Commodity Futures Trading Commission

Office of Public Affairs

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Proposed Rule Regarding Prohibitions and Restrictions on Proprietary Trading (Volcker Rule)

The Commodity Futures Trading Commission (Commission) is proposing rules implementing the so-called "Volcker Rule" requirements of Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd Frank Act).

Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act)

Section 619 of the Dodd-Frank Act, among other things, generally prohibits two activities of banking entities.

- It prohibits federally insured depository institutions, bank holding companies, and their subsidiaries or affiliates (banking entities) from engaging in short-term proprietary trading of any security, derivative, and certain other financial instruments for a banking entity's own account, subject to certain exemptions.
- It prohibits owning, sponsoring, or having certain relationships with a hedge fund or private equity fund, subject to certain exemptions.

Section 619 also prohibits banking entities from entering into any transaction or engaging in any activity that would:

- Involve or result in a material conflict of interest,
- Result in a material exposure to high-risk assets or high-risk trading strategies,
- Pose a threat to the safety and soundness of the banking entity,
- Pose a threat to the financial stability of the United States.

To implement Section 619, the Commission is considering a proposal that would clarify the scope of the section's prohibitions and, consistent with statutory authority, provide certain exemptions.

The Commission's proposal to implement Section 619 is substantively similar to the joint rule proposal issued by the Board of Governors of the Federal Reserve System (the Board); the Office of the Comptroller of the Currency, Treasury (OCC), the Federal Deposit Insurance Corporation (FDIC); and the Securities and Exchange Commission (SEC) in October of 2011 (the Joint Volcker Rule). The Commission's proposal also includes several additional questions asking whether certain provisions of the Joint Volcker Rule are applicable to CFTC-regulated banking entities.

Proposed rules

The Commission's proposal to implement the so-called "Volcker Rule" requirements is substantively similar to the Joint Volcker Rule. Under the proposed rule, banking entities would be required to establish an internal compliance program that is designed to ensure and monitor compliance with the prohibitions and restrictions of Section 619, and the implementing regulations. The internal compliance program would be subject to oversight by the banking entity's board of directors and the appropriate federal supervisory agency.

The proposal also requires firms with significant trading operations to report to the appropriate federal supervisory agency certain quantitative measurements designed to assist the supervisory agency and banking entities in identifying prohibited proprietary trading from permitted activities.

The proposal also exempts transactions in certain instruments from the prohibition on proprietary trading, including obligations of:

- The U.S. government or a U.S. government agency,
- The government-sponsored enterprises,
- State and local governments.

Additionally, the proposal would exempt activities such as:

- Market making;
- Underwriting;
- Risk-mitigating hedging.

Notwithstanding the general prohibition on investments in, and certain relationships with, hedge funds and private equity funds, the statute contains several exemptions. The proposal, for example, would exempt:

- Organizing and offering a hedge fund or private equity fund under certain conditions, including limiting investments in such funds to a de minimis amount.
- Making risk-mitigating hedging investments.
- Making investments in certain non-U.S. funds.

This proposed rule also includes regulatory commentary intended to assist banking entities in distinguishing permitted market making-related activities from prohibited proprietary trading activities, and in identifying permitted activities in hedge funds and private equity funds. It also includes a number of elements intended to reduce the effect of the proposal on smaller, less-complex banking entities. For example, the proposal limits the extent to which smaller banking entities are required to report quantitative measurements.

Comment Period

This proposed rule will be open for public comment for 60 days following its publication in the Federal Register.