December 24, 2013

The Honorable Ben Bernanke
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

The Honorable Martin J. Gruenberg
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

The Honorable Thomas Curry
Comptroller of the Currency
Office of the Comptroller of the Currency
400 7th Street, SW
Washington, DC 20219

The Honorable Gary Gensler
Chairman
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

The Honorable Mary Jo White
Chair
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

RE: "Ownership Interests" in Connection with Certain CLO Debt Securities

Dear Chairman Bernanke, Comptroller Curry, Chairman Gensler, Chairman Gruenberg, and Chair White:

The Loan Syndications and Trading Association ("LSTA"),[1] the Securities Industry and Financial Markets Association ("SIFMA"),[2] the Structured Finance Industry Group ("SFIG"),[3] the American Bankers Association,[4] and the Financial Services Roundtable[5] submit this letter in connection with certain aspects of the final rule implementing the Volcker Rule, adopted by your respective agencies ("Agencies") on December 10, 2013.[6] Specifically, we ask for confirmation that the term "ownership interest" as defined in §__.10(d)(6) does not include debt securities of collateralized loan obligation ("CLO") issuers that are covered funds where these CLO debt securities have a contingent right to remove a manager "for cause" or to nominate or vote on a nominated replacement upon a manager's removal for cause or resignation, but contain none of the other indicia of ownership interests listed in the definition.[7]

Section __.10(d)(6)(i)(A) of the Final Rule defines "ownership interest" to include "the right to participate in the selection or removal" of an investment manager of a covered fund, "(excluding the rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event)." We believe it is reasonable to interpret the "for cause" trigger relating to the right of the holders of CLO debt securities to remove a manager or nominate or

[1] The LSTA is a not-for-profit trade association that is made up of a broad and diverse membership involved in the origination, syndication, and trading of commercial loans. The 350 members of the LSTA include commercial banks, investment banks, broker-dealers, hedge funds, mutual funds, insurance companies, fund managers, and other institutional lenders, as well as service providers and vendors. The LSTA undertakes a wide variety of activities to foster the development of policies and market practices designed to promote just and equitable marketplace principles and to encourage cooperation and coordination with firms facilitating transactions in loans. Since 1995, the LSTA has developed standardized practices, procedures, and documentation to enhance market efficiency, transparency, and certainty.

[2] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

[3] SFIG is a member-based, trade industry advocacy group focused on improving and strengthening the broader structured finance and securitization market. SFIG provides an inclusive network for securitization professionals to collaborate and, as industry leaders, drive necessary changes, be advocates for the securitization community, share best practices and innovative ideas, and educate industry members through conferences and other programs. Members of SFIG represent all sectors of the securitization market including issuers, investors, financial intermediaries, law firms, accounting firms, technology firms, rating agencies, servicers, and trustees. Further information can be found at www.sfindustry.org.

[4] The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's $14 trillion banking industry and its 2 million employees. Learn more at aba.com.

[5] The Financial Services Roundtable represents 100 integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. Roundtable member companies provide fuel for America's economic engine, accounting directly for $98.4 trillion in managed assets, $1.1 trillion in revenue, and 2.4 million jobs.

[6] Final Rule, Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds (Dec. 10, 2013) ("Final Rule").

[7] For the avoidance of doubt, our request does not extend to the "equity" tranche of a CLO, even where denominated as debt, given that it does have other indicia of ownership interests.

vote on a nominated replacement upon a manager's removal for cause or resignation to constitute a "right[ ] of a creditor to exercise remedies upon the occurrence of a default" since a "for cause" removal under the management agreement is typically linked to a significant breach of the manager's obligations under the CLO transaction documents. Nevertheless, this issue has resulted in considerable confusion among our banking entity and asset manager members as they seek to understand the impact of the Final Rule on holders of CLO debt securities.

We understand that, as a result of this uncertainty, a large number of our members, which include both large and small banks, are weighing whether they will be permitted to acquire or retain any covered fund CLO debt securities that have such a controlling class feature that is a protective creditors' right. We are concerned that, unless the Agencies provide guidance that the rights described herein do not amount to an ownership interest, banking entities (including a significant number of regional and community banks) could begin to dispose of these CLO debt securities and stop acquiring new covered fund CLO debt securities, even though we believe that these rights should not be read to constitute an ownership interest. Divestment of CLO debt securities will unnecessarily disrupt the CLO market, could result in immediate and substantial capital losses for banking entities, and will ultimately impair the availability of, and increase the cost of, corporate lending since banking entities play a significant role in providing continued liquidity to the CLO debt market and CLOs provide significant capital and liquidity to the corporate loan market.[8] The impact of these losses will not only be felt by banking entities but also by non-bank investors that hold CLO debt securities, as these securities will experience a loss in market value driven by the forced selling.

CLOs provide the holders of their debt securities with a number of creditor rights designed to protect their debt interests. Most of these rights are vested in the "controlling class," typically the most senior class of debt securities then outstanding. However, since CLO debt securities are paid serially, any class of these debt securities can become the controlling class after the prior classes have been paid in full. An important creditor's right is to remove the CLO manager for cause. Events constituting cause for removal may involve, for example, a willful breach by the manager of its obligations under the CLO transaction documents, the dissolution or insolvency of the manager, or fraud or criminal activity by the manager in connection with its investment management business. These types of events pose clear and direct threats to the interests of holders of debt securities as creditors of a CLO, and their ability to respond to and remediate these threats is properly viewed as an essential creditor's right, and not as an ownership interest.

In addition, the resignation of the manager is tantamount to a change of control of the issuer — a circumstance under which traditional bank lenders often receive consent rights or the right to be repaid. Investors thus view the ability to vote on a replacement manager, too, as an important creditors' right.

[8] *See* Forbes, "Volcker Rule's Non-Exemption of CLOs with Bonds Holds Potential to Disrupt Markets," Dec. 17, 2013, available at http://www.forbes.com/sites/spleverage/2013/12/17/volcker-rules-non-exemption-of-clos-with-bonds-holds-potential-to-disrupt-market/.

In almost all CLOs, some percentage of the controlling class of holders of debt securities (sometimes with holders of other classes of debt securities as well) have the contingent right to remove the manager for cause.[9] In the event of a removal for cause or a manager's resignation, typically the controlling class of debt securities and the equity holders each have the right to propose to the other a successor manager. If the parties are unable to agree on a replacement, they, or even the CLO issuer or the resigning manager, may ask a court to appoint a successor.

While for cause removal and replacement upon resignation or removal rights are common creditor protective rights in CLOs, they are not typically structured to occur in the context of an event of default or an acceleration event under the CLO securities indenture, even though they are only triggered upon a manager's default under the CLO management agreement or its resignation. As such, there is some uncertainty as to whether CLO debt security holders that have these rights would or would not be deemed to have an "ownership interest" under the Final Rule.

If a CLO debt security with these contingent creditor protective rights is treated as an "ownership interest," a banking entity would be prohibited from, or severely limited in, acquiring or continuing to hold debt securities in any CLO that is a covered fund, even though none of the attributes of such debt securities has the characteristics of an equity or other typical ownership interest. Holders of CLO debt securities only have the right to specified principal and interest. They do not have the right or ability, directly or indirectly, to share in the CLO's profits or losses or to earn a return based on the CLO's performance. They also do not have the types of voting rights that typically attach to equity securities, like the right to vote on establishing an entity's objectives and policies or electing its board of directors. The contingent right to participate in the replacement of a manager in the remote event of a removal for cause or resignation is far narrower than rights that accompany equity-like interests and do not provide holders of CLO debt securities with the ability to control the decisions of the manager.[10]

Moreover, as a practical matter, it is very difficult to restructure an existing CLO or to obtain consent to amend CLO documentation to modify the rights of holders of debt securities. The Agencies recently indicated in a different context that banking entities could consider whether an investment structure could be restructured, for example to avail itself of an exemption under the Investment Company Act other than Sections 3(c)(1) or 3(c)(7), thereby taking it out of the scope of the covered fund definition.[11] However, each Investment Company Act exemption contains conditions that would be unworkable for existing CLOs. For example, if a CLO were to be restructured to rely on Investment Company Act Rule 3a-7, the manager could

[9] CLO equity holders may also have this right. Unlike the holders of CLO debt securities, however, and as noted above, the CLO equity holders satisfy most if not all of the indicia of "ownership interest" under the Final Rule, and we are not seeking clarification as to their interests in this letter.

[10] We understand that, to the extent that a CLO debt security in fact meets any of the indicia of "ownership interest" in the Final Rule (other than the limited right to participate in the selection or removal of a manager discussed above), such security would constitute an "ownership interest" and be subject to all applicable covered fund restrictions.

[11] We refer to the FAQ issued by the federal banking agencies on December 19, 2013, titled, "FAQ Regarding Collateralized Debt Obligations Backed by Trust Preferred Securities under the Volcker Rule."

be significantly limited in its ability to sell assets, even outside of the reinvestment period. Neither managers nor equity holders of actively managed CLOs would likely agree to such restrictions. There may also be significant logistical difficulties in amending outstanding CLOs (especially in the case of CLO debt securities held through a clearing organization whose holders are not known to the CLO issuer), and the amendment of a large number of outstanding transactions would require significant expense. Furthermore, even when all affected debt security holders are known, certain security holders that are not banking entities may be unwilling to give up what are considered to be important creditors' rights.[12]

We thus request confirmation from the Agencies in an interpretive letter, FAQ, or other appropriate form that the term "ownership interest" as defined in §__.10(d)(6) does not include debt securities of CLO issuers that are covered funds, where these CLO debt securities give holders a contingent right to remove a manager "for cause" or to nominate or vote on a nominated replacement upon a manager's resignation or removal, but contain none of the other indicia of ownership interests listed in the definition.

Please feel free to contact Elliot Ganz, LSTA's General Counsel, at (212) 880-3003 if you have any questions regarding this letter.

Sincerely,

R. Bram Smith
Executive Director
Loan Syndications and Trading Association

Christopher Killian
Managing Director
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Richard Johns
Executive Director
Structured Finance Industry Group

[12] As of the date of this letter, the aggregate amount of U.S. CLOs outstanding is $303 billion, of which $153 billion were issued before September 2008.

Cecelia A. Calaby
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