MEMORANDUM

To: File No. S7-41-11

From: Division of Investment Management

Date: December 5, 2012

Re: Meeting with BlackRock

On December 5, 2012, representatives from BlackRock met with the following staff from the Division of Investment Management: Diane Blizzard, Associate Director, Tram Nguyen, Branch Chief, Paul Schlichting and Jane H. Kim. Attending from BlackRock were Barbara Novick, Vice Chairman, Head of Government Relations; Howard Surloff, Managing Director, Legal; Kathryn Fulton, Managing Director, Government Relations.

The BlackRock representatives discussed issues raised in their February 13, 2012 comment letter including the scope of the banking entity definition. At the meeting, BlackRock provided the attached summary of legal arguments.

Summary Legal Arguments for Exclusion of Certain Non-Bank Subsidiaries from Volcker Rule Definition of "Banking Entity"

1. Purpose and Policy of the Volcker Rule

    a. The Volcker Rule aims to prevent banking organizations, which benefit from access to government funds (via federal deposit insurance or access to the discount window), from using those funds to cover or support financial losses resulting from activities perceived to carry a higher degree of risk – in this case, proprietary trading and investing in hedge funds and private equity funds.

    b. Unconsolidated subsidiaries of banks appear to be captured by the Volcker Rule, even though they do not have access to the discount window or rely on customer deposits. We believe that certain unconsolidated subsidiaries are so removed from the banking business that they are outside the intent and spirit of the Volcker Rule.

2. Impact of the Volcker Rule on Asset Managers

    a. Co-investments limited to 3% of a fund's equity interests and overall co-investment limited to 3% of Tier I capital.
        i. Clients often seek greater amounts of co-investment to show that the asset manager has "skin in the game."
        ii. Larger businesses could be impacted by the Tier I capital aggregate limit.

    b. Only employees who directly provide services can invest in covered funds.
        i. At large organizations, senior management and many other key employees could be prohibited from investing in covered funds.
        ii. For closed-end funds, employees who change roles within a firm or are promoted may have to divest their interests at a significant loss.

    c. Current definition of "similar funds" is extraordinarily broad, with the potential to capture numerous long-only products globally that are not "hedge funds" or "private equity funds" in the traditional sense.

    d. Asset managers will be required to remove their name from covered funds.
        i. Asset managers generally invest significantly in their brands.
        ii. Particularly problematic if offshore retail funds (e.g., UCITS) are captured as "similar funds."

    e. Asset managers will be required to build costly compliance programs, with no corresponding benefit to taxpayers.

3. Volcker Rule Definitions

    a. The prohibitions of the Volcker Rule apply to "banking entities."

    b. Statutory definition of "banking entity" in the Volcker Rule includes:
        i. any insured depository institution;
        ii. any company that controls an insured depository institution;

iii. any company that is treated as a bank holding company for purposes of Section 8 of the International Banking Act of 1978; and
iv. any *affiliate or subsidiary* of [any of the foregoing].

c. The terms "affiliate" and "subsidiary" are not defined in the statutory text of the Volcker Rule.

d. The Proposed Rule[1] issued in October 2011 imports the definitions of "affiliate" and "subsidiary" from the Bank Holding Company Act of 1956 (the "BHC Act").

e. BHC Act definition of "subsidiary"
   i. the bank holding company directly or indirectly or acting through one or more other persons owns, controls, or has power to vote 25 per centum or more of any class of voting securities of the bank or company;
   ii. the bank holding company controls in any manner the election of a majority of the directors or trustees of the bank or company; or
   iii. the Federal Reserve Board determines, after notice and opportunity for hearing, that the bank holding company directly or indirectly exercises a *controlling influence* over the management or policies of the bank or company. [2]

4. Statutory Authority

   a. The Volcker Rule statute was drafted as a new section 13 of the BHC Act.

   b. We believe the Board of Governors of the Federal Reserve System (the "Board") and the other regulatory agencies charged with implementing the Volcker Rule (the "Agencies") are not bound to wholly incorporate the BHC Act definitions of "affiliate" and "subsidiary" into the Volcker Rule.

   c. The Board and the other Agencies have two alternative legal theories for choosing a different definition:

      i. Language of Dodd-Frank
         1. Section 2 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") states "As used in this Act, the [specific definitions set forth in Section 2 of the Dodd-Frank Act] shall apply, *except as the context otherwise requires* or as otherwise specifically provided in this Act."
            a. Section 2 of the Dodd-Frank Act includes definitions of "subsidiary" and "affiliate" that are the same as those in the BHC Act.
         2. Agencies can use different definitions *"as the context otherwise requires."*

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[1] Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds (proposed Oct. 11 and 12, 2011) (to be codified at 12 C.F.R. Pts. 44, 248 and 351 and 17 C.F.R. Pt. 255), available at http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20111011a1.pdf.

[2] 12 U.S.C. 1841(a)(2).

3. For example, in Section 618 of the Dodd-Frank Act, which focuses on the supervision of securities holding companies, Congress specifically defined "subsidiary" and "affiliate" by reference to their definitions in the BHC Act. Therefore, in this circumstance, the Agencies do not have the ability to choose another definition.
4. Congress did not choose to define "affiliate" or "subsidiary" in the Volcker Rule, and therefore the Agencies have authority to choose their own definition "as the context otherwise requires."

ii. Authority to interpret "controlling influence"
1. Pursuant to the language of the BHC Act definition of control, whether a "controlling influence" exists is determined by the Board.
2. The Board has the clear authority to determine what constitutes "controlling influence" for purposes of the Volcker Rule.
3. The meaning of "controlling influence" can be interpreted differently for purposes of the Volcker Rule, and does not have to impact the interpretation of that term for the rest of the BHC Act.

5. Alternative Proposals to Exclude Certain Non-Bank Subsidiaries

a. Controlling Influence Safe Harbor
i. Solely for Volcker Rule purposes, create a "safe harbor" from the BHC Act definition of "control" that no "controlling influence" will exist where:
1. the banking entity owns less than 25% of a company, and
2. the banking entity agrees that it will not directly or indirectly provide support to the company.

b. Characteristic-Based Exclusion
i. Solely for purposes of the Volcker Rule, exclude from the definition of "banking entity" a company that, although affiliated with a banking entity in some way:
1. has less than 25% of its equity owned by the banking entity and does not have its assets and liabilities consolidated with the assets and liabilities of the banking entity either on the consolidated financial statements of the banking entity or in the calculation of the risk-weighted assets of the banking entity for regulatory capital purposes;
2. is not managed or operated by the banking entity;
3. does not share the same name or a variation of the same name with any depository institution for corporate, marketing, promotional, or other purposes;
4. does not have (i) its obligations or performance or (ii) the obligations or performance of any covered fund it organizes and offers, guaranteed, assumed, or otherwise insured, directly or indirectly, by the banking entity; and
5. an Agency has not determined that the banking entity has taken actions with respect to the company that function as an evasion of the requirements of § 13 of the BHC Act.

c. Section 165(e) Bright Line Standard
    i. Substitute the three-part objective test set forth within the single-counterparty credit exposure limits section of the *Enhanced Prudential Standards and Early Remediation Requirements for Covered Companies.*[3]

    Under those standards, a company would "control" another company if it:
    1. owns or controls with the power to vote 25 percent or more of a class of voting securities of the company;
    2. owns or controls 25 percent or more of the total equity of the company; or
    3. consolidates the company for financial reporting purposes.

d. Regulatory Forbearance
    i. The Board can decline to apply the "controlling influence" standard in identifying banking entities subject to the Volcker Rule.

[3] Enhanced Prudential Standards and Early Remediation Requirements for Covered Companies, 77 Fed. Reg. 594 (Jan. 5, 2012) (to be codified at 12 C.F.R. Pt. 252).