



The Outline

Overview and Understanding:



Situation:

The Federal Reserve, FDIC, OCC, CFTC, SEC approved §619 of the U.S. Dodd-Frank Act, also known as the [Volcker Rule](#), in Dec 2013. The law went into effect April 1, 2014 with a full compliance requirement by July 21, 2015. The statute:

Subpart B: Bans covered entities from engaging in Proprietary Trading (Out of scope for this outline);

Subpart C: Restricts investments (sponsoring, acquiring, or retaining an interest) in Covered Funds, and activities in connection with Covered Funds.

The Outline and the enclosed Presentation focus on Subpart C: Covered Funds requirements.

Banks are supposed to divest all covered funds held after December 31, 2013 by July 21, 2015. Thus **by now, banks should only have covered funds held prior to December 31, 2013**, which regulators have provided relief to extend the deadline to July 2016 (additional 1-year extension to July 2017 at discretion of the Federal Reserve is highly probable). For certain “qualifying illiquid funds” (in existence on May 1, 2010), regulators allow a transition period for a stable run-off of illiquid interests through 2022, but **exemption has to be obtained on a fund-by-fund basis**.

According to the OCC [analysis of 12 CFR Part 44](#), it estimated that U.S. banks held appropriate \$66 billion of impermissible assets. OCC assumed a fire sale would reduce prices by 5.5%. Therefore, **banks can at least expect \$3.6 billion from the required divestiture of impermissible assets**, such as CLO notes.

Per SIA Partners’ [briefing note](#), “**Bloomberg** has enlisted KPMG in an effort to evaluate the development of a tool that would be used specifically to determine whether or not a secondary trading instrument is or is not a covered fund simply by searching for its CUSIP in a specific database. The tool is **expected to be up and running by July 2016**. Participation in the industry wide effort has been quite **costly**, and the tool itself has **not yet proven to**



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provide significant added value, especially for certain American banking entities and Foreign Banking Organizations with significant covered funds activities outside of the United States.”

With reference to a Bloomberg’s [press release](#), “CFID uses nearly 30 data fields to extract relevant details from offering documents to classify securities”. From [public available information](#), we know Bloomberg’s offer has an identifier tag that “will deliver a wide variety of data sets, including an indicative flag called ‘covered funds yes’, ‘covered funds no’ or ‘needs legal review’”. **How many funds fall into Bloomberg’s ‘need legal review’ category is unknown.** This data license product “provides data feeds for clients to feed into databases ... subscribe to the premium service ... **The product will require banks selling securities via the (Bloomberg) terminal** to inform Bloomberg whether it is a covered fund ...” One bank counsel responded to IFLR inquires, quoted **“there will be a not insignificant subscription fee”** and Bloomberg is guarding the data very closely.

SIA further quoted that, “This cost (external counsel), combined with costs for external resources to complement the work of internal teams in organizing and performing the covered funds review process has easily added up to **approximately 15 million dollars or more for the majority of major financial institutions.**”

Objectives:

Based on initial conversations between [REDACTED] and Data Boiler Technologies (DBT), DBT understands [REDACTED] would like to:

- (1) identify covered funds in their global portfolio:
 - (i) Ensuring that the compliance program **provides a process for identifying** all covered funds that the banking entity sponsors, organizes or offers, and covered funds in which the banking entity invests;
 - (ii) ensuring that the compliance program provides a method for **identifying** all funds and pools that the banking entity **sponsors or has an interest in** and the type of exemption from the Investment Company Act or Commodity Exchange Act (whether or not the fund relies on section 3(c)(1) or 3(c)(7) of the Investment Company Act or section 4.7 of the regulations under the Commodity Exchange Act), and the amount of **ownership interest** the banking entity has **in those funds or pools**;
- (2) ensure ongoing conformance with the Volcker Rule covered fund requirements:
 - (iii) identifying, documenting, and mapping where any covered fund **activities** are **permitted to be conducted** within the banking entity; and
 - (iv) including an **explanation of compliance**;



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- (v) **describing** sponsorship **activities** related to covered funds; and
- (vi) establishing, maintaining and **enforcing internal controls** that are reasonably designed to ensure that its covered fund activities or investments comply with the requirements of section 13 of the BHC Act and subpart C, and
- (vii) **monitoring** of the banking entity's investments in and transactions with any covered funds.

█ looks for outside help in achieving the above two objectives and seeking an alternate vendor choice besides the Bloomberg's offer. DBT is in the process of evaluating the business requirements. Possibly we'll partner with an international Business Process Outsourcing (BPO) company and reference data provider to jointly prepare a suite of comprehensive services at a competitive price to give the industry an alternate choice for the Volcker Rule Covered Funds compliance.

Disclaimers:

In preparing for this outline and the enclosed presentation, DBT has reviewed the covered Funds requirements as suggested by Davis Polk and other regulatory compliance documents, while noted that:

- This outline and the enclosed presentation are for informational purposes only and do not constitute legal advice or create a client relationship.
- Please consult your own attorney for legal advice on the issues discussed in this outline and the enclosed presentation.
- Because of the generality of this outline, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations.



Presentation

Tasks and Assumptions:

Following tasks aim to augment [redacted] conformance with the Volcker Rule covered fund requirements. The suggested tasks are assumed to help substantiate that a given investment or activity does not qualify as covered fund nor does it imply relationships with covered funds. The task list may not be all encompassing. The information provided herein is generalized, and may not be applicable in all situations. Please consult your own attorney for legal advice on the compliance effectiveness discussed in this presentation.

Please to indicate [redacted] interest in the following Compliance Technologies (CT) and/or Business Process Outsourcing (BPO) or Consulting Services (CS).

✓	Sq.#	Tasks	Covered	248.10(C)	Remarks
<input type="checkbox"/>	1	Identify Registered Investment Companies (RIC) under the 1940 Act	No*	(b)(3)	EDGAR
<input type="checkbox"/>	1.1	Verify if the issuer is in compliance with SEC 1940 Act §18 requirements that imposes limitations on funds' issuance of "senior securities", generally prohibiting, among other things, a fund from issuing or selling any senior security representing indebtedness unless it maintains 300% asset coverage.	No*		Segregated account approach ; Alt - 2010 ABA Derivatives Report , the bifurcated approach set out in CESR's Global Exposure Guidelines
<input type="checkbox"/>	1.2	Identify Business Development Companies (BDC) - Section 54(a) 1940 Act	No*		Form N-6 & 54A; 1933/34Act N-2
<input type="checkbox"/>	2	Verify if issuer use 3(c)(1) or 3(c)(7) exemption	Yes*	(c)(12) Excluded Private Funds	SEC Rule 506 Reg. D
<input type="checkbox"/>	2.1	Verify other 1940 Act Exemption - Section 3(c)(3) Common Trust Funds	No		17CFR 270.3c-4, 15USC 80a3(c)(3)
<input type="checkbox"/>	2.2	Verify other 1940 Act Exemption - Section 3(c)(5) Certain Types of REITs	No		SEC Form S-11
<input type="checkbox"/>	2.3	Verify other 1940 Act Exemption - Section 3(c)(11) Pension & Profit Sharing Plans	No		Section 401 of title 26
<input type="checkbox"/>	2.4	Verify other 1940 Act Exemption - SEC Rule 3a-7 Asset-Backed Securities which entitle their holders to receive payments that depend primarily on the cash flow from static pool	No		<> 17 CFR 230.501(a) accredited investor / 230.144A private resales of securities to institutions
<input type="checkbox"/>	2.5	Verify if the issuers of certain mortgage-backed securities are sponsored by government-sponsored enterprises (GSEs)	No	FAQ#9	Flow of Funds Accounts of the US Table L.125 ; SIFMA - XLS
<input type="checkbox"/>	3	Identify Foreign Public Fund (Non-US Issuer)	No*	(c)(1)	<> 1940 Act, Form 6-K, annual



				Excluded Foreign Public Funds	report on Form 20-F / Form 40-F
<input type="checkbox"/>	3.1	<p>Validate Foreign Public Fund</p> <ul style="list-style-type: none"> public offering to retail investors >= 85% sold to investors that are not US person The fund sponsor is not a US Organized or located banking entity 	No		
<input type="checkbox"/>	3.1.1	<p>Validate Foreign Public Fund is not an affiliates of the U.S. Banking Sponsor</p> <ul style="list-style-type: none"> does not own, control, or hold with the power to vote >= 25% of the voting shares of the fund 	No*	FAQ#14	§248.12(b)(i)
<input type="checkbox"/>	3.2	<p>Verify foreign issuer as if it was subjected to US securities laws (<101 beneficiary, is not and do not propose to make public offer; owned by qualified purchaser)</p>	No*	(c)(12) Excluded Private Funds	
<input type="checkbox"/>	3.2.1	<p>Verify if the foreign issuer may qualify for excluded private fund</p>	No		
<input type="checkbox"/>	3.3	<p>Document the seeding vehicles that will become a Foreign Public Fund</p> <ul style="list-style-type: none"> Written plan to document the banking entity's plan to market the vehicle to third-party investors and convert it into a foreign public fund within the time period specified in § 248.12(a)(2)(i)(B) of subpart C, and the banking entity's plan to operate the seeding vehicle in a manner consistent with the investment strategy, including leverage, of the issuer upon becoming a foreign public fund. 	No	FAQ#5	
<input type="checkbox"/>	4	<p>Identify Foreign Pension Funds</p> <ul style="list-style-type: none"> Organized and admin outside of the US for the benefit of foreign beneficiary; No single participant or beneficiary with a right to more than 5% of its assets or income. 	No	(c)(5) Excluded Foreign Pension or Retirement Funds	Section 897(l)(2)
<input type="checkbox"/>	5	<p>Verify if Wholly Owned Subsidiary / Joint Venture / Acquisition Vehicle met exclusions</p> <ul style="list-style-type: none"> JV exclusion is not met by an issuer that raises money from a small number of investors primarily for the purpose of investing in securities; The Rule intended to prevent the JV exclusion from being used as a 	No*	(c)(2), (c)(3), FAQ#15	Para support under guidance of legal counsel



		vehicle to raise funds from investors primarily for the purpose of profiting from investment activity in securities for resale or other disposition or otherwise trading in securities.			
<input type="checkbox"/>	6	Identify Loan Securitizations	No*	(c)(8) Exclusion for loan securitizations	Section 3(a)(79) of the Securities Exchange Act of 1934
<input type="checkbox"/>	6.1	Verify if assets & holdings of the issuers comprised solely of permissible interest rate derivatives or Foreign Exchange derivatives	No		
<input type="checkbox"/>	6.2	Verify if assets & holdings of the issuers comprised solely of Special Unit of Beneficial Interest (SUBIs) and Collateral Certificates	No		
<input type="checkbox"/>	6.3	Verify if assets & holdings of the issuers comprised solely of directly held loan	No		
<input type="checkbox"/>	6.4	Verify if assets & holdings of the issuers comprised solely of cash equivalents and securities received in lieu of debts previously contracted	No		
<input type="checkbox"/>	6.4.1	Verify if assets & holdings of the issuers comprised solely of other servicing assets that display characters of cash equivalents <ul style="list-style-type: none"> "Cash equivalents" mean high quality, highly liquid short term investments whose maturity corresponds to the expected or potential need for funds by the securitization and whose currency corresponds to either the underlying loans or the asset-backed securities. 	No	FAQ#4	any servicing asset that is a security must be a permitted security under § 248.10(c)(8)(iii)
<input type="checkbox"/>	7	Identify Asset-Backed Commercial Paper (ABCP) Conduits	No*	(c)(9) Excluded ABCP Conduits	https://www.imf.org/external/np/seminars/eng/2010/mcm/pdf/Rutan1.pdf
<input type="checkbox"/>	7.1	Verify if ABCP conduit: <ul style="list-style-type: none"> Issue only ABS comprised of a residual interest and ABS < 397 days Hold only permissible assets for a loan securitization Initial issuance, no secondary market purchases Commitment to provide 100% and unconditional liquidity coverage 	No		See 6.1 – 6.4
<input type="checkbox"/>	8	Identify Covered Bonds <ul style="list-style-type: none"> debt obligation issued by a foreign banking organization or an eligible entity that is a wholly-owned subsidiary of a foreign banking organization 	No*	(c)(10) Excluded Covered Bonds	Dual-recourse, claim in priority to unsecured, BV > notional value, Independent cover pool monitor
<input type="checkbox"/>	8.1	Verify if Covered Bond Entities own or hold dynamic or fixed pool of loans and	No		See 6.1 – 6.4



		other permitted assets			
<input type="checkbox"/>	9	Verify if Small Business Investment Companies (SBIC) / Public Welfare Investment Funds / Qualified Rehabilitation Expenditures met exclusion	No	(c)(11)	SBA license#, 12USC24 CRA, IRC47
<input type="checkbox"/>	10	Verify if Separate Accounts – Insurance Co/ Bank Owned Life Insurance met exclusion	No	(c)(6) (c)(7)	Para support under guidance of legal counsel
<input type="checkbox"/>	11	Ongoing monitoring of entities regulated under the investment company act	Yes	(b)(3)	Fund-by-Fund Portfolio Mgt.
<input type="checkbox"/>	11.1	Verify if Financial Market Utilities (FMU) may rely on 3(b)(1) exemption to the definition of investment company	No*	(d)(1) non-specific	Business nature other than those that would make it an IC
<input type="checkbox"/>	11.2	Verify if Cash Collateral Pools may rely on sections 3(c)(1) and 3(c)(7) of the Investment Company Act to avoid being an investment company <ul style="list-style-type: none"> register cash collateral pools with the SEC as IC, or to operate pools as separate accounts to exclude from the covered fund definition 	No*	(d)(2) Non-specific	See 2
<input type="checkbox"/>	11.3	Verify if Pass-through REITS may rely on sections 3(c)(1) and 3(c)(7) of the Investment Company Act to avoid being an investment company (See 2) <ul style="list-style-type: none"> Pass through statutory trust between the banking entity and the REIT may not rely on the exclusion contained in section 3(c)(5) or 3(c)(6) 	No*	(d)(3) Not-specific	3(c)(5) not engaged in business of issuing redeemable securities... 3(c)(6) engaged in business other than investing, reinvesting ...
<input type="checkbox"/>	11.4	Verify if Employee Securities Companies may rely on exemption available under section 80a-6(b) of the Investment Company Act <ul style="list-style-type: none"> ... shall apply, the Commission ... weight ... form of organization and the capital structure ..., the persons by whom its voting securities, evidences of indebtedness, and other securities are owned and controlled, ... 	No*	(d)(7) Not-specific	Form S-8
<input type="checkbox"/>	11.5	Verify if certain mortgage-backed securities issuers sponsored by government-sponsored enterprises ("GSEs") may rely on an exclusion or exemption from the definition of investment company	No*	FAQ#9	Section 2(b) of Investment Company Act
<input type="checkbox"/>	12	Ongoing monitoring of Commodity Pools <ul style="list-style-type: none"> exempt pool status under CFTC Rule 4.7(a)(1)(iii) QEP only, no units have been publicly offered 	Yes	(b)(2)	NFA Form 7-R
<input type="checkbox"/>	13	Verify if Municipal Securities Tender Option Bond Transactions may rely on exclusion for loan securitizations <ul style="list-style-type: none"> not permitted to provide credit enhancement, liquidity support, and other 	No*	(d)(4) Not-specific	Section 13(g)(2) of the BHC Act, See 6



		similar services if it serves in a capacity covered by section 13(f) with the tender option bond program <ul style="list-style-type: none"> If a tender option bond vehicle is a covered fund and an exclusion from that definition is not available, then banking entities sponsoring such a vehicle will be subject to the prohibitions in §.14 of the final rule and the provisions of section 13(f) of the BHC Act. 			
<input type="checkbox"/>	14	Verify if Credit Funds may rely on exclusion for joint ventures, or exclusion for loan securitizations <ul style="list-style-type: none"> partnerships with third-party capital and invest in loans or make loans or otherwise extend the type of credit that banks are authorized to undertake on their own balance sheet 	No*	(d)(6) Not-specific	See 5 and 6
<input type="checkbox"/>	15	Verify if Venture Capital Funds may be covered fund <ul style="list-style-type: none"> Permit from making a venture capital-style investment in a company, business, so long as That investment is not through or in a covered fund, such as through a direct investment made pursuant to merchant banking authority or through business development companies which are not covered funds. 	Yes*	(d)(5) Not-specific	section 13(d)(1)(G)

The List of Tasks to be continued ...

<input type="checkbox"/>	16	Would an entity that is formed and operated pursuant to a written plan to become a foreign public fund receive the same treatment (i.e. excludes from the definition of covered fund a registered investment company and business development company, including an entity that is formed and operated pursuant to a written plan to become one of these entities)?		FAQ#5	See 3
<input type="checkbox"/>	17	Is a registered investment company or a foreign public fund a banking entity subject to section 13 of the BHC Act and implementing rules during its seeding period?		FAQ#16	
<input type="checkbox"/>	18.1	May a banking entity's compliance program for market making-related activities include objective factors on which a trading desk may reasonably		FAQ#17	



		rely to determine whether a security is issued by a covered fund? Furthermore, may a market maker meet its compliance program requirements by making use of a shared utility or third party service provider that utilizes objective factors if the market maker reasonably believes the system of the shared utility or third party service provider will identify whether a security is issued by a covered fund?			
<input type="checkbox"/>	19	How do the requirements of section 13 of the BHC Act and the final rule apply to a banking entity during the conformance period? For instance, must a banking entity deduct its investment in a covered fund from its tier 1 capital prior to the end of the conformance period?		FAQ#3	
<input type="checkbox"/>	19.1	Is a banking entity required to deduct from its tier 1 capital an investment in a collateralized debt obligation backed by trust preferred securities retained pursuant to section 248.16(a) of the interim final rule (Qualifying TruPS CDO)?		FAQ#21	
<input type="checkbox"/>	20	Conditions require that the covered fund, for corporate, marketing, promotional or other purposes does not share the same name or a variation of the same name with the banking entity (or an affiliate thereof). What does it mean for a covered fund to share the same name or a variation of the same name with a banking entity?		FAQ#6	
<input type="checkbox"/>	21	Does the marketing restriction apply only to the activities of a foreign banking entity that is seeking to rely on the SOTUS covered fund exemption or does it apply more generally to the activities of any person offering for sale or selling ownership interests in the covered fund?		FAQ#13	
<input type="checkbox"/>	22	Section 248.14 Covered Transaction (Super 23A)		Section 14(a)-(d)	