

## CFTC Proposes Regulations to Implement the Volcker Rule

*If you have any questions regarding the matters discussed in this memorandum, please contact the following attorneys or call your regular Skadden contact.*

**Mark D. Young**  
Washington, D.C.  
202.371.7680  
mark.d.young@skadden.com

**George M. Gilbert**  
Washington, D.C.  
202.371.7516  
george.gilbert@skadden.com

**Daniel S. Konar II**  
Washington, D.C.  
202.371.7102  
daniel.konar@skadden.com

\* \* \*

*This memorandum is provided by Skadden, Arps, Slate, Meagher & Flom LLP and its affiliates for educational and informational purposes only and is not intended and should not be construed as legal advice. This memorandum is considered advertising under applicable state laws.*

1440 New York Avenue, NW,  
Washington, D.C. 20005  
Telephone: 202.371.7000

Four Times Square, New York, NY 10036  
Telephone: 212.735.3000

[WWW.SKADDEN.COM](http://WWW.SKADDEN.COM)

On January 11, 2012, the Commodity Futures Trading Commission (CFTC) voted 3-2 to propose regulations to implement Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act), commonly referred to as the “Volcker Rule.” The CFTC’s proposal follows the October 2011 Volcker Rule regulations proposed by the Office of the Comptroller of the Currency, the Department of the Treasury (OCC), the Board of Governors of the Federal Reserve System (Federal Reserve), the Federal Deposit Insurance Corporation (FDIC) and the Securities and Exchange Commission (SEC) in a joint release (Joint Release).

The Volcker Rule prohibits an insured depository institution (IDI), any company that controls an IDI, a bank holding company (BHC), and any subsidiaries or affiliates of IDIs or BHCs (collectively, “banking entities”) from engaging in proprietary trading, or acquiring or retaining an ownership interest in, or sponsoring, a hedge fund or private equity fund.<sup>1</sup> The Volcker Rule and the regulations that were proposed to implement the Volcker Rule in the Joint Release were the subject of a [Skadden Insights Special Edition](#) last November. The CFTC’s proposal only would apply to banking entities that also are CFTC registrants.

Public comments on the CFTC’s proposed regulations may be submitted to the CFTC individually or jointly to the OCC, the Federal Reserve, the FDIC, the SEC and the CFTC.

### Why is the CFTC proposing rules to implement the Volcker Rule?

The Dodd-Frank Act requires coordination by the federal banking agencies, the Federal Reserve, the SEC and the CFTC in developing and issuing the regulations to implement the Volcker Rule.<sup>2</sup> For its part, the CFTC is required to promulgate regulations to implement the Volcker Rule for any banking entity for which the CFTC is the “primary financial regulatory agency.”<sup>3</sup> The Dodd-Frank Act designates the CFTC as the primary financial regulatory agency for the following entities with respect to the activities that require registration under the Commodity Exchange Act (CEA):

- Registered swap execution facilities, swap data repositories, swap dealers and major swap participants;
- Registered derivatives clearing organizations;
- Registered futures commission merchants and introducing brokers;
- Registered commodity pool operators and commodity trading advisors;
- Registered retail foreign exchange dealers; and
- Any “registered entity” under the CEA.<sup>4</sup>

1 Dodd-Frank Act § 619(a), 12 U.S.C. 1851(a). The Volcker Rule also imposes additional restrictions on nonbank financial companies that are supervised by the Federal Reserve, including companies that the Financial Stability Oversight Council has determined shall be subject to supervision by the Federal Reserve pursuant to Section 113 of the Dodd-Frank Act.

2 Dodd-Frank Act § 619(b)(2)(B); 12 U.S.C. 1851(b)(2)(B).

3 Dodd-Frank Act § 619(b)(2)(B)(i)(III); 12 U.S.C. 1851(b)(2)(B)(i)(III).

4 Dodd-Frank Act § 2(12)(C).

The Dodd-Frank Act also designates the CFTC as the primary financial regulatory agency for any board of trade that is designated as a contract market and any registered futures association. Accordingly, if any of the above-listed entities also is a “banking entity” (either through its status as an IDI or BHC, as affiliate or a subsidiary of an IDI or a BHC, or otherwise by virtue of controlling an IDI), then it is subject to the Volcker Rule and any implementing regulations adopted by the CFTC.

### **Does the CFTC’s proposal differ substantively from the Joint Release?**

The CFTC has proposed the same Volcker Rule regulations (and appendices) that were proposed by the banking agencies, the Federal Reserve and the SEC in the Joint Release, subject to one substantive difference.<sup>5</sup> The CFTC omitted from its proposed regulations Subpart E, which was included in the Joint Release by the Federal Reserve, acting alone, to incorporate rules regarding conformance periods for entities supervised by the Federal Reserve.

The CFTC has characterized the overview and section-by-section analysis in the preamble to its proposal as being “substantively consistent” with the same overview and analysis in the Joint Release, with the exception of 14 additional questions.<sup>6</sup> The CFTC has explained that any other discrepancies in these sections “are solely for stylistic purposes and are not intended to create any substantive differences between these sections of the [CFTC’s proposed Volcker Rule regulations] and the Joint Release.”<sup>7</sup>

### **How many entities would be subject to the CFTC’s Volcker Rule regulations?**

The CFTC’s proposal does not identify how many entities would be subject to the CFTC’s Volcker Rule regulations.<sup>8</sup> While such information would ordinarily be included in a CFTC rulemaking as part of the CEA’s required discussion of costs and benefits,<sup>9</sup> the CFTC stated that it has omitted such discussion because its Volcker Rule regulations are proposed exclusively under the Bank Holding Company Act of 1956, as amended (BHC Act), not the CEA.<sup>10</sup>

Further, the CFTC’s proposal does not account for the burdens of the information collections that would be required by the Volcker Rule regulations (as would ordinarily be required by the Office of Management and Budget) because such burdens were considered by the OCC and the Federal Reserve in the Joint Release.<sup>11</sup>

### **Would the CFTC’s proposal narrow the scope of “covered funds” where commodity pools are concerned?**

The Volcker Rule, subject to certain exceptions, prohibits a banking entity from sponsoring or investing in a hedge fund, a private equity fund or such “similar funds” as the banking agencies, the

5 [Proposal](#) at 354.

6 The CFTC’s additional questions are numbered: 8.1, 14.1, 30.1, 30.2, 64.1, 87.1, 88.1, 168.1, 168.2, 177.1, 218.1, 227.1, 296.1 and 302.1.

7 [Proposal](#) at 6 (footnote 13). Additionally, during the CFTC’s open meeting, Chairman Gensler and staff emphasized the importance of consistent application of the Volcker Rule regulations across regulatory agencies. [Transcript](#) at 184, 203, 213 and 230.

8 Further, during the January 11, 2012, meeting, staff stated they did not know how many registered entities would be subject to the CFTC’s Volcker Rule regulations. [Transcript](#) at 212.

9 7 U.S.C. § 19(a).

10 Section 619 of the Dodd-Frank Act amends Section 13 of the BHC Act. Therefore, the CFTC’s statutory authority to promulgate Volcker Rule regulations arises from the BHC Act, not the CEA.

11 [Proposal](#) at 305 (footnote 359).

Federal Reserve, the SEC and the CFTC determine appropriate.<sup>12</sup> The Joint Release proposed to refer to these collectively as “covered funds” and would specifically include commodity pools in the “covered funds” definition by way of the authority to designate similar funds. However, given the breadth of the definition of “commodity pool,” this proposed definition of “covered funds” has the potential to extend the Volcker Rule’s prohibition to entities not traditionally considered to be hedge funds or private equity funds. The potential implications of the definition of a “covered fund” in the Joint Release are explained further in our [Skadden Insights Special Edition](#).<sup>13</sup>

The CFTC proposal would not narrow the scope of “covered funds.” Rather, the CFTC has proposed a definition of a “covered fund” that is identical to the definition proposed in the Joint Release. The CFTC’s only contribution to the definition of a “covered fund” comes in the form of an additional question, Question 218.1, which asks: “Is the use of [the] definition of ‘commodity pools’ [in the definition of a ‘covered fund’] too broad? For example, will this definition potentially pull in additional pools that may be outside the intent of the proposed regulations?”<sup>14</sup> This additional question may be a recognition of the industry reaction to the proposed definition of “covered funds” in the Joint Release and an invitation for the industry to use the comment period to propose a more appropriate alternative.

### **What is the Impact of the CFTC’s Proposal?**

The CFTC’s Volcker Rule regulations were proposed three months to the day following the issuance of the Joint Release. Given this delay, some had anticipated that the CFTC’s proposal would attempt to address some of the issues identified in the Joint Release. Overall, the CFTC’s proposed regulations have not provided any further clarity as to how the Volcker Rule might be applied in practice.

---

12 Dodd-Frank Act § 619(h)(2); 12 U.S.C. 1851(h)(2). The Volcker Rule defines a hedge fund and a private equity fund as “an issuer that would be an investment company, as defined in the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), but for section 3(c)(1) or 3(c)(7) of that Act, or such similar funds. ...” *Id.*

13 [Skadden Insights Special Edition](#) at 24. A “commodity pool” is defined as any investment trust, syndicate, or similar form of enterprise operated for the purpose of trading in commodity interests.” 7 U.S.C. 1a(10). The definition of “commodity pool” is broad enough to include, for example, mutual funds, exchange traded funds and real estate investment trusts — none of which generally would be thought of as similar to hedge funds or private equity funds.

14 [Proposal](#) at 206.