Lori Gayle Nuckolls, Esq.
[redacted]

September 16, 2018

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street SW, Suite 3E–218
Washington, DC 20219
Sent via email to: VolckerReg.Comments@occ.treas.gov, Re: Docket ID OCC–2018–0010

Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551
Sent via email to: regs.comments@federalreserve.gov, Re: Docket No. R–1608; RIN 7100–AF 06

Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429
Sent via email to: comments@FDIC.gov, Re: RIN 3064–AE67

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549–1090.
Sent via email to: rule-comments@sec.gov, Re: File Number S7– 14–18

Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
1155 21st Street NW
Washington, DC 20581.
Sent via email to: https://comments.cftc.gov, Re: RIN 3038–AE72

Re: Proposed Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds

Dear Agency Administrators,

I write in reference to the proposed revision of the 2013 Volcker Rule, 12 C.F.R. Part 44, collectively by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve, the Federal Deposit Insurance Corporations, the Securities and Exchange Commission and the Commodities Futures Trading Commission, (individually, an ''Agency,'' and collectively, the ''Agencies''). Please consider this letter to be a formal submission of comments upon this proposed rule amendment in response to the Notice of proposed rulemaking published by your Agencies in the *Federal Register*, on July 17, 2018, 83 Fed. Reg. 33432. All citations herein to proposed amendments to the Code of Federal Regulations reference the proposed rules of the Comptroller of the Currency only and parallel citation to the proposed rules of all Agencies has not been attempted.

The Purpose of the Proposed Amendment of the Volcker Rule

The Agencies state that the rationale and premise for the amendment of the Volcker Rule is the learning and improvement of the largest banking entities since the 2013 amendment of the Bank Holding Company Act (the "BHC") and the 2013 amendment to the Volcker Rule promulgated thereunder. In that, since 2013, the Agencies have found that the banking entities have engaged in detailed compliance under the 2013 BHC Volcker Rule. These requirements were intended to prevent great economic loss and distress from speculative, proprietary trading by the banking entities. (83 Fed. Reg. 33432, 33434 (July 17, 2018)).

The Agencies profess that the banking entities are more sophisticated, more prudent and consequently, less of a threat to the safety and soundness of the financial system if engaging in the purchase and sale of securities for their own account. Thus, the Agencies are amending the 2013 Volcker Rule to lessen the regulatory burden of reporting proprietary trading in order that compliance resources may be directed, instead, to profit making commercial activities. (83 Fed. Reg. 33432, 33434 (July 17, 2018)). The Agencies propose that the extent of reporting compliance required be determined by the monetary value of assets available to each individual banking entity for trading. The amendment creates three categories of banking entities with three different levels of reporting compliance. *Id,*

My comments are offered in request that the Agencies reflect upon the amendment of the Volcker Rule as it would govern those banking entities with no more than $1 billion in available trading assets, globally, including affiliates. This is the third and smallest designated tier of banking entities both within the American economy and international banking, subject to the proposed amendment of the Volcker Rule. The Agencies have designated these smallest of banking entities to be by definition those entities with ‘‘limited trading assets and liabilities.” (83 Fed. Reg. 33437 (July 17, 2018))(to be codified at 12 C.F.R. § 44.2(t)).

Creating a regulatory *safe harbor,* the amendment would exempt these smallest of banking entities, possibly for the first time, from all proprietary trading reporting compliance. Under the safe harbor, the small banking entities are not required to routinely file periodic proprietary trading reports with their respective agency. And, the small banking entities must only do so after notice of regulatory inquiry, and a request for evidence of compliance *ex post facto.* The amendment proposes to transfer the burden of proof as to proprietary regulatory compliance from the small entity to the Agency. (83 Fed. Reg. 33432, 33450 (July 17, 2018)).

The Agencies only grant this safe harbor to the small banking entities. This is done through the recognition by the Agencies of a "presumption of compliance." (83 Fed. Reg. 33460 (July 17, 2018)(to be codified at 12 C.F.R. § 44.20(g)). No small banking entity would bear the burden of demonstrating affirmatively on a periodic basis that its proprietary trading is in due compliance with governing regulatory proscriptions. The safe harbor also exempts the small entity from all compliance requirements as to potential conflict of interests. (83 Fed. Reg. 33432, 33441 (July 17, 2018)). With respect to large and mid size banking entities, as the first and second tiers regulated, the amendment merely lessens and does not completely remove requirements as to proprietary trading reporting and conflict of interest. (83 Fed. Reg. 33432, 33441 (July 17, 2018)). As the Notice states:

> [an] Agency may exercise its authority to rebut the presumption of compliance and require the banking entity to comply with the requirements of the rule applicable to banking entities that have moderate trading assets and liabilities. The purpose of this presumption of compliance would be to further reduce compliance costs for small and mid-size banks that either do not engage in the types of activities subject to section 13 of the BHC Act or engage in such activities only on a limited scale.

83 Fed. Reg. 33432, 33437 (July 17, 2018). I support the stated objectivities of the Agencies in formulating the amendments to the Volcker Rule in theory, yet I am uncertain and quite doubtful that these objectives will be fully achieved in practice without too great a compromise of the public interest,

As published in the Federal Register, with respect to the Volcker Rule:

> the Agencies are issuing this proposal … to amend the 2013 final [Volcker] rule [promulgated pursuant

> to section 13 of the Bank Holding Company Act, the "BHC Act"], in order to provide banking entities with **greater clarity** and certainty about what activities are prohibited and [the Agencies] seek **to improve effective allocation of compliance resources where possible.** The Agencies also believe that the modifications proposed herein would improve the ability of the Agencies to examine for, and make supervisory assessments regarding, compliance relative to the statute and the implementing rules. While section 13 of the BHC Act addresses certain risks related to proprietary trading and covered fund activities of banking entities, the Agencies note that the nature and business of banking entities involves other inherent risks, such as credit risk and general market risk. To that end, the Agencies have various tools, such as the regulatory capital rules of the Federal banking agencies and the comprehensive capital analysis and review framework of the [Federal Reserve] Board, to require banking entities to manage the risks associated with their activities. The Agencies believe that the proposed changes to the 2013 final rule would be **consistent with safety and soundness** and enable banking entities to implement appropriate risk management policies in light of the risks associated with the activities in which banking entities are permitted to engage under section 13.

(83 Fed. Reg. 33432, 33434 (July 17, 2018))(emphasis added). The proposed Volcker Rule amendment proposes to balance the principles governing the substantive public rights granted by federal law to the banking entities with public concern for the safety and soundness of the American banking system. The public interest includes the wellbeing of the global macroeconomic economy of the United States in the world, as well as the wellbeing of the microeconomic economy of the small community depository institution in rural and provincial American geographic areas. To achieve the purpose of the proposed Volcker Rule, the Agencies must safeguard both the American economy and individual financial institutions.

The Rationale for the Volcker Rule

The Volcker Rule is founded upon the perceived need to prevent depositary institutions and their defined affiliates from engaging in speculative, proprietary trading, deemed inherently too risk averse for the banking system. The Agencies offer a revision of compliance obligations incumbent upon banking entities engaged in certain proprietary trading activities which are expressly exempted from the general prohibitions by law. In doing so the Agencies would lessen the compliance and reporting requirements of banking entities concerning information regarding their proprietary trading activities

Still, the proposed amendment of the Volcker Rule remains conservative in that it would reinforce the time honored prohibitions begun with the Banking Act of 1933 (popularly known as the "Glass-Steagall Act"). (83 Fed. Reg. 33432, 33436 (July 17, 2018)). The Agencies expressly state that the new rights as to proprietary trading reporting compliance must abide preexisting prohibitions regarding certain types of securities activity. Most importantly, no trading activity by a banking entity may: (1) create a conflict of interest between the banking entity and a customer; (2) directly or indirectly create a material exposure to a high-risk asset or high-risk management strategy; nor (3) create a threat to the safety or soundness to the banking entity or the United States. *Id.*

The Glass Stegall Act provided, in Sections 2 and 20, that a depositary institution, or bank, could not affiliate in any manner with any corporation engaged primarily in the issue flotation, underwriting, public sale, or distribution of stocks, bonds or other securities. This created the existing barrier against conflict of interests by prohibiting an officer or director of a corporation involved in such securities activity from serving as a bank officer or director. Similarly, Sections 16 and 21 of the Glass Stegall Act created a reciprocal prohibition by preventing banks from issuing securities and by preventing underwriters from accepting deposits.

The Volcker Rule Amendment Lacks Guidance for Small Banking Entities

Even with the continued conservativism as to small banking entities, there is an absence of concern in both the Notice and the proposed regulation for the extent to which the amendment leaves small banking entities without the didactic guidance of federal regulation and compliance. The Agencies offer in explanation that the small banking entities do not in engage in proprietary trading to an extent necessary to merit the cost, time and effort required in complying with current regulation. And, foremost, little regulation of the smaller entities is indicated for the sake of the safety and soundness of the banking industry and American economy. The practices of small banking entities have not proved a source of economic risk and loss with systemic implications, as have, to a truly great extent, the commercial activities of the mid and larger size banking entities.

The safe harbor presumption of compliance provides small banking entities with reduced cost of compliance, for reasons that reducing their compliance burdens as well as reducing and more greatly systemizing compliance of the mid and larger size banking entities will promote profit and economic growth without risk. Yet, small banking entities more greatly defer to and rely upon agency expertise. Small entities have reduced access to the information gleaned from periodic compliance as well as the due diligence periodic compliance requires. The Agencies should supplement the newfound freedom from affirmative regulatory compliance, which the presumption of compliance provides, with greater oversight, guidance and public education as to the role and function of small banking entities in cities and their communities. The Agencies should transition the small banking entities, which with the larger entities merit the reduction in regulatory compliance, into the greater commercial activity and profit envisioned by the amendment.

Adhering to and satisfying the detailed requirements of regulations has over many years provided learning through compliance for the smaller entities beyond the information and management resources of larger entities, regardless of market. Such remains true for the larger banking entities. For example, the amendment requires the larger banking entities to self-tailor an in-house reporting system that would require analysis of regulation and the entity's commercial activities, a six-pillar compliance program. (83 Fed. Reg. 33436 (2018)) (proposed to be codified at 12 C.F.R. § 44.20(a)) and (83 Fed. Reg. 33560-33563 (2018))(proposed to be codified at app. to 12 C.F.R. Part 44). The larger entities would be required to analyze: (1) written policies and procedures; (2) internal controls; (3) managerial structures; (4) independent compliance reviews; (5) training and recordkeeping; and (6) metrics reporting requirements. (83 Fed. Reg. 33432, 33439 (July 17, 2018)). The Agencies provide guidance to the larger entities in imposed regulatory obligations found in the Appendix as published in the Notice and proposed rule. Yet, if the small entities are expected to be guided by these provisions without obligation, the level of their regulatory burden is not minimized, yet presumably increased as the financial markets changes over time and they must self-regulate.

While small entities are not so anonymously amorphous as to require as extensive a review and reporting system as those much larger, the small entities will no longer conduct business under the same incentive for compliance as once before. Even without an inability to self-govern and delegate in-house measures for avoiding improper proprietary trading, the small banking entities should be encouraged to work promptly upon the effective date of the amendment with the business school centers of the institutions of higher education in their areas to provide a national view of compliance in the ordinary course of business, Thus, if a routine audit generates an Agency request for documentation of compliance over many years, the small entity may comply.

The Agencies might ask the effect of replacing a detailed and stringent regulatory burden with a "presumption of compliance" in a small banking entity. Perhaps the Agencies should encourage: (1) the development of prudent market sophistication among competitors and customers as well as (2) collaboration among the administrators and staff of small banking entities with members of institutions of higher education on topics of financial institution regulation and management. Promoting sound self-governance would permit the amendment with all requisite safety and soundness in even the most remote and smallest of regions in the United States. For, a small banking entity might well be inadvertently less than conservative and less risk averse than it should be in its investments if it believes its only risk of noncompliance is in the course of its ordinary periodic audit. Evolving standards governing the presumption of compliance during after-the-fact reviews permit agency discretion, yet without some transition small entities may not as readily self-regulate to produce a revision of the compliance standards being removed with changes in the marketplace and the effectiveness of the presumption.

Under the proposed Volcker Rule, small banking entities in small cities and towns may no longer rely upon the overarching policies of federal agencies to temper the autocratic micromanagement of CEOs and Officers. The Agencies give rise to an affirmative vision of the banking industry within an international context through regulation and compliance review. The presumption of compliance requires a new approach by the Agencies in guiding the business decisions of the small banking entities with similar agency efficiency. This should be neither difficult nor costly for small banking entities possessing worldwide assets of less than $1 billion constitute only 2% of America’s banking entities according to the Notice. 83 Fed. Reg. 33432, 33440-33441 (July 17, 2018).

<u>In Conclusion</u>

I suggest that the small banking entity not be abandoned by the regulators and that the Agencies provide some guidance in behest of the public interest concerns of fair, just and equal commercial development throughout American cities, states and regions. A different systemic risk exists if an absence of regulation for those least able to self-regulate promotes fear among small banking entities and their customers and then, not for reasons of evasion or misplaced or imprudent motives, transactions are made merely for want of deference to the metaphysical guidance once perceptible above.

The Agencies together govern a complex and diverse financial industry, composed of many types of financial institutions and entities created by right and privilege under the laws the Agencies administer. The Agencies may only continually seek to achieve an equilibrium in the burden of regulatory compliance to be borne themselves as each a governing agency, and as to that burden to be borne by the public. In doing so, the Agencies guide all market stakeholders and thereby produce national prosperity and capital growth. The proposed amendment is a result of what the Agencies have gleaned from the marketplace and the amendment may readily promote public participation, research, discussion of policy making, examination and enforcement.

I thank you greatly for considering my comments on this rule. And, I may certainly be contacted as indicated above.

Sincerely,

Lori G. Nuckolls

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