

**American Public Power Association  
Council of Infrastructure Financing Authorities  
Government Finance Officers Association  
Education Finance Council  
International City/County Management Association  
International Municipal Lawyers Association  
Large Public Power Council  
National Association of Counties  
National Association of Health and Educational Facilities Finance Authorities  
National Association of Local Housing Finance Agencies  
National Association of State Auditors, Comptrollers and Treasurers  
National Association of State Treasurers  
National Conference of State Legislatures  
National Council of State Housing Agencies  
National League of Cities  
U.S. Conference of Mayors**

February 13, 2012

Ms. Jennifer J. Johnson  
Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> and Constitution Avenue, NW  
Washington, DC 20551

Mr. Robert Feldman  
Executive Secretary  
Federal Deposit Insurance Corporation  
ATTN: COMMENTS  
550 17<sup>th</sup> Street, NW  
Washington, D.C. 20429

Office of the Comptroller of the Currency  
250 E Street, SW  
Mail Stop 2-3  
Washington, D.C. 20219

Ms. Elizabeth Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549-1090

Proposed Rule Making:

- Board of Governors of the Federal Reserve System, [Docket No. R-1432] (RIN 7100-AD82)
- Federal Deposit Insurance Corporation, (RIN 3064-AD85)
- Office of the Comptroller of the Currency, [Docket No. OCC-2011-14] (RIN 1557-AD44)
- Securities and Exchange Commission, [Release No. 34-65545; File No. S7-41-11]

Dear Ladies and Gentlemen:

The organizations listed above represent states, counties, cities and other governmental entities and authorities that access the municipal bond market in order to provide critical infrastructure and services to their jurisdictions and communities. Our comments are directed to the proposed rulemakings referenced above, namely the proposed “Volcker Rule” related to Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act and specifically related to questions 120 and 124 in the proposed rule. We urge each agency above to replace the proposed exemption for obligations of states and political subdivisions so that it is consistent with the definition of “municipal securities” included in the Securities Act of 1934<sup>1</sup> (“the ‘34 Act”).

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<sup>1</sup> Section 3(a)(29) of the Securities Act of 1934.

The proposed rule appropriately seeks to exempt municipal securities from the section related to banking institutions engaging in certain proprietary trading activities in keeping with the statute and Congress' intent. However, the proposed rule would create an exemption for municipal obligations that is defined too narrowly as including only "obligations of states and political subdivisions thereof." This definition is grossly under-inclusive and differs from the well-established and relied upon definition of municipal securities that is found in the '34 Act - "obligations guaranteed as to principal or interest by, a State or any political subdivision thereof, or any agency or instrumentality of a State or any political subdivision thereof, or any municipal corporate instrumentality of one or more states, or any security which is in an industrial development bond." If made final, the definition in the proposed rule would exclude thousands of municipal securities, disrupting the municipal market and raising costs for state and local governments. Given that one of the principal purposes behind the Volcker Rule is to mitigate risk, the lack of uniformity would unfairly treat economically similar debt instruments differently from one another for the purposes of municipal securities trading. Additionally, "one-off" rulemaking should not be used to develop a new, separate definition of municipal securities.

Municipal debt is issued both by governmental entities themselves (e.g., states, cities, and counties) for their own purposes and also through statutorily defined authorities and agencies for defined, circumscribed, and critical purposes such as for water and sewer, electricity, airports, housing, health care and education. Due to the variety of ways in which debt can be issued pursuant to federal, state and local laws, most expert reviewers believe the definition in the proposed rule does not adequately capture our market and could leave at least 40% of the market exposed to Volcker Rule restrictions on proprietary trading, therefore limiting market liquidity and increasing costs for municipal securities. There is absolutely no indication that Congress contemplated or supported this severe bifurcation and distortion of the market. Indeed, other areas of financial regulation have interpreted "obligations of states and political subdivisions thereof" broadly to include all municipal securities in the '34 Act.

The narrow interpretation of which types of municipal securities are exempted under the proposed Volcker Rule would result in arbitrary distinctions between economically similar assets held by banks. For example, in some states, such as Georgia, a substantial portion of bonds issued for the purpose of financing water and sewer projects are supported by water and sewer system revenue and, due to requirements in state law, are issued as limited, direct government obligations. Under the proposed Volcker Rule, Georgia water and sewer bonds would generally be exempt from proprietary trading restrictions. In neighboring South Carolina, on the other hand, many water and sewer bonds, while also backed exclusively by water and sewer revenue, are issued by government authorities, not by governments themselves. South Carolina water and sewer bonds, while similar in many fundamental respects to Georgia water and sewer bonds, would be subject to Volcker Rule restrictions. There is no reasonable basis for such a distinction.

Moreover, expanding the exemption for municipal securities under the Volcker Rule would pose no additional risk to banks or the banking system. Municipal securities are among the safest assets in the U.S. capital markets. Default rates for municipal securities are among the lowest of all sectors of the capital markets, second only to bonds backed directly by the U.S. government. Banks have been active participants in the U.S. municipal bond market, holding nearly nine percent of the over \$3.7 trillion of municipal obligations outstanding, and have been active municipal bond investors for many decades. We are not aware of any cases where municipal securities holdings have caused safety and soundness problems for either individual banks or on a systemic basis.

We believe that the intent of the proposed Rule, as well as the Dodd Frank Act law itself, is to exclude all municipal securities from being captured under the Volcker Rule. Previous rulemaking by the agencies involved in developing the proposed rules demonstrates a more inclusive definition of municipal securities, mirroring the definition included in the Securities Act of 1934.

Again, we urge the Federal Reserve, OCC, SEC and FDIC to amend the exemption contained in the proposed rule and align it with the common definition of municipal securities found in the '34 Act that has served our country well for 80 years.

Thank you again for the opportunity to comment on this important issue.

Sincerely,

American Public Power Association, Amy Hille, 202-467-2929  
Council of Infrastructure Financing Authorities, Rick Farrell, 202-256-0298  
Government Finance Officers Association, Susan Gaffney, 202-393-8468  
Education Finance Council, Vince Sampson, 202-955-5510  
International City/County Management Association, Elizabeth Kellar, 202-962-3611  
International Municipal Lawyers Association, Chuck Thompson, 202-742-1016  
Large Public Power Council, Noreen Roche-Carter, 916-732-6509  
National Association of Counties, Mike Belarmino, 202-942-4254  
National Assn. of Health and Educational Facilities Finance Authorities, Chuck Samuels, 202-434-7311  
National Association of Local Housing Finance Agencies, John Murphy, 202-367-1197  
National Association of State Auditors, Comptrollers and Treasurers, Cornelia Chebinou, 202-624-5451  
National Association of State Treasurers, Jon Lawniczak, 859-244-8175  
National Conference of State Legislatures, Michael Bird, 202-624-8686  
National Council of State Housing Agencies, Garth Riemen, 202-624-7710  
National League of Cities, Lars Etkorn, 202- 626-3173  
U.S. Conference of Mayors, Larry Jones, 202-861-6709