THE VOLCKER RULE & INDUSTRIAL COMPANIES
Unnecessary Harmful Consequences

NAIB
National Association of Industrial Bankers

The Volcker Rule was intended to regulate certain trading and investment activities of banks, bank holding companies and their affiliates, such as broker-dealers. It restricts so-called proprietary trading – the purchase and sale of financial instruments for purposes of short-term profits – and sponsoring and investing in hedge funds and private equity funds. The Volcker Rule applies to companies that are not predominantly engaged in financial activities, but control an industrial loan company or industrial bank (ILC) or thrift. Therefore, they are treated as "banking entities" under the Volcker Rule's expansive definition of that term. Consequently, companies that are primarily engaged in industrial and commercial endeavors are now subject to significant regulatory burdens and activity limits imposed under the Volcker Rule.

Impact on Industrial Companies

• Regulatory Burdens: As a result of the Volcker Rule's failure to account for the important differences with Wall Street banks, industrial companies that hold a stake in a depository institution are faced with regulatory compliance burdens that were designed only for large financial institutions. These compliance burdens include establishing company-wide internal controls, periodic independent testing, training programs, record keeping, and written policies and procedures to monitor and limit certain trading and investment activities.

• Restricts Business Growth: Industrial companies frequently use financial products such as interest rate and foreign exchange derivatives and prime money market funds to mitigate the risks of commercial activities and ensure short-term liquidity. These are not speculative activities and do not pose any threat to financial stability. Indeed, in many cases they are actually permitted under the Volcker Rule. Nonetheless, engaging in these activities even in a tightly constrained manner could require industrial companies to implement extensive Volcker Rule compliance and monitoring programs on a company-wide basis. This is extraordinarily inefficient and does nothing to advance the safety of the U.S. financial system.

• Chills Investment: Including an industrial parent in the definition of "banking entity" could chill investment in the industrial company. That is because an investor that acquires more than 5% of the parent company could itself be a "banking entity" subject to the Volcker Rule, if other factors related to the investment are deemed to give it "control" for Volcker Rule purposes.

Need for Change

The Volcker Rule, while nominally focused on banks, actually applies to entire corporate groups. Action is needed for an appropriate balance between sound regulation of financial institutions and permitting industrial companies to operate without unnecessary restrictions. Left unaltered, the enforcement of the Volcker Rule (as currently written and interpreted) will have a disastrous effect on the American economy. Financial safety will not be enhanced, but capital investments to regulated entities will diminish over time. This situation strangles opportunities for small businesses, consumers and expansion of the credit pool.

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