Meeting between Federal Reserve Board Staff and Representatives of the Committee on Investment of Employee Benefit Assets February 23, 2012

Participants: Sean Campbell, Anna Harrington, James O'Brien, and Christopher Paridon (Federal Reserve Board)

William Donovan (United States Steel and Carnegie Pension Fund); David Felsenthal (Clifford Chance); Deborah Forbes (Association for Financial Professionals); and James Harshaw (GM Asset Management)

Summary: Staff of the Federal Reserve Board met with representatives and members of the Committee on Investment of Employee Benefit Assets ("CIEBA") to discuss the restrictions on proprietary trading and hedge fund and private equity fund activities under section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (also known as the "Volcker Rule").

Among matters discussed in the meeting were CIEBA's views regarding the proposed rule's distinction between prohibited proprietary trading and permitted market-making related activities and that it would be preferable for the proposed rule to err on the side of protecting market making in light of the need for pension plans to be able to sell assets, often highly illiquid ones, to banking entities. The CIEBA representatives expressed concerns that uncertainty surrounding the Volcker Rule and implementation of Basel III would result in negative effects on liquidity by the end of the year. The CIEBA representatives also indicated that in their view the more appropriate concerns that the Volcker Rule was intended to address are high concentration and volumes in certain assets, and that the Board and other agencies could use their supervisory authority to evaluate high concentrations and volumes after-the-fact on a case-by-case basis in order to determine whether positions or activities represent market-making.

In terms of more specific suggestions, the CIEBA representatives requested that the statutory requirement that permissible market-making activities "are designed not to exceed the reasonably expected near term demands of clients, customers, or counterparties," be interpreted softly in light of not only the need for client accommodation of pension plans that may have to unload positions to comply with fiduciary duties to pay out their beneficiaries, but also that dealers may not be able to find a perfectly offsetting trade on the other side and may need to take assets into inventory as a consequence. The CIEBA representatives expressed concerns with the criteria that the market making-related activities of the banking entity must be designed to generate revenues primarily from fees, commissions, bid/ask spreads or other income not attributable to appreciation in the value of covered financial positions and also noted that additional clarity is needed with respect to the requirement that the trading desk or other organizational unit that conducts the purchase or sale holds itself out as being willing to buy and sell the covered financial position for its own account on a regular or continuous basis in terms of the level of asset class granularity expected for this requirement.