Dinner Is Served: Will The Volcker Rule Spur Interest In California's Capital Access Company Law?

Posted In California Securities Laws

6-15-2011

Congress issues an invitation

When Congress enacted the National Securities Markets Improvement Act of 1996 (aka the "NSMIA"), it added a new exemption to the Investment Company Act of 1940. Under Section 6(a)(5), a company will be exempt if, among other things,

- It is not engaged in the business of issuing redeemable securities; and
- Its operations are subject to regulation by the state in which the company is organized under a statute governing entities that provide financial or managerial assistance to enterprises doing business, or proposing to do business, in that state.

The California legislature cooks the dinner

In response, the California legislature enacted "Capital Access Company" law in 1998, California Corporations Code Section 28000 *et seq.*

The Commissioner sets the table

The Commissioner of Corporations responded in turn by adopting regulations, 10 CCR Section 280.100 *et seq.*

No one partakes

Although Congress has issued the invitation, the California legislature has cooked the dinner, and the Commissioner has set the table, no one, to my knowledge, has yet seen fit to partake of the repast placed before them.

As I mentioned in this post last fall, the California legislature enacted amendments last year to ease some of the perceived problems with the Capital Access Company law. Still, there have been to my knowledge no takers.

Please contact **Keith Paul Bishop** at Allen Matkins for more information kbishop@allenmatkins.com

Will Dodd-Frank supply the raison d'etre?

Perhaps the Dodd-Frank Act will provide the missing raison d'etre for the Capital Access Company law. Section 619 of the Dodd-Frank Act is commonly referred to as the "Volcker Rule". In very general terms, the Volcker Rule provides that a "banking entity" may not "acquire or retain any equity, partnership, or other ownership interest in or sponsor a hedge fund or a private equity fund". 12 U.S.C. § 1851(a)(1)(B). The act defines a hedge fund or private equity fund as follows:

> *An issuer that would be an investment company, as defined in the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), but for section 3(c)(1) or 3(c)(7) of that Act, or such similar funds as the appropriate Federal banking agencies, the Securities and Exchange Commission, and the Commodity Futures Trading Commission may, by rule, as provided in subsection (b)(2), determine.*

12 U.S.C. § 1851(h)(2). The Volcker Rule obviously directly impacts banking entities. However, hedge funds and private equity funds will also be indirectly affected because the rule will affect their investor bases.

Here's where the Capital Access Company law may come into play. As noted above, Capital Access Companies are exempt under Section 6(a)(5) of the Investment Company Act and thus do not have to rely on the exclusion from the definition of an "investment company" in either Section 3(c)(1) or 3(c)(7). Thus, they may not fall within the definition of a hedge fund or private equity fund under the Volcker Rule.

What's next

The Dodd-Frank Act required the new Financial Stability Oversight Council to conduct a study and issue recommendations. The Council issued its study in January. As mentioned in this post, California's Commissioner of Financial Institutions, William Haraf, is a member of the Council.

The Securities and Exchange Commission's website currently states that it plans to adopt regulations implementing Section 619 in the August to December time period. It is poossible that the SEC will use its authority to include "other similar funds" within the penumbra of the Volcker Rule.

This is complicated stuff

The Volcker Rule is complex and I've necessarily omitted a lot of detail in this post. As always, you should not rely on this Blog as legal advice or as a legal opinion. See this Blog's "Terms of Use".

Please contact **Keith Paul Bishop** at Allen Matkins for more information kbishop@allenmatkins.com