



## Neighborhood Economic Development Advocacy Project

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**Re: Docket No. FSOC-2010-0002, Public Input for the Study Regarding the Implementation of the Prohibition on Proprietary Trading and Certain Relationships with Hedge Funds and Private Equity Funds**

Dear Members of the Financial Stability Oversight Council:

Thank you for the opportunity to comment on the Financial Stability Oversight Council's study to inform the implementation of the Merkley-Levin ("Volcker Rule") provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Sections 619-621). We support strong and effective implementation of the Volcker Rule, and fully support the comments submitted by Americans for Financial Reform.

NEDAP is a resource and advocacy organization, based in New York City. NEDAP's mission is to promote community economic justice in New York and to eliminate discriminatory economic practices that harm communities and perpetuate inequality and poverty. NEDAP employs multiple strategies – including community outreach and education, advocacy, coalition organizing, policy research and analysis, media outreach, technical support for community groups, and direct legal services – to ensure that communities have access to fair and affordable credit and financial services, and to address inequities in the financial services system.

Irresponsible and reckless speculation by financial institutions brought the banking system to the brink of failure, at great cost to the economy and communities. The resulting taxpayer-funded bailouts did nothing to address the underlying causes of the financial institutions' instability, and failed to push them toward a more responsible and productive role in the economy. It is thus vital that the FSOC recommend the implementation of a strong Volcker Rule with clear prohibitions on risky practices to effectively limit trading and counter-party risks at banks and other financial institutions that are systemically important. Given that financial institutions are already hard at work seeking out loopholes in the law, regulators must be rigorous in rule writing and enforcement to ensure that financial institutions cannot subvert the fundamental principles of the Volcker Rule.

*1(ii). How can the Volcker Rule best serve to protect taxpayers and consumers and enhance financial stability by minimizing the risk that insured depository institutions and the affiliates of insured depository institutions will engage in unsafe and unsound activities?*

The recent financial crisis has exposed proprietary trading and other high-risk activities by banks and non-bank financial companies as practices that put both the financial institutions themselves and the economy as a whole at risk. The implementation of the Volcker Rule must allow regulators sufficient leeway to address risky practices that may arise from new financial instruments and trading strategies, or from financial institutions' attempts to evade the new

regulation. Regulators will need timely access to trade data, including all positions, counterparties, and funding sources, in order to identify problematic practices before they pose a threat to our financial stability. The FSOC should take all steps available to ensure that regulators have real-time access to these data in a format that allows for immediate analysis, and should recommend that the data allow regulators to identify prohibited trading practices, including trading against products structured for clients, and risky trading practices, such as funding illiquid trades with repurchase agreements.

Enforcement of the final rule should be made a priority by all regulators represented on the FSOC. Proprietary trading funded by short-term agreements, such as repos, have generated huge losses for banks and other systemically important financial institutions. Whether or not proprietary trading is profitable in any given moment, it is vital that the FSOC keep in mind the Volcker Rule's purpose and not overlook the very real risks to taxpayers and the economy posed by these risky practices.

*3. What are the key factors and considerations that should be taken into account in making recommendations on implementing the provisions of the Volcker Rule that restrict the ability of banking entities to invest in, sponsor or have certain other covered relationships with private equity and hedge funds?*

The exemptions for seeding and investing in hedge funds and private equity funds permitted by the Dodd-Frank Act will complicate both the rule-making process and enforcement of the regulations promulgated. It is vital that this exception remain limited and well-defined so that it does not undermine the purpose of the Volcker Rule. Although banks will be permitted to make seed investments and other limited investments in hedge funds and private equity funds, the FSOC must recommend that these investments not be used to mask proprietary trading or other prohibited activities and that they must be monitored to ensure that the risks to an individual bank cannot spread to the wider economy. Most importantly, it should be made clear that banks will not be permitted to bail out these funds under any circumstances, and banks should be required to disclose that limitation to customers. The FSOC should also recommend strict limits on the total leverage taken on by these funds when they are financed by banks.

*9. What factors and considerations should be taken into account in making recommendations to safeguard against evasion of the Volcker Rule?*

Financial institutions have every incentive to evade the Volcker Rule. The FSOC must recommend clear, enforceable rules, and vigorous data collection and analysis by regulators, and must ensure that the exceptions and extensions to the rule do not undermine its efficacy. The FSOC must recommend clear enforcement mechanisms and significant penalties to deter evasion, including meaningful protections for whistleblowers and clawbacks of profits and trader compensation from illegal trades.

Finally, we urge the FSOC and its members, both in this study and in the ultimate writing and enforcement of regulations, to define the exemptions in the law carefully and narrowly to limit the ability of financial institutions to circumvent the principles of the Volcker Rule.

Reckless speculation by financial institutions, fueled by financial deregulation, has led to tragic consequences for communities across the country. Particularly after the massive taxpayer bailout, the nation's largest financial institutions must bolster the real economy through responsible banking and lending practices, rather than continue to imperil the economy through risky trading practices. It is absolutely critical that regulators promote financial stability and economic equity through vigorous and effective rule-writing and enforcement of the Merkley-Levin/Volcker Rule.

Sincerely,

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