

November 24, 2021

Office of the Comptroller of the Currency Issues Bulletin Regarding Investments in Venture Capital Funds

Bulletin Reminds Banks of Prohibitions that Apply to Most Equity Investments in Venture Capital Funds

Yesterday, the Office of the Comptroller of the Currency (the “OCC”) issued a bulletin to remind banks that they are generally prohibited from making equity investments in venture capital funds. The bulletin applies to national banks, federal savings associations and federal branches and agencies of foreign banking organizations. It does not impact the ability of bank holding companies and non-bank subsidiaries to make investments in qualifying venture capital funds under the new exclusion from the definition of “covered fund” in the amendments to the Volcker Rule adopted in June 2020.¹ In addition, the bulletin notes that equity investments in venture capital funds may be permissible for banks if they are public welfare investments or investments in small business investment companies.

Background

Under Section 13 of the Bank Holding Company Act of 1956, as amended (the “Volcker Rule”),² banking entities³ are generally prohibited from engaging in proprietary trading or investing in, sponsoring or having certain relationships with, “covered funds.” Since the rule’s initial adoption by the federal agencies (the “Agencies”)⁴ responsible for implementing the Volcker Rule in 2013, the definition of “covered fund” under the Volcker Rule has included most venture capital funds.

On June 25, 2020, the Agencies issued a final rule (the “Final Rule”) which streamlined the “covered funds” provisions of the regulations and permitted banking entities to engage in activities that the Agencies concluded do not raise concerns that the Volcker Rule was intended to address. One of the key

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amendments included in the Final Rule, which became effective on October 1, 2020, is a new exclusion from the definition of “covered fund” for “qualifying venture capital funds.”⁵

The amendments to the Volcker Rule, however, do not expand the authority of banks to make equity investments under applicable law. For example, national banks are restricted in their ability to make direct equity investments under 12 U.S.C. 24(Seventh) and 12 CFR part 1.⁶

The OCC Bulletin

OCC Bulletin 2021-54, issued on November 23, 2021, highlights the following matters:

- Banks generally may not make equity investments in venture capital funds.
- Equity investments in venture capital funds may be permissible if they are public welfare investments or investments in small business investment companies.
- Qualifying for the Volcker Rule's venture capital fund exclusion does not make a fund a permissible investment for a bank.
- As with any investment, before a bank invests in a venture capital fund, the bank must determine whether the investment is permissible and appropriate for the bank. Impermissible and inappropriate investments expose the bank and its institution-affiliated parties to enforcement actions and civil money penalties. National bank directors may be personally liable for losses in respect to impermissible investments.

The OCC bulletin notes, among other things, that it is an unsafe or unsound practice to make investments without determining their appropriateness. In addition, management should know and understand the risks and rewards of each equity security before purchasing, and should have a logical reason for the investment and know whether the investment is within legal limitations. Finally, the OCC bulletin notes that it applies to community banks. Although the bulletin does not directly apply to state banks, these institutions will also need to consider whether they are permitted to make equity investments in venture capital funds under applicable federal and state law.⁷

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ENDNOTES

- ¹ Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds, 85 Fed. Reg. 46,422 (July 31, 2020).
- ² 12 U.S.C. § 1841 *et seq.*
- ³ A “banking entity” is (1) any insured depository institution, (2) any company that controls an insured depository institution, (3) any company that is treated as a bank holding company for purposes of section 8 of the International Banking Act of 1978 (12 U.S.C. 3106), and (4) any affiliate or subsidiary of any entity described in (1), (2), or (3). 12 C.F.R. § 248.2.
- ⁴ The Agencies include the OCC, the Board of Governors of the Federal Reserve, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission and the Commodity Futures Trading Commission.
- ⁵ 12 C.F.R. § 248.10(c)(16). As a result of these amendments, banking entities are no longer subject to the prohibitions under the Volcker Rule on investing in or sponsoring venture capital funds as long as the conditions of the exclusion in the Final Rule are met.
- ⁶ Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds, 85 Fed. Reg. 46,422, 46,463 (July 31, 2020).
- ⁷ Under the Federal Deposit Insurance Act of 1950, insured state banks generally may not acquire or retain any equity investment of a type that is not permissible for a national bank. 12 U.S.C. 1831a(c).

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