



U.S. GOVERNMENT ACCOUNTABILITY OFFICE

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V. Countryman  
S7-14-18



B-331605

November 26, 2019

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; Commodity Futures Trading Commission, Securities and Exchange Commission: Prohibitions and Restrictions on Propriety 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); Federal Reserve System (Board), Federal Deposit Insurance Commission (FDIC); Commodity Futures Trading Commission (CFTC), Securities and Exchange Commission (SEC) (collectively, the agencies) entitled "Prohibitions and Restrictions on Propriety Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds" (RINs 1557-AE27, 7100-AF 06, 3064-AE67, 3038-AE72, 3235-AM10). SEC is the only agency that submitted this final rule as a major rule. The rule further stated that for SEC, the Office of Information and Regulatory Affairs (OIRA) designated this rule as a major rule, but that for FDIC and OCC, OIRA designated this rule as not a major rule. We received the rule on October 21, 2019. It was published in the *Federal Register* as a final rule on November 14, 2019. 84 Fed. Reg. 61974. The effective date of SEC's provisions of the rule is January 13, 2020.

This final rule amends the regulations implementing section 13 of the Bank Holding Company Act (BHC Act). Section 13 contains certain restrictions on the ability of a banking entity and 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. 12 U.S.C. § 1851. The agencies issued an initial final rule implementing section 13 of the BHC Act in December 2013. 79 Fed. Reg. 5535 (Jan. 31, 2014) (the 2013 rule). The final rule modifies the scope of permitted activities for all or a subset of banking entities and in many cases—according to the agencies—simplifies, tailors, or eliminates the application of certain aspects of the 2013 rule to reduce compliance and reporting burdens. The final rule includes the following: (1) a three-tiered approach to tailoring the compliance program requirements; (2) revisions to the definition

of "trading account"; (3) additional exclusions from the definition of "proprietary trading"; (4) changes to the exemptions from the prohibition on proprietary trading for underwriting or market making-related activities; (5) changes to the exemption from the prohibition on proprietary trading for risk mitigating hedging activities; (6) modifications to the limitations on the exception that permits certain foreign banking entities to engage in proprietary trading that occurs solely outside of the United States; (7) changes to the compliance requirements of the 2013 rule to eliminate the requirements in Appendix B of the 2013 rule; and (8) modifications that limit the application of the metrics reporting requirements to banking entities with significant trading assets and liabilities.

Enclosed is our assessment of SEC's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule, as among the agencies, the rule was designated as major only for SEC. 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 Janet Temko-Blinder, Assistant General Counsel, at [REDACTED].



Shirley A. Jones  
Managing Associate General Counsel

Enclosure

✓cc: 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 COMMISSION;  
COMMODITY FUTURES TRADING COMMISSION;  
SECURITIES AND EXCHANGE COMMISSION  
ENTITLED  
"PROHIBITIONS AND RESTRICTIONS ON  
PROPRIETARY TRADING AND CERTAIN INTERESTS IN, AND  
RELATIONSHIPS WITH, HEDGE FUNDS AND PRIVATE EQUITY FUNDS"  
(RINs: 1557-AE27, 7100-AF 06, 3064-AE67, 3038-AE72, 3235-AM10)

(i) Cost-benefit analysis

The Securities and Exchange Commission (SEC), Department of the Treasury, Office of the Comptroller of the Currency, Federal Reserve System, Federal Deposit Insurance Commission, and Commodity Futures Trading Commission (collectively, the agencies) conducted an economic analysis of this final rule. In the analysis, SEC focused on the potential effects of the final rule on SEC registrants, in their capacity as such, the functioning and efficiency of the securities markets, investor protection, and capital formation. SEC evaluated the impact of the rule on efficiency, competition, and capital formation. SEC discussed alternative approaches it considered, such as splitting banking entities into only two groups according to their trading assets and liabilities. SEC also discussed the costs and benefits of each portion of the rule, such as the portion of the rule defining "trading account."

SEC stated that in some instances it cannot quantify many of the effects because they are inherently difficult to quantify or because it lacks the information or data necessary to provide reasonable estimates. In the analysis SEC explains that some of the potential economic effects, such as effects on incentives that may give rise to conflicts of interest in various regulated entities and the efficacy of regulatory oversight under various compliance regimes, are inherently difficult to quantify. Moreover, some of the benefits, such as potential benefits for resilience during a crisis, are less readily observable under strong economic conditions and cannot be isolated from the effects of other post-crises regulatory efforts intended to enhance resilience.

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

SEC certified that this final rule will not have a significant economic impact on a substantial 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

As an independent regulatory agency, SEC is not subject to the Act.

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

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

On July 17, 2018, the agencies published a proposed rule. 83 Fed. Reg. 33432. The agencies received over 75 unique comments from banking entities and industry groups, public interest groups, and other organizations and individuals. In addition, the agencies received approximately 3,700 comments from individuals using a version of a short form letter to express opposition to the proposed rule. The agencies responded to the comments in the final rule.

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

The agencies determined that certain provisions of this final rule contain information collection requirements (ICRs) under the Act. The agencies reviewed the final rule and determined that the final rule revises certain ICR requirements that have been previously cleared under various Office of Management and Budget (OMB) control numbers. The ICRs have been submitted by OCC and FDIC to OMB for review and approval. The agencies estimated the burden of each ICR.

Statutory authorization for the rule

SEC promulgated this final rule pursuant to section 1851 of title 12, United States Code.

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

As an independent regulatory agency, SEC is not subject to the Order.

Executive Order No. 13,132 (Federalism)

As an independent regulatory agency, SEC is not subject to the Order.