THOMAS R. CARPER, DELAWARE, CHAIRMAN

CARL LEVIN, MICHIGAN
MARK L. PRYOR, ARKANSAS
MARY L. LANDRIEU, LOUISIANA
CLAIRE McCASKILL, MISSOURI
JON TESTER, MONTANA
MARK BEGICH, ALASKA
TAMMY BALDWIN, WISCONSIN
HEIDI HEITKAMP, NORTH DAKOTA

TOM COBURN, OKLAHOMA
JOHN McCAIN, ARIZONA
RON JOHNSON, WISCONSIN
ROB PORTMAN, OHIO
RAND PAUL, KENTUCKY
MICHAEL B. ENZI, WYOMING
KELLY AYOTTE, NEW HAMPSHIRE

RICHARD J. KESSLER, STAFF DIRECTOR
KEITH B. ASHDOWN, MINORITY STAFF DIRECTOR

United States Senate

COMMITTEE ON
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS
WASHINGTON, DC 20510–6250

March 20, 2013

The Honorable Ben S. Bernanke
Chairman
Federal Reserve Board of Governors
20th Street and Constitution Avenue NW
Washington, DC 20551

The Honorable Martin Gruenberg
Chairman
Federal Deposit Insurance Commission
550 17th Street, NW
Washington, DC 20429

The Honorable Thomas J. Curry
Comptroller of the Currency
Office of the Comptroller of the Currency
U. S. Department of the Treasury
Independence Square
250 E Street, N.W.
Washington, DC 20219

The Honorable Elisse Walter
Chairman
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

The Honorable Gary Gensler
Chairman
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

RE: Proposed Rule to Implement Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds

Dear Messrs. Bernanke, Curry, Gensler, and Gruenberg, and Ms. Walter:

The Merkley-Levin provisions prohibiting federal insured banks and systemically important financial institutions from engaging in high risk proprietary trading, also known as the "Volcker Rule," were enacted into law over two years ago. Your agencies first proposed rules to implement the Volcker Rule in October 2011. As of yet, however, those rules have not been finalized, and American families and businesses are not yet protected against the risks associated with banks' high risk proprietary trading.

While your agencies have deliberated over the final rule, there have been several reminders of why this rule is so important and why you should finalize it without delay. In that vein, please find enclosed a copy of a recent bipartisan staff report of the Permanent Subcommittee on Investigations entitled, "JPMorgan Chase Whale Trades: A Case History of Derivatives Risks and Abuses," which was released in connection with a Subcommittee hearing on March 15, 2013.

The Levin-McCain report summarizes a nine-month, bipartisan Subcommittee investigation into a complex set of synthetic credit derivative trades, also known as the whale trades, that caused a loss of at least $6.2 billion at JPMorgan Chase in 2012. Those derivatives trades represent exactly the type of high risk trading activity that the Volcker Rule was intended to prohibit at federally insured banks and their affiliates.

The 301-page report provides a useful case history addressing a variety of fact patterns and policy issues critical to effective implementation of the Volcker Rule. It provides examples of:

1) the risks inherent in a large portfolio of synthetic derivatives;
2) the value of requiring contemporaneous hedging documentation in distinguishing proprietary trades from risk-mitigating hedges;
3) the difficulty in reducing risks through so-called portfolio hedges, which carry their own substantial risks, as well as actions taken to disguise proprietary trading as portfolio or macro hedging activities or asset-liability management;
4) the need for strong derivatives valuation and risk assessment policies and procedures to prevent banks from understating or disguising the risks and losses associated with a complex derivatives portfolio;
5) the challenges facing regulators seeking to detect, measure, and track derivatives risks and losses; and
6) the magnitude of risks to U.S. banks that may arise from derivatives trading conducted by a non-U.S. affiliate.

The Levin-McCain report also offers a number of policy recommendations that I hope you will consider in connection with finalizing the Volcker Rule, and which supplement my previous comment letters to you. One of those recommendations, which would mandate the use of contemporaneous hedging documentation detailing the assets being hedged, how the hedge would reduce the risks associated with those assets, and how the hedge's effectiveness would be tested, was actually endorsed by JPMorgan Chase during the Subcommittee hearing. Another recommends that your agencies make use of the Section 619 legal authority to impose enhanced capital charges for derivatives trading characterized as a "permitted activity" under the Merkley-Levin provisions. The current proposal makes no use of this critical authority.

The enclosed report, as well as all materials related to the Subcommittee hearing on March 15, 2013, are submitted for your consideration and for inclusion in the administrative record supporting development of the final Volcker Rule. Thank you for your consideration of these additional comments.

Sincerely,

Carl Levin

Carl Levin
Chairman
Permanent Subcommittee on Investigations

cc: The Honorable Jacob J. Lew, Secretary of the Treasury
The Honorable Paul Volcker