CFTC is the primary financial regulator.² The CFTC is requesting comments within 60 days after the publication of the CFTC Proposal in the Federal Register, which is expected to occur shortly. The Volcker Rule becomes effective on July 21, 2012.

The CFTC Proposal closely follows the notice of proposed rulemaking issued by the Federal Reserve Board, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation and the Securities and Exchange Commission in October of 2011 (the “Joint Proposal”), with the following modifications:³

- The CFTC has revised its version of the proposed common rules to make certain non-substantive CFTC-specific changes and to remove Subpart E, which is issued solely by the Federal Reserve Board.⁴
- The CFTC has included a number of supplemental questions in the preamble to the proposed common rules. The supplemental questions primarily solicit comment on the application of specific provisions to CFTC-regulated banking entities and the rationale for including or excluding such provisions in or from the CFTC’s version of the common rules. The CFTC also specifically requests comment regarding the general impact of the proposed rules on, among other things, market-making, liquidity and the competitiveness of the US financial services sector. See [Appendix A](#) to this alert for the supplemental questions.
- The CFTC notes in the preamble that its version of the market-making exemption in the common rules may ultimately be influenced by the agency’s final rulemaking further defining Swap Dealer under the Dodd-Frank Act.

The Commission voted 3-2 in favor of the CFTC Proposal, with Commissioners Scott O’Malia and Jill Sommers dissenting. In a statement, Commissioner O’Malia cited, among other things, concerns regarding the complexity of the rules and their extraterritorial reach, as well as on the ability of the CFTC to adequately enforce the rules as written.

¹ For an overview of the statutory provisions of Dodd-Frank that comprise the Volcker Rule, please see our previous client alert: [Final Volcker Rule Provisions \(July 21, 2010\)](#).

² CFTC registrants potentially subject to the Volcker Rule include Futures Commission Merchants (FCMs), Swap Dealers (SDs), Commodity Trading Advisors (CTAs), and Commodity Pool Operators (CPOs).

³ For an overview of the Joint Proposal, please see our previous client alerts: [Volcker Rule: Proposed Regulations – Covered Fund Provisions \(October 11, 2011\)](#) and [Volcker Rule: Proposed Regulations – Proprietary Trading Provisions \(October 11, 2011\)](#).

⁴ Subpart E addresses the conformance and transition periods applicable to the Volcker Rule.

If you would like to discuss the proposed regulations and our capabilities to assist you in the upcoming rulemaking process, please contact the following members of our firm:

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APPENDIX A

SUPPLEMENTAL QUESTIONS INCLUDED IN CFTC PROPOSAL

- 8.1 What is the best method for the CFTC and the other regulators to coordinate regarding the allocation of supervisory responsibilities under the proposed CFTC Rule?
- 14.1 Should the CFTC Rule's proposed definition of trading account include: (i) § __.3(b)(2)(i)(B), relating to Federal Banking Agencies' Market Risk Capital Rules; or (ii) §§ __.3(b)(2)(i)(C)(1),(2) and/or (4), relating to SEC registered dealers and dealers who have filed notice with the appropriate regulatory agency? Please explain the rationale for including or excluding the provisions in the proposed CFTC Rule.
- 30.1 Should the proposed CFTC Rule include the clarifying exclusion for certain positions taken by clearing agencies that are registered with the SEC under section 17A of the Exchange Act? Please explain the rationale for including or excluding the provision in the proposed CFTC Rule.
- 30.2 The CFTC notes that only the actual repurchase or reverse repurchase arrangements would be exempt from the definition of trading account, and not the collateral or position that is being financed by the repurchase or reverse repurchase arrangement. The CFTC further notes that if a banking entity used a repurchase arrangement to finance a purchase of a covered financial position, that covered financial position would be considered in the trading account if it satisfied, at the time of its purchase, one of the three prongs set forth in the definition of trading account. Is this treatment of repurchase and reverse repurchase arrangements appropriate for the proposed CFTC Rule?
- 64.1 Should the proposed CFTC Rule include the underwriting exemption? Please explain the rationale for including or excluding the provision in the proposed CFTC Rule.
- 87.1 Should the proposed CFTC Rule's market making exemption include the requirements set forth in §§ __.4(b)(2)(iv)(A),(C), (D) and (E), relating to SEC registered dealers and dealers who have filed notice with the appropriate regulatory agency? Please explain the rationale for including or excluding the provision in the proposed CFTC Rule.
- 88.1 Alternatively, to what extent should the CFTC incorporate concepts regarding market making from the Entities Definitions Rulemaking for purposes of section 13 of the BHC Act?
- 168.1 Should the proposed CFTC Rule include all of the required metrics? In particular, the Commission is interested in which metrics are most relevant for swaps, futures, and their related hedges. Please explain the rationale for including or excluding the provisions in the proposed CFTC Rule.
- 168.2 If the CFTC Rule reduces the number of required metrics, should both sets of covered banking entities described in sections III. A. (i) and III. A. (ii) of Appendix A be required to comply with the reduced number of required metrics?

- 177.1 Should the proposed CFTC Rule include the entire Appendix B (e.g., description of market-making in liquid exchange-traded equity)? Please explain the rationale for including or excluding certain provisions of Appendix B in the proposed CFTC Rule.
- 218.1 The proposed CFTC Rule defines a “covered fund” to include a commodity pool, as defined in section 1a(1) of the Commodity Exchange Act. Is the use of this definition of “commodity pools” too broad? For example, will this definition pull in additional pools that are not registered with the CFTC?
- 227.1 Should the proposed CFTC Rule cover securitization vehicles? Please explain the rationale for including or excluding securitization vehicles in the proposed CFTC Rule.
- 296.1 Should the proposed CFTC Rule include the securitization exemption in § __.13(d)? Please explain the rationale for including or excluding the securitization exemption in the proposed CFTC Rule.
- 302.1 Should the proposed CFTC Rule include the additional exemptions listed in section 13(d)(1)(J) of the BHC Act in Section __.14 (e.g., BOLI, certain acquisition vehicles)? Please explain the rationale for including or excluding the exemptions in the proposed CFTC Rule.
- 348.1 The CFTC seeks comment on the proposed rule’s effects on market-making and liquidity, the costs of borrowing by businesses and consumers, the prices of financial assets, and the competitiveness of the United States financial services sector. The Commission also solicits comment on the benefits that will result from the proposed regulations and how these benefits compare to the costs of complying with the proposed regulations. The Commission also solicits comment on the CFTC’s assessments of the costs and benefits of the regulations proposed herein.