Wednesday, October 6, 2010

DODD-FRANK TITLE VI TO SECURITIES AND EXCHANGE COMMISSION. **ACTION:** Request for comment.

<u>Sec. 619 – Prohibitions on Proprietary Trading and Certain Relationships with Hedge Funds and Private Equity Funds</u>

With regard to Section 13(d)(3) of the Bank Holding Company Act of 1956 as amended, any determination pertaining to capital and quantitative limitations must consider variability extremes in asset correlations during times of systemic duress. Further, personnel who have both theoretical- and experience-based operational experience in measuring and controlling the financial stability of interdependent books of business within and across multiple institutions, whether they be contract consultants or Federal employees, should be retained to validate this determination.

U.S. Senators Jeffrey Merkley and Carl Levin, in their letter dated August 3, 2010 regarding the Merkley-Levin provisions in sections 619-621 of the Dodd-Frank Act, share concern that some financial institutions already may have acted to evade the restrictions of these provisions. The Senators recommend "robust use of the strong anti-evasion authority." Some financial institutions may perceive any inflexibility in the definitions of "Hedge Fund" and "Private Equity Fund" as an opportunity to evade the restrictions; one route to effecting the Senators' recommendations could involve writing maximum flexibility into SEC rules, pursuant to Sections 13(e) and 13(h)(2) of the Bank Holding Company Act of 1956 as amended, to allow the SEC to adjust the scope of entities under the umbrella of "Hedge Fund" and "Private Equity Fund" as defined in the Investment Company Act of 1940.

The Securities & Exchange Commission must consider ensuring that their revised policies and activities explicitly, consistently, and regularly audit supervised institutions for functional evasions of the aforementioned provisions and Acts. Such supervision could involve significant taxpayer expense. Alternatively, the SEC might consider simply adjusting the stakes for noncompliance at the individual-employee level where managers can be reasonably expected to know the details of their back-to-front office operations, investments, or other activities – and therefore can accept personal responsibility for compliance via certification that their activities have involved no functional evasions. For example, the numerous certifications required of municipal bond issuer management, investment bankers and advisers, and counsel at transaction closings assure (at least for high-volume / high-profile conduit-issue participants whose livelihoods depend on truthful certifications) that the principals comply with state and Federal regulations. Redistributing compliance risk toward the individual-employee level could yield cost-efficient enforcement by increasing the downside risk to anyone attempting to evade rules – without requiring additional taxpayer resources.

Regardless of how the Securities & Exchange Commission determines to move forward with the requirements of the Dodd-Frank Act, the SEC must make a meaningful effort to obtain experienced non-legal personnel, whether they be contract consultants or Federal employees, who have back-to-front office operational and strategic expertise and insight into how, where, and why alternative asset managers might take evasive measures.

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