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KIRKLANDPEN
Private Equity Newsletter

March 3, 2015

New Volcker Rule SOTUS Guidance Improves Environment for Private Fund Investments by Non-U.S. Banking Entities

PENpoints

New Volcker Rule SOTUS guidance will, in most situations, eliminate the need to create a parallel fund to address the Volcker Rule concerns of non-U.S. banking entities.

On February 27, 2015, federal banking agencies, the U.S. Securities and Exchange Commission and the U.S. Commodity Futures Trading Commission jointly published formal guidance that will make it easier for a private fund sponsor to accommodate investments from non-U.S. banking entities. The guidance clarifies that the marketing restriction in the Volcker Rule's so-called SOTUS exemption (i.e., "solely outside the United States"), which prohibits the offer or sale of interests in a SOTUS-eligible private fund to U.S. persons, applies only to the non-U.S. banking entity relying on the SOTUS exemption and not to a third-party private fund sponsor.[1]

The new guidance represents a significant departure from prior interpretations of the SOTUS marketing restriction. While not inconsistent with the Private Equity Growth Capital Council's *Consensus Interpretation of the Implementation of Parallel Fund Structures under the Volcker Rule* (May 1, 2014), in most situations the new guidance will eliminate the need to create a parallel fund to address the Volcker Rule concerns of non-U.S. banking entities.[2]

Previously, the marketing restriction was widely interpreted to mean that interests in a SOTUS-eligible private fund should not be offered to U.S. persons by any party, including a third-party private fund sponsor. Consequently (and as contemplated in the May 2014 *Consensus Interpretation*), a private fund sponsor wishing to accommodate a non-U.S. banking entity intending to rely on the SOTUS exemption typically established a parallel fund where:

- no interest in the parallel fund was offered to any U.S. person by the private fund sponsor;
- interests in the parallel fund were separately offered to avoid integration with any offering of fund interests to U.S. persons;
- the parallel fund would need to qualify for the §3(c)(1) or §3(c)(7) exemptions from registration under the Investment Company Act because the SOTUS exemption applies only to a fund with a sufficient U.S. jurisdictional nexus; and
- ownership of 25 percent or more of the interests in the parallel fund by any non-U.S. banking entity was generally avoided to address traditional concerns under the Bank Holding Company Act.

Establishing a private fund meeting all of these requirements, while balancing tax efficiency and ERISA considerations, frequently was problematic for the private fund sponsor and/or resulted in uncertainty as to whether the private fund satisfied all of the requirements of the Volcker Rule. As a result, many private fund sponsors could not (or elected not to) accommodate investments from non-U.S. banking entities.

The new guidance permits non-U.S. banking entities to rely on the SOTUS exemption while allowing private fund managers to offer interests in the SOTUS-eligible private fund to U.S. persons. Further, because interests in private funds are typically offered to U.S. persons in reliance on §3(c)(1) or §3(c)(7) of the Investment Company Act, that SOTUS exemption requirement can be satisfied without any extra effort required on the part of the private fund sponsor.

Note that the new guidance does not provide any relief for U.S. banking entities under the Volcker Rule, and

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that traditional Bank Holding Company Act concerns must continue to be addressed, including avoiding affiliation with any non-U.S. banking entity investor.

1 Additionally, the SOTUS exemption requires that the non-U.S. banking entity (i) is not ultimately controlled by a U.S. banking entity, (ii) in general, is a "qualifying foreign banking organization" under Regulation K, (iii) has the decision to invest made by personnel located outside of the United States, and (iv) accounts for, and funds the investment from a source located, outside of the United States.

2 The new guidance will also streamline Volcker Rule compliance for non-U.S. banking entities, in particular with respect to the ability to retain private fund investments made prior to the issuance of the final Volcker Rule regulations in December 2013.

If you have any questions about the matters addressed in this *KirklandPEN,* please contact the following Kirkland authors or your regular Kirkland contact.

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Cayman FATCA and CDOT Registration and Reporting Deadline

The Cayman Islands Tax Information Authority ("TIA") has announced that Cayman financial institutions (which include most Cayman fund partnerships and feeder entities as well as certain holding companies) are required to register with the TIA by April 30, 2015. In addition, FATCA-related reporting for calendar year 2014 will be due by May 31, 2015.

The registration and reporting requirements apply for purposes of both U.S. FATCA and the U.K.-Cayman intergovernmental agreement concerning sharing of information.

Both registration and reporting must be done through the TIA's website portal and will be accessible via the links on the following page: http://www.tia.gov.ky/pdf/AEOI_News_&_Updates.pdf. As of the date of this *KirklandPEN,* the portal is not yet live, but it is expected to be ready for use in early March.

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PENbriefs

IRS Rules Foreign Debt Discharge Excluded From Income if Recognized Under Chapter 15

A recent IRS private letter ruling that a debtor need not recognize as taxable income any cancellation of debt income realized on debt cancelled via a non-U.S. bankruptcy proceeding highlights the benefits of seeking recognition of multinational bankruptcy proceedings by a U.S. Bankruptcy Court. To learn more, see our recent *Alert*.

Employee Benefits Update

In a recent *Alert*, we highlighted several changes in employee benefits laws and regulations, including changes to multiemployer pension plan liabilities and new plant-shutdown rules for single employer pension plans.

China Continues Its Aggressive Anti-Monopoly Law Enforcement with a Record-Breaking $975 Million Fine Against Qualcomm

A recent settlement between Qualcomm and Chinese antitrust regulators is the latest in large, high-profile antitrust fines against foreign companies and further demonstrates that Chinese regulators are prepared to continue to aggressively enforce China's antitrust laws against foreign companies. To learn more, see our recent *Alert*.

PENnotes

Columbia Business School's 21st Annual Private Equity and Venture Capital Club Conference
New York, New York
March 6, 2015

Kirkland will sponsor Columbia Business School's 21st Annual Private Equity & Venture Capital Conference. This year's conference focuses on the evolving strategies in a new era of investing. Kirkland partner Douglas Ryder will participate in the "LBOs: Managing Cycles and the Road Ahead Panel," while Kirkland partners Andrew Wright, Daniel Lavon-Krein and Nadia Murad will lead a lunchtime discussion about the "State of the Market: Fundraising." Click here for more information.

2015 Private Equity & Venture Capital Conference
Chicago, Illinois
April 15, 2015

The Kellogg School of Management is proud to present its annual Private Equity and Venture Capital Conference. This year's conference will explore the challenges of building value at both the fund and portfolio company level. Kirkland partners Meg Gibson and John O'Neil will speak at the conference. Click here for more information.

35th Annual Ray Garrett Jr. Corporate and Securities Law Institute
Chicago, Illinios
April 30 - May 1, 2015

The Ray Garrett Jr. Corporate and Securities Law Institute is the pre-eminent securities law conference in the Midwest. It is the only Midwest conference that brings together senior officials from the U.S. Securities and Exchange Commission and leading securities practitioners. Kirkland partners Robert Hayward, Scott Falk, and Keith Crow are members of the Executive Committee. Robert Hayward will also chair a session on Cybersecurity and Data Breach. Click here for more information.

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Kirkland & Ellis' nearly 400 private equity attorneys have handled leveraged buyouts, growth equity transactions, recapitalizations, going-private transactions and the formation of private equity, venture capital and hedge funds on behalf of more than 400 private equity firms around the world.

Kirkland has been widely recognized for its preeminent private equity practice. The Firm was named "Private Equity Group of the Year" in 2012, 2013 and 2014 by *Law360* and was commended as being the most active private equity law firm of the last decade in *The PitchBook Decade Report*. Kirkland & Ellis was named "Law Firm of the Year" in Mergers and Acquisitions Law by U.S. News Media Group and Best Lawyers in their 2014 "Best Law Firms" rankings. The Firm was named "Best M&A Firm" at *World Finance*'s 2014 Legal Awards, "North American Law Firm of the Year: Fund Formation" and "North American Law Firm of the Year: Transactions" at Private Equity International's 2014 Private Equity International Awards and "Private Equity Deal of the Year" at the 2014 IFLR Americas Awards.

In 2012, 2013 and 2014, Chambers and Partners ranked Kirkland as a Tier 1 law firm for Investment Funds in the United States, United Kingdom, Asia-Pacific and globally. The Firm was ranked as the #1 law firm for both Global and U.S. Buyouts by deal volume in Mergermarket's *League Tables of Legal Advisors to Global M&A for Full Year 2011, 2012, 2013* and *2014*, and has consistently received top rankings among law firms in Private Equity by The Legal 500, the Practical Law Company and IFLR, among others.

The Lawyer magazine has recognized Kirkland as one of its "Transatlantic Elite" every year since 2008, having noted that the Firm is "leading the transatlantic market for the provision of top-end transactional services ... on the basis of a stellar client base, regular roles on top deals, market-leading finances and the cream of the legal market talent."

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