



April 1, 2020

**BY ELECTRONIC TRANSMISSION**

The Honorable Joseph M. Otting, Comptroller  
Office of the Comptroller of the Currency (OCC)  
400 7th Street SW, Suite 3E-218  
Washington, DC 20219

**RE: Proposed Revisions to Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds (Docket ID OCC-2020-0002)<sup>1</sup>**

Dear Comptroller Otting:

On behalf of its membership, the Small Business Investor Alliance (“SBIA”) is pleased to submit the following comments in response to the above-referenced joint notice of proposed rulemaking by federal banking regulators to amend section 13 of the Bank Holding Company Act of 1958, as amended (the “Act”).<sup>2</sup>

The SBIA is the national organization that represents small business private equity funds and their investors, including Small Business Investment Companies (“SBICs”) and banks that invest in them. SBIA has filed comments, most recently in 2019, in support of the exclusion for SBICs from the definition of “covered funds” under the Volcker Rule.<sup>3</sup> We acknowledge the effort of federal regulators in this current rulemaking and support its proposal to expand the current exemption for bank investments in SBICs to include SBICs that voluntarily surrender their licenses and do not make new investments after surrender.

The SBIC program, administered by the Small Business Administration (“SBA”), is a market-driven platform that serves an important public purpose of facilitating private investment into domestic small businesses. The program was created in 1958 during the Glass-Steagall era. SBIC investments by banks are specifically and clearly permitted in statute in the Dodd-Frank Act, as

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<sup>1</sup> 85 Fed. Reg. 12120-12206 (Feb. 28, 2020) (“Proposed Rulemaking”).

<sup>2</sup> 12 U.S.C. 1851 *et seq.*

<sup>3</sup> On December 10, 2013, the Federal Reserve (“Fed”), Federal Deposit Insurance Company (“FDIC”), the Commodity Futures Trading Corporation (“CFTC”), the Securities and Exchange Commission (“SEC”), and the OCC issued final rules implementing the Volcker Rule. Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”), which created the new Section 13 of the Bank Holding Company Act, and the final regulations issued by multiple agencies (together, the “Volcker Rule”) were made effective on April 1, 2014, and all “banking entities” were required to conform to the rule by July 21, 2015. The Volcker Rule prohibits these banking entities from proprietary trading and from ownership or sponsorship relationships with private equity funds and hedge funds (“covered funds”). In August 2017, the agencies issued another request for comments, and SBIA submitted a comment letter in September 2017.

they were under Glass-Steagall. SBICs were permitted because they are highly regulated, have a clear public policy purpose, and because of their unique role in job creation and economic impact.

An independent study prepared for the Library of Congress found that SBIC-backed small businesses created almost three million new jobs and supported an additional 6.5 million jobs over the 20-year period of their study.<sup>4</sup>

## **Volcker Rule Exclusion for SBICs and RBICs**

SBIA applauds federal regulators for accepting SBIA's November 2019 recommendation to extend the Volcker Rule exemption for bank investments in SBICs to include SBICs that voluntarily surrender their licenses and do not make new investments after surrender. SBIA recommends against adding a new requirement that SBICs "operate pursuant to a written plan to dissolve within a set period of time" because it would be redundant and costly.<sup>5</sup> Instead, we recommend that federal banking regulators rely upon the SBA's existing requirement for a windup plan from each SBIC that surrenders a license.<sup>6</sup>

SBIC funds have a finite life with four basic stages: Fundraising, investing, harvesting, and wind-down. While there is some overlap in these stages, all funds get to a point where they are no longer investing and only harvesting and realizing returns for their investors. During this wind-down phase, SBICs often surrender their licenses, which can cause unintended problems for bank investors who could lose their SBIC exemption at exactly the time when profits are being realized and selling their stake in the secondary market would be least liquid because of the short time left in the fund.

Without the proposed exemption extension, if the SBIC voluntarily surrenders the license prior to termination of the fund, it may be viewed as no longer exempt from the definition of a "covered fund" under the Volcker Rule. Bank LPs typically cannot control whether or when an SBIC surrenders its license. Therefore, banks are put in a position where they may need to engage in a regulatory-forced fire sale or withdrawal of their interest from the fund (oftentimes at values below current valuations) in order to avoid being out of compliance with the Volcker Rule.

Allowing banks to realize their investments from funds in wind-down that held an SBIC license is consistent with the intent of the law, does not present any safety and soundness concerns from a

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<sup>4</sup> Paglia and Robinson, Measuring the Role of the SBIC Program in Small Business Job Creation, Report for the Library of Congress, at 4 (January 2017) <[https://www.sba.gov/sites/default/files/articles/SBA\\_SBIC\\_Jobs\\_Report.pdf](https://www.sba.gov/sites/default/files/articles/SBA_SBIC_Jobs_Report.pdf)>.

<sup>5</sup> See Proposed Rulemaking at Question 24 ("Should the proposed exclusion from issuers that surrender their SBIC licenses include a requirement that the issuer operate pursuant to a written plan to dissolve within a set period of time, such as five years? Why or why not?")

<sup>6</sup> 13 CFR 107.1900 and 13 CFR 107.590(c). ("Wind-up Plan" means a plan that [SBIC licensees] prepare when you decide that you will no longer make any Financings other than follow-on investments, and that you update annually when you file your SBA Form 468. The plan must contain your best estimates of the following: (i) the expected number of years you expect to operate; (ii) for each of your Loans and Investments, the expected liquidation date and anticipated proceeds; (iii) the timing of your repayment of obligations to SBA; (iv) the timing and amount of any planned reductions in your Management Expenses.")

regulatory standpoint, and would protect banks from forced sales of what should be valuable investments.

Additionally, federal banking regulators ask whether the “covered funds” exemption should be expanded to include bank investments in Rural Business Investment Companies (RBICs).<sup>7</sup> SBIA answers yes. Extending the Volcker Rule exemption for bank investments in RBICs is consistent with the Act’s intent because the law permits “a banking entity to make and retain investments that are designed primarily to promote the public welfare.”<sup>8</sup>

The U.S. Department of Agriculture operates the RBIC program, a developmental venture capital program for the purpose of promoting economic development and the creation of wealth and job opportunities in non-metropolitan areas and among residents living in those areas. Like the SBA, the USDA licenses investment fund applicants as RBICs to address the unmet equity capital needs of small enterprises primarily located in rural areas.

SBIA endorses the policy perspective of federal banking regulators that “permitting a banking entity to sponsor and invest” in funds like SBICs and RBICs, which do make public welfare investments, would result in the provision of “valuable expertise and services to [those funds] and to provide funding and assistance to small businesses and low- and moderate-income communities.”<sup>9</sup>

### **Proposed Additional Covered Funds Exclusions**

Regulators propose extending the Volcker Rule exclusion to several other categories including qualifying credit funds and venture capital funds. Credit funds that use debt to invest in portfolio companies earn income on loan repayments making them somewhat less risky for bank investments because there is an immediate revenue stream. Venture capital funds, according to congressional supporters, promote the public interest by funding startup companies critical to spurring innovation, job creation, and economic competitiveness.<sup>10</sup>

SBIA acknowledges the intent of regulators to expand the Volcker Rule’s exclusion and, while we do not take a specific position on its extension for either credit funds or venture capital funds, we appreciate the policy arguments because they parallel those in support of the exclusion for SBICs, including improving the flow of financing to small businesses and better distributing capital to regions of the country that do not typically attract it. We also recognize that the Volcker Rule was intended to prevent short-term, speculative proprietary trading and that regulators are seeking to exempt only longer-term investment vehicles from its prohibitions.

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<sup>7</sup> See Proposed Rulemaking at Question 21 (“Should the agencies provide an express exclusion from the definition of covered funds for RBICs, similar to the exclusion for SBICs?”)

<sup>8</sup> See 12 U.S.C. 1851 (d)(1)(E). Related, the federal Office of the Comptroller of the Currency (“OCC”) maintains regulations for its regulated banks that define eligible “public welfare” investments to include those designated as a “qualified investment” under the Community Reinvestment Act, which include investments in SBICs and RBICs. 12 C.F.R. 25.23.

<sup>9</sup> 85 Fed. Reg. 12129-12130 (Feb. 28, 2020).

<sup>10</sup> Id. at 12134, n110.

## Conclusion

SBIA supports sensible regulation that promotes soundness in our financial system. We believe that excluding SBICs from the definition of covered funds for purposes of the Volcker Rule fits squarely within those purposes.

We ask that, per the statute, SBICs continue to be excluded and that the exemption be expanded to include SBICs that retire their licenses after their investment period. This small change will eliminate the costly burden associated with banks needing to exit SBIC investments prior to final dissolution of the partnership without sacrificing the safety and soundness of the institutions impacted.

As always, SBIA appreciates the opportunity to discuss these issues and looks forward to working together to update applicable regulations to ensure America's small businesses have access to the capital they need.

Sincerely,



Brett Palmer  
President  
Small Business Investor Alliance