Occupy the SEC

http://www.occupythesec.org

September 7, 2012

House Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Re: Request for Public Comment on Alternatives to the Volcker Rule

Dear Sirs and Madam:

This letter is being submitted in response to your request for public comment on alternatives to Section 619 of the Dodd-Frank Act, better known as the Volcker Rule.

As you are aware, the Treasury and five concerned regulatory agencies ("the Agencies") are currently in the process of finalizing the rules that will implement Section 619 of the Dodd-Frank Act. In February of this year, Occupy the SEC[1] submitted a 325-page comment letter in response to the proposed rule that had been issued by the Agencies.[2] In that letter, we detailed our concerns with the proposal and provided recommendations to strengthen the Volcker Rule. We applaud the Financial Services Committee ("FSC") for reconsidering the Volcker Rule, and fully expect that it will give due consideration to proposals to strengthen, and not just weaken, the Rule from its current form. Further, we urge the Financial Services Committee to address the shortcomings that we have identified in our comment letter, and to take legislative initiative to remedy those weaknesses in the language of Section 619. We would also encourage the members to exert pressure upon the regulators to tighten and fortify the Rule in its final form.

We remain concerned about the inordinate influence of the financial services lobby on legislative initiatives such as the proposed revision to the Volcker Rule under consideration here. The vast majority of comment letters that the Agencies received in connection with the Volcker Rule (numbering over 17,000) favored strengthened regulation. Unfortunately, based on data

[1] Occupy the SEC (http://occupythesec.org) is a group within the New York-based Occupy Wall Street ("OWS") protest movement. This letter represents the opinion of our group's members, and does not represent the viewpoints of OWS as a whole.
[2] Occupy the SEC, Comment Letter to SEC, FRB, OCC and FDIC on Section 619 of the Dodd Frank Act of 2010 (Feb. 13, 2012), *available at* http://www.occupythesec.org/letter/OSEC%20-%20OCC-2011-14%20-%20Comment%20Letter.pdf.

compiled by Public Citizen,[3] it appears that 36 of the 61 members of the House Financial Services Committee (59% of the membership) have gone on record in favor of weakening the Volcker Rule, by signing certain comment letters to the Agencies that echo industry lobbyists' positions. Shockingly, no member of the Committee submitted or signed a comment letter advocating strengthening of the Rule. The divergence between public support for the terms of the Rule and the opposition of many of the Committee members is a particular point of concern.

A. Recommendations for Strengthening Specific Provisions in the Volcker Rule

We recommend that the FSC adopt the following specific modifications to Section 619.

Loans
Section 619 exempts the sale or securitization of "loans" without defining that term. The Agencies' Proposed Rule implies that securities, derivatives, and commodity futures do not fall within the purview of exempted "loans," but we recommend that Congress explicitly define the contours of "loan" to read as follows:

Loan means any loan, lease, extension of credit, or secured or unsecured receivable. A loan shall not mean a position:

1. having the expectation of profits arising from a common enterprise which depends solely on the efforts of a promoter or third party,
2. in which there is common trading for speculation or investment, or
3. that materially has the characteristics of a commodity, security, or derivative.

Exclusion of Commodities
Section 619's coverage of commodities is troubling. The statute defines proprietary trading to include transactions in:

> any security, any derivative, any contract of sale of a commodity for future delivery, any option on any such security, derivative, or contract, or any other security or financial instrument that the appropriate Federal banking agencies, the Securities and Exchange Commission, and the Commodity Futures Trading Commission may, by rule as provided in subsection (b)(2), determine. [4]

The statute does not explicitly include spot commodities, instead referring to commodity futures and forwards. In the Congressional Record, Senator Merkley stated that the intent behind Section 619 was to define proprietary trading to cover "a wide range of financial instruments, including securities, commodities, futures, options, derivatives, and any similar financial instruments."[5] This colloquy suggests that a revised Volcker Rule should cover spot

[3] Public Citizen, Industry's Messengers: Congressional Recipients of Large Contributions from the Financial Services Sector Swamp Agencies With Requests To Weaken the Volcker Rule *passim* (Mar. 2012), http://www.citizen.org/documents/industrys-messengers-volcker-rule-report.pdf.
[4] 12 U.S.C. § 1851(h)(4) (2012).
[5] 156 Cong. Rec. S5895 (daily ed. July 15, 2010) (statement of Sen. Levin) (emphases added).

commodities as well. The expansive breadth of this language also militates in favor of the inclusion of foreign exchange and currency positions within the ambit of the Rule.

Underwriting

Section 619(d)(1)(B) exempts certain "underwriting . . . activities" from the prohibition on proprietary trading. This section is bereft of any mention of "private placement activities" or "placement agent." The Agencies have transgressed their delegated authority by allowing the underwriting exemption in the Volcker Rule to include private placements.

Under the basic securities law definition of the term, an "underwriter" includes "any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security."[6] Such a person is required to file a registration statement before offering to sell a security as part of a primary distribution.[7] Conversely, if a person is legally exempt from the registration statement requirement, that person cannot be an "underwriter" under Section 2(a)(11) of the Securities Act of 1933 ("'33 Act"). For example, a placement agent relying on the Rule 144 exemption is not considered an "underwriter."[8] Thus, the Section 2(a)(11) definition of underwriter would require that any underwriting activities permitted under the Volcker Rule be in connection with regulated securities.

Much to our chagrin, the Agencies have found a way to bypass this basic stricture. In defining the term "underwriter" in the Proposed Rule, the Agencies curiously rely on the definition of that term in Regulation M, instead of the more obvious and basic definition found at Section 2(a)(11) of the '33 Act.[9] Section 2(a)(11) has close to a century of case law and interpretive guidance supporting it, and is therefore more appropriate than the Regulation M definition. Regulation M is also a poor definitional source because the underlying purpose behind it conflicts with the underlying purpose behind the Volcker Rule. Regulation M was designed to prevent manipulation and other activities that could artificially influence the market for an offered security.[10] Thus, a broad interpretation of the term "underwriter" was naturally necessary in that context to promote greater investor protection and market stability. However, using the same broad interpretation of "underwriter" in the context of Section 619 would actually undermine

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[6] 15 U.S.C. § 80b-2(a)(11).
[7] 15 U.S.C. §§ 80b-4(1), 5(c).
[8] Preliminary Note to Rule 144, 17 C.F.R. § 230.144 (2012).
[9] *Compare* 17 C.F.R. § 242.100 (2011) (Regulation M definition) ("Underwriter means a person who has agreed with an issuer or selling security holder: (1) to purchase securities for distribution; or (2) to distribute securities for or on behalf of such issuer or selling security holder; or (3) to manage or supervise a distribution of securities for or on behalf of such issuer or selling security holder."), *with* 15 U.S.C.. § 77b(11) (2011) (Section 2(a)(11) definition of underwriter) ("The term 'underwriter' means any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking; but such term shall not include a person whose interest is limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission. As used in this paragraph the term 'issuer' shall include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer.").
[10] FINRA, *Regulation M Filings*, http://www.finra.org/Industry/Compliance/RegulatoryFilings/RegulationM/ (last visited Jan. 5, 2012).

investor protection, as it would increase the size of the underwriting loophole through which covered banking entities could conduct risky proprietary trading activities.

The FSC should enact clarifying legislation that would firmly define the exemption for "underwriting" to follow Section 2(a)(11) (should it deem such an exemption necessary in the first place).

Market Making

Market making is an indispensable component of liquid, efficient markets. This service, however, simply does not belong in banks. One of the most challenging aspects of our attempt to digest and comment on the Volcker Rule has been understanding the presupposition that government-backstopped banks have some inherently proper role in market making. We are familiar with the extensive lobbying efforts by the banking industry to present this idea as a fact, but we propose that the FSC seriously reconsider this premise for both the safety and soundness of the industry and the simplicity of this Rule.

It is our opinion that the Volcker Rule would be universally improved by removing the blanket exemption for market making, as this exemption creates great financial risk (by providing substantial opportunity for evasion) with limited commensurate economic benefit. As we explain below, market making and other currently-exempted activities can continue unabated at non-banks even after the implementation of the Volcker Rule.

Risk Mitigating Hedging

Our general interpretation of the Risk-Mitigating Hedging exemption is that any proprietary trade can be effectively disguised as the hedge to some risk, thereby facilitating evasion around the ban on proprietary trading. In an attempt to account for the substantial differences among traded instruments, the Rule has broadened the scope of permissible hedging activity to ubiquity.

The statute allows for aggregated hedging in Section 619(d)(1)(C), which is troubling and worthy of correction in a revised iteration of the Volcker Rule. An effective Volcker Rule would remove all implicit or explicit allowances for the dangerous practice of aggregated or "portfolio" hedging. Generally, a banking entity's need to engage in substantive aggregated hedging is actually indicative of a failure to appropriately mitigate risks at lower levels within the entity. Therefore, allowing this high-level hedging to continue unhindered runs counter to the underlying risk-mitigating purposes of the Rule.

The 'London Whale" fiasco, involving multi-billion dollar proprietary trading losses at JPMogan's Chief Investment Office (CIO), should serve as a wake-up call to the Committee to clarify the statutory language relating to the hedging exemption so as to preclude any firm from availing itself of the hedging exemption to surreptitiously run proprietary trades.

We strongly urge Financial Services Committee members who favor stronger financial reform to endorse these proposed changes and to submit comment letters to the Agencies to that effect.

B. <u>The Need for a Fortified Version of the Volcker Rule</u>

During the legislative process, the Volcker Rule was woefully enfeebled by the addition of numerous loopholes and exceptions. The banking lobby exerted inordinate influence on Congress and succeeded in diluting the statute, despite the catastrophic failures that bank policies have produced and continue to produce. We encourage the FSC to take the initiative to revamp the Volcker Rule into a stronger and more effective piece of legislation.

A fortified Volcker Rule has the potential to rein in certain speculative trading practices by banking entities that enjoy ready access to customer deposits and virtually limitless funding through various Federal Reserve programs. We encourage the members of the FSC to stand strong against the flood of deregulatory pressure that they have and will continue to face in connection with their proposed revision of the Volcker Rule. A vigorously implemented and enforced Volcker Rule would serve as insurance against the need for future bank bailouts funded by taxpayers. It would also reduce the risk of rampant macroeconomic inflation caused by the Federal Reserve's multi-trillion dollar bailout of banks.[11] Moreover, a strong Volcker Rule would reduce the risk of the FDIC having to replace missing deposits occasioned by heedless proprietary trading – a not-inconceivable possibility given the recent example of broker-dealer MF Global and its "missing" customer funds. In short, Congress must take advantage of this historic opportunity to protect the financial position of the average person living in the United States.

We recognize that many House Financial Services Committee members have been vehemently opposed to the Volcker Rule and its implementation. But the majority of informed members of the public are not. **Over 98% of commenters** to the Agencies' proposed Volcker Rule have expressed support for a strengthened version of the Rule, or an outright return to the Glass Steagall standard. A recent poll asked certified financial advisors, "Do you think the Volcker rule will make the financial system safer and healthier?"[12] 57% of close to 1400 respondents said yes. Similarly, Federal Reserve Governor Sarah Bloom Raskin has recently made a strong showing of support for the Volcker Rule, questioning whether banks that engage in proprietary trading actually provide any real benefit to the overall economy.[13] She further dismissed the notion that the Volcker Rule would curtail market liquidity, given that pure investment banks

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[11] A July 21, 2011 study by the Government Accountability Office indicated that the "total transaction amounts" for Federal Reserve lending actually totaled a staggering $16 trillion. U.S. Gov't Accountability Office, GAO-11-696, Opportunities Exist to Strengthen Policies and Processes for Managing Emergency Assistance Needed 131 (2011); *see also* Bill McGuire, *Fed Loaned Banks Trillions in Bailout, Bloomberg Reports*, ABC News, Nov. 28, 2011, http://abcnews.go.com/blogs/business/2011/11/fed-gave-banks-trillions-in-bailout-bloomberg-reports/. By comparison, the entire inflation-adjusted GDP of the United States as of the last quarter was only $13.35 trillion. Timothy R. Homan, *Economy in U.S. Surpasses Pre-Recession Level After 15 Quarters*, Bloomberg Businessweek, Oct. 31, 2011, *available at* http://www.businessweek.com/news/2011-10-31/economy-in-u-s-surpasses-pre-recession-level-after-15-quarters.html. To make matters worse, despite being on the Federal Reserve's dole, the same banks have continually issued outlandish bonuses to executives, largely as rewards for highly speculative transactions.

[12] Smartbrief, Financial NewsBrief: Reader Survey, Feb. 16, 2012, http://www.smartbrief.com/servlet/ArchiveServlet?issueid=95D40925-145E-4A6C-838D-58A1F486B83E&lmid=archives.

[13] M.J. Lee, *Bachus Considering Volcker Alternatives*, Politico, Aug. 7, 2012, *available at* http://www.politico.com/news/stories/0812/79461.html.

and hedge funds can continue to make markets that are vacated by banks covered under the Volcker Rule.[14] In fact, supporters of the Volcker Rule and other financial regulations are legion, and include many former insiders with an intimate knowledge of the operations of large banks, such as George Vasey of Merrill Lynch,[15] and Greg Smith of Goldman Sachs.

C. Fallacious Arguments Commonly Raised in Opposition to the Volcker Rule by Conflicted Members of the Financial Services Committee

Many members of the Financial Services Committee that have written letters to the Agencies in opposition to the Volcker Rule have essentially restated industry talking points in thinly-veiled language. Not surprisingly, these same Congresspeople have received millions of dollars in political donations from the financial services industry. Given this glaring conflict of interest, we urge members of the Committee to take more deliberate steps to properly consider alternative views regarding the Volcker Rule (including those in favor of the Rule), irrespective of funding sources.

A report compiled by Public Citizen[16] reveals the uncomfortably close linkages between industry donations and the tone and content of letters filed in opposition to the Rule. The attached spreadsheet summarizes these relationships, which we explore in more detail below

Chairman Bachus's Letter

In a letter dated December 7, 2011 ("Bachus letter"),[17] Chairman Spencer Bachus (R-Ala.) expressed various oft-repeated criticisms of the Volcker Rule. Joining him as cosigners were Rep. Jeb Hensarling (R-Texas), Rep. Scott Garrett (R-N.J.), and Rep. Shelley Moore Capito (RW.Va.). These Representative have received $5.1 million from the financial services industry since 2010.

This letter first repeats a standard industry talking point used against financial regulation, claiming that the Volcker Rule could "spark an exodus of clients from U.S. banks to competitors based overseas."[18] This statement echoes the Chamber of Commerce's viewpoints on the Volcker Rule: "If customers seek to use full-service financial firms, they may be forced to go overseas to engage in certain transactions, or engage other businesses that fall outside of the Volcker Rule prohibitions."[19]

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[14] *Id*.

[15] Travis Waldron, *Former Merrill Lynch Banker: Volcker Rule 'Necessary To Correct A Mistake That Poses A Danger To Our Economy'*, Thinkprogress: Economy, Apr. 17, 2012, http://thinkprogress.org/economy/2012/04/17/465811/former-merrill-banker-volcker/?mobile=nc.

[16] Public Citizen, *supra* note 3.

[17] Rep. Spencer Bachus, Comment Letter to Agencies (Dec. 17, 2011), *available at* http://www.federalreserve.gov/SECRS/2012/February/20120217/R-1432/R-1432_021312_105463_511628921984_1.pdf.

[18] *Id.*

[19] Center for Capital Markets Competitiveness of the United States Chamber of Commerce, Comment Letter to Financial Stability Oversight Council (Nov. 5, 2010), *available at* http://www.centerforcapitalmarkets.com/wp-content/uploads/2010/04/VOLCKER-11.5.2010-Final.pdf.

First, despite the extensive attention plied upon the Volcker Rule over the last two years, it can hardly be claimed that there has been an "exodus" of clients from U.S. banks, partly because foreign jurisdictions have themselves strengthened their regulations in light of bank excesses during the current financial crisis.

Indeed, it would be in American banks' best interest for Congress to revamp and fortify the Volcker Rule. Stable, customer-focused banks actually enjoy a competitive advantage as they are freed from the shackles of risk attendant to proprietary trading activities. This competitive advantage will create a first-mover advantage for American banks that pursue less risky, more productive activities. Foreign banks that continue to conduct proprietary trading will fail at higher rates, thereby undermining their competitiveness.

The Bachus letter also claims that the Rule will reduce liquidity across multiple markets. However, this claim loses sight of the fact that the Volcker Rule does not prohibit proprietary trading activities outright. Rather, the Rule only restricts banks that have an implicit government insurance policy from engaging in such activities. The "invisible hand of the free market," that darling cherub of neoliberal economics, will likely push much of the current proprietary trading into the folds of hedge funds or traditional investment banks, not eliminate them outright (assuming, of course, that such activities actually add productive value to the economy). The Volcker Rule simply removes the government's all-too-visible hand from underneath the pampered haunches of banking conglomerates.

The Bachus letter does correctly state one point: that as a matter of practice, banks may find it impossible to differentiate between permitted market-making and proprietary trading.[20] It is for this very reason that we have argued in favor of abandoning the market-making exemption to the ban on proprietary trading. This revision would move the Volcker Rule closer to the venerable Glass-Steagall Act standard, which protected the overall financial markets for seven decades. The Glass Steagall Act succeeded in keeping the country safe from major financial catastrophes of the type that preceded its creation (the Great Depression) and that proceeded its repeal (the recent Great Recession). Small wonder then that even the architects of the Act's repeal, such as John Reed and Sandy Weill of Citibank, have recently gone on record in support of a rejuvenated Glass Steagall standard.[21] Congress can achieve this goal by strengthening the Volcker Rule, and removing the market-making exemption and other glaring loopholes. The resulting regulation would materially approximate the Glass Steagall Act.

Rep. Neuegbauer's Letter

On December 20, 2011[22] Rep. Randy Neugebauer (R-Tex.) issued a letter, co-signed by 121 House members (including 22 members of the FSC), asking the Agencies to extend the initial

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[20] Bachus, *supra* note 17, at 1.

[21] *See* Bill Moyers, *John Reed on Big Banks' Power and Influence*, Moyers & Company, Mar. 16, 2012, http://billmoyers.com/segment/john-reed-on-big-banks-power-and-influence/; *see also* Evan Weinberger, *Despite Weill's Words, Breaking Up Banks Won't Be Easy*, Law360, July 25, 2012, http://www.law360.com/banking/articles/363653/despite-weill-s-words-breaking-up-banks-won-t-be-easy.

[22] Rep. Randy Neugebauer, Comment Letter to Agencies (Dec. 20, 2011), *available at* http://www.federalreserve.gov/SECRS/2012/March/20120301/R-1432/R-1432_021312_105460_511628140719_1.pdf.

deadline for comment to the Proposed Volcker Rule. These members of Congress received a combined $36 million in donations from the financial lobby.

The letter expressed concern about the Volcker Rule's costs to the American economy: "the rule, as drafted, would result in higher borrowing costs for American businesses, thereby impacting economic growth and job creation." Once again, these words seem to echo the viewpoints routinely expressed by pro-industry groups like the Securities Industry and Financial Markets Association (SIFMA), the American Bankers Association (ABA), the Financial Services Roundtable, and the Clearing House Association. The reasoning behind this claim is that the Volcker Rule will hamper so-called "liquidity" in all financial markets, thereby raising the cost of capital across the board. This argument overstates and mischaracterizes the Rule's impact.

First, it is important to differentiate between the financial products that actually drive economic growth (i.e. conventional loans), and the risky financial products upon which covered banks increasingly focus their capital (i.e. complex structured products).

Free from the enforced separation between commercial and investment banking, as originally required by the Glass-Steagall Act, banks now prefer to engage in self-interested proprietary trading rather than pursuing traditional banking activities that actually promote true "liquidity" across markets. Liquidity in opaque financial instruments may have increased in recent years, but real liquidity, which benefits consumers, investors, small business owners, and homeowners, has not followed suit. The inflation-adjusted Dow Jones Industrial Average is around the same level that it was in the mid-to-late 1990's.[23] Similarly, the income of the typical American family is at the same level that it was in 1996.[24] However, unlike in 1996, over 28% of American homes are "underwater."[25] The banking lobby's elixir, financial market liquidity, has done little to reverse this trend. We therefore urge Congress to take banks' animadversions regarding "liquidity" with a grain of salt.

The Volcker Rule may well increase borrowing costs in opaque financial products, but given the monumental damage caused by those products in the current financial crisis, we believe the public will actually benefit from such increased costs.

One can hardly argue that capital markets were inefficient or illiquid before the burgeoning of esoteric financial products in the last 15 years. After all, the late 1990's saw a burst of real economic growth driven by technological innovation, which was in turn dependent on the ready availability of capital. Indeed, many well-informed people believe that securitizations and similar "innovations" have no productive value other than as a fee generation mechanism for financial companies. For example, in describing structured finance derivatives, President Bill Clinton has stated that "[w]e created all these new securities which have no value and create no jobs."[26] In his view, the markets as a whole would be better benefited by longer-term, less

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[23] E.S. Browning, *Adjusted for Inflation, Dow's Gains Are Puny*, Wall St. J., Dec. 28, 2009.
[24] Conor Dougherty, *Income Slides to 1996 Levels*, Wall St. J., Sep. 14, 2011.
[25] John Gittelsohn, *U.S. 'Underwater' Homeowners Increase to 28 Percent, Zillow Says*, Bloomberg, May 9, 2011, *available at* http://www.bloomberg.com/news/2011-05-09/u-s-underwater-homeowners-increase-to-28-percent-zillow-says.html.
[26] Robert Lenzner, *Clinton's Cure For Capitalism*, Forbes.com, Sep. 25, 2009, http://www.forbes.com/2009/09/25/clinton-global-initiative-personal-finance-investing-ideas-bill-clinton.html.

complex forms of capitalization.[27] Paul Volcker has expressed a similar sentiment with respect to exotic financial instruments: “I wish someone would give me one shred of neutral evidence that financial innovation has led to economic growth—one shred of evidence.”[28]

These viewpoints have empirical support. A comprehensive survey of empirical economic data has revealed little evidence for the existence of the financial innovation that is giddily extolled by financial institutions and their proponents.[29]

Financial innovation goes hand-in-hand with increased concentrations of risk and pricing opacity. The banking model has shifted away from “old-fashioned” prudential banking of the George Bailey variety, in favor of an “originate and distribute” model that revels in risk-taking. “[T]he banker today pays less attention to credit evaluation since the interest and principal on the loans originated will be repaid not to the bank itself, but to the final buyers of the collateralized assets.”[30] From a Pareto-optimal, macroeconomic perspective, the markets would actually benefit if the Volcker Rule were to reduce “financial innovation” by government-backstopped banking entities.

Rep. Peters' et al's Letters

Several representatives suggested that the Volcker Rule should exempt venture capital funds. For instance, on February 17, 2012, Rep. Gary C. Peters (D-Mich.) and 24 of his House colleagues (recipients of $8.7 million in campaign contributions from the financial services industry since 2010) wrote:

> Congress treated venture capital funds differently than hedge funds and private equity funds because of the unique characteristics of their investment model … These characteristics mean that investment in venture capital funds does not pose a danger to the safety and soundness of the banking system or create systemic risk for the larger economy.[31]

Other letters from Rep. Anna Eshoo (D-Calif.), Rep. Bob Goodlatte (R-Va.), Rep. Michael Honda (D-Calif.), Rep. Jackie Speier (D-Calif.), Sen. Michael Bennet (D-Colo.) Sen. Barbara Boxer (D-Calif.), and a jointly signed letter from Sens. Thomas Carper (D-Del.) Scott Brown (R-Mass.), Christopher A. Coons (D-Del.), Mike Crapo (R-Idaho), Pat Toomey (R-Pa.) and Mark Warner (D-Va.) also sought exemptions for venture capital investments.

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[27] *See id*.
[28] Interview with Satyajit Das, *The Financial Zoo: An Interview with Satyajit Das – Part I*, Naked Capitalism, Sep. 7, 2011, http://www.nakedcapitalism.com/2011/09/the-financial-zoo-an-interview-with-satyajit-das-%E2%80%93-part-i.html (last visited Nov. 12, 2011) (“US financial services increased its share of value added from 2% to 6.5% but is that a reflection of your financial innovation, or just a reflection of what you're paid?”).
[29] *See* W. Scott Frame & Lawrence J. White, *Empirical Studies of Financial Innovation: Lots of Talk, Little Action?*, 42 J. Econ. Lit. 1 (2004).
[30] Anastasia Nesvetailova, *The End Of A Great Illusion: Credit Crunch And Liquidity Meltdown* 16 (2008), http://www.diis.dk/graphics/publications/wp2008/wp2008-23_credit_crunch_and_liquidity_meltdown.pdf.
[31] Rep. Gary C. Peters, Comment Letter to Agencies (Feb. 17, 2012), *available at* http://www.sec.gov/comments/s7-41-11/s74111-440.pdf.

Venture capital funds should not be exempted from the Volcker Rule. While venture capital is sometimes responsible for supplying needed capital that can create lasting businesses, very few venture-backed companies actually make it to a merger, and even fewer make it to the IPO stage. As Fred Wilson, partner at Union Square Ventures, noted: "Based on the NVCA statistics on the venture capital industry, there are on average 1,000 early stage financings every year."[32] Of that, "1–3% get to an IPO and 5–10% get to an M&A exit over $100mm. So 85–95% of all venture backed startups will either fail or exit below $100mm."[33] Venture capital funds are inherently risky, as the majority of such funds will either fail outright, or exit for less than $100 million. Thus, it would not be in the interest of the safety and soundness of the banking entities, or in the interest of the financial stability of the United States, to create a blanket exemption for venture capital funds.

Furthermore, a blanket exemption for venture capital funds would allow banking entities to house their proprietary trading activities under the guise of such funds, which already avail of many of the same exemptions from securities laws as hedge funds do. While we note that the SEC, in rule 203(l)-1 under the Advisers Act, sought "to distinguish venture capital funds from other types of private funds, such as hedge funds and private equity funds, and to address concerns expressed by Congress regarding the potential for systemic risk,"[34] we feel that at this stage Congress should not underestimate the ability of the banking entities to structure new entities that fall within the law but subvert its intent.

Thus, in order to prevent interests in hedge funds or private equity funds from being structured as venture capital funds and thereby circumventing the Volcker Rule, as well as to prevent banking entities from investing in yet another highly risky asset class, we **strongly oppose** an additional exclusion from the Volcker Rule for venture capital funds.

Rep. Himes' Letter

Rep. Jim Himes (D- Conn.), recipient of $1.7 million in financial lobby funds,[35] asked that the Agencies define "covered funds" to "specifically exclude all wholly owned subsidiaries and joint ventured used for ordinary course investing and transactions otherwise permitted by the Volcker Rule."[36] We find this suggestion, while well-meaning, to be superfluous. If certain subsidiaries and joint ventures of banks are truly engaged in ordinary loan-making and investing, then those activities will necessarily fall outside the scope of the Volcker Rule. Creating a *per se* exemption for subsidiaries, on the mere basis of their status as subsidiaries, would create obvious avenues for evasion around the Volcker Rule's restrictions.

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[32] A VC, *There Aren't Many Exits Over $100mm*, June 22, 2011, http://www.avc.com/a_vc/2011/06/there-arent-many-exits-over-100mm.html.

[33] A VC, *There Aren't Many Venture Backed IPOs*, June 23, 2011, http://www.avc.com/a_vc/2011/06/there-arent-many-venture-baced-ipos.html.

[34] Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than $150 Million in Assets Under Management, and Foreign Private Advisers, Investment Advisers Act Release No. 3222, 76 Fed. Reg. 39,646, 39,648 (July 6, 2011) (to be codifed at 17 C.F.R. §§ 275.202(a)(30)-1, 275.203(l)-1, (m)-1), *available at* http://www.sec.gov/rules/final/2011/ia-3222.pdf.

[35] Rep. Jim Himes, Comment Letter to Agencies (Mar. 16, 2012), *available at* http://www.fdic.gov/regulations/laws/federal/2011/11c284ad85.pdf.

[36] *Id*.

D. Conclusion

Section 619 of Dodd Frank is already law. The time for proposing a simple alternative to the Volcker Rule has come and gone. In our view, the energy of the Financial Services Committee's members should be directed at crafting novel legislative proposals that strengthen the existing law so that the regulators can craft a more efficient and straightforward set of rules. The FSC's quixotic quest to develop an industry-coddling Volcker alternative is the antithesis of what the American citizens demand and need. Taxpayers and consumers deserve protection from the predation of bankers who enjoy access to the public purse, coupled with financial immunity for their multi-billion dollar "mistakes."

Thank you.

Sincerely,
/s/
Occupy the SEC

George Bailey
Akshat Tewary
Elizabeth K. Friedrich
et al

Congressional Recipients of Large Contributions from the Financial Services Sector Aimed at Weakening Financial Regulation

Financial Services Committee Member	**Comment letters signed in support of/ opposition to strengthening the Volcker Rule**	**Financial Services Sector**
Totals	*Totals*	
34 Republicans (28 signed weakening letters) **27 Democrats (8 signed weakening letters)**	**17 letters to weaken the Volcker rule were signed by 172 House members (66.7 m received by FIRE donors to these members, avg 338K/per member)**	
	3 letters to strengthen signed by 20 members ($1.9M received an average $96k/per) No FSC member signed any of these letters	
	Democrats (Majority Party)	
Barney Frank, Massachusetts, Ranking Member		
Maxine Waters, California		
Carolyn B. Maloney, New York		
Luis Gutierrez, Illinois		
Nydia Velázquez, New York		
Mel Watt, North Carolina		
Gary Ackerman, New York		
Brad Sherman, California		
Gregory W. Meeks, New York	Signator on McCarthy memo	$643 thousand
Michael Capuano, Massachusetts		
Ruben Hinojosa, Texas		
William Clay, Jr., Missouri	Signator on McCarthy memo	$178 thousand
Carolyn McCarthy, New York	**Lead signator (17 signatures) Weaken**	$ 8.4 million Total ($476 thousand to McCarthy)
Joe Baca, California		
Stephen Lynch, Massachusetts		
Brad Miller, North Carolina		
David Scott, Georgia		
Al Green, Texas		

Emanuel Cleaver, Missouri		
Gwen Moore, Wisconsin	Signator on Peters memo Weaken & Signator on McCarthy letter	$311 thousand (2)
Keith Ellison, Minnesota		
Ed Perlmutter, Colorado	Signator on Peters memo Weaken	$852 thousand
Joe Donnelly, Indiana		
André Carson, Indiana		
Jim Himes, Connecticut	**Lead signator (1 signatures) Weaken Signator on Mcarthy letter**	$1.7 million
Gary Peters, Michigan	**Lead signator (24 signatures) Weaken & Signator on McCarthy letter**	$8.7 million ($778 thousand to Peters)
John Carney, Delaware	Signator on Peters memo Weaken & Signator on McCarthy letter	$199 thousand
*data came from: http://www.citizen.org/documents/industrys-messengers-volcker-rule-report.pdf		

Congressional Recipients of Large Contributions from the Financial Services Sector Aimed at Weakening Financial Regulation

Financial Services Committee Member	Comment letters signed in support of/ opposition to strengthening the Volcker Rule	Financial Services Sector
Totals	*Totals*	
34 Republicans (28 signed weakening letters) 27 Democrats (8 signed weakening letters)	**17 letters to weaken the Volcker rule were signed by 172 House members (66.7 m received by FIRE donors to these members, avg 338K/per member)**	
	3 letters to strengthen signed by 20 members ($1.9M received an average $96k/per) No FSC member signed any of these letters	
	Republicans (Majority Party)	
Spencer Bachus, Alabama, Chairman	**Lead signator (4 signatures) Weaken**	$5 million / (4) Scott Brown $3.6m, Warner 1M
Peter T. King, New York	Signator on Neugebauer letter	$454 thousand
Ed Royce, California	Signator on Neugebauer letter	$1.4 million
Frank Lucas, Oklahoma	Signator on Neugebauer letter	$378 thousand
Ron Paul, Texas		
Donald A. Manzullo, Illinois	Signator on Neugebauer letter	$412 thousand
Walter B. Jones, North Carolina	Signator on Neugebauer letter	$140 thousand
Judy Biggert, Illinois	Signator on Neugebauer letter & Signator on Mcarthy letter	$860 thousand
Gary Miller, California	Signator on Neugebauer letter	$389 thousand
Shelley Moore Capito, West Virginia	Signator on Bachus letter- Weaken	$5 million / (4)
Jeb Hensarling, Texas, Vice Chair	Signator on Bachus letter- Weaken	$5 million / (4)
Scott Garrett, New Jersey	Signator on Bachus letter- Weaken	$5 million / (4)
Randy Neugebauer, Texas	**Lead signator (121 signatures) Weaken**	$36 million/ 121 ($ 867 to Neugebauer)
Patrick McHenry, North Carolina	Signator on Neugebauer letter & Signator on Mcarthy letter	$565 thousand

John Campbell, California	Signator on Neugebauer letter	$743 thousand
Michele Bachmann, Minnesota		
Thaddeus McCotter, Michigan		
Kevin McCarthy, California		
Steve Pearce, New Mexico		
Bill Posey, Florida	Signator on Neugebauer letter	$374 thousand
Mike Fitzpatrick, Pennsylvania	Signator on Neugebauer letter	$172 thousand
Lynn Westmoreland, Georgia	Signator on Neugebauer letter	$309 thousand
Blaine Luetkemeyer, Missouri	Signator on Neugebauer letter	$437 thousand
Bill Huizenga, Michigan	Signator on Neugebauer letter	$137 thousand
Sean Duffy, Wisconsin	Signator on Neugebauer letter & Signator on McCarthy letter	$261 thousand
Nan Hayworth, New York	Signator on Neugebauer letter & Signator on McCarthy letter	$437 thousand
Jim Renacci, Ohio	Signator on Neugebauer letter & Signator on McCarthy letter	$226 thousand
Robert Hurt, Virginia	Signator on Neugebauer letter & Signator on McCarthy letter	$243thousand
Robert Dold, Illinois	Signator on Neugebauer letter & Signator on McCarthy letter	$501thousand
David Schweikert, Arizona	**Lead signator (1 signature) Weaken**	$328 thousand
Michael Grimm, New York	Signator on Neugebauer letter & Signator on McCarthy letter	$378 thousand
Quico Canseco, Texas		
Steve Stivers, Ohio	Signator on Neugebauer letter & Signator on McCarthy letter	$445 thousand
Stephen Fincher, Tennessee	Signator on Neugebauer letter	$283 thousand
*data came from: http://www.citizen.org/ documents/industrys-messengers-volcker-rule-report.pdf		