Statement Regarding the Treatment of Collateralized Loan Obligations Under Section 13 of the Bank Holding Company Act

Introduction

Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") added a new section 13 to the Bank Holding Company Act of 1956 ("BHC Act") (codified at 12 U.S.C. 1851) that generally prohibits banking entities from engaging in proprietary trading and from acquiring or retaining an ownership interest in, sponsoring, or having certain relationships with a hedge fund or private equity fund. These prohibitions are subject to a number of statutory exemptions, restrictions and definitions.

Section 13 provides that a banking entity must conform its activities and investments to the prohibitions and restrictions of that section and any final implementing regulation no later than 2 years after the statutory effective date of section 13, which is July 21, 2012, unless extended by the Board. Under the statute, the Board may, by rule or order, extend the two-year conformance period not more than one year at a time, for a total of not more than 3 years, if in the judgment of the Board, an extension is consistent with the purposes of section 13 and would not be detrimental to the public interest.

In December 2013, the Board, OCC, FDIC, SEC and CFTC (collectively, "the Agencies") approved a final regulation implementing the provisions of section 13 of the BHC Act.[1] In December 2013, the Board also extended the conformance period until July 21, 2015.

[1] See 79 FR 5536 (Jan. 31, 2014).

After approval of the final rule, a number of banking entities, trade associations and members of Congress expressed concern that the final rule would require divestiture by banking entities of ownership interests in collateralized loan obligation vehicles ("CLOs") that would be covered funds under the final rule. CLOs are securitization vehicles backed predominantly by commercial loans. CLOs may also hold, or have the right to acquire, a certain amount of nonconforming non-loan assets (e.g., debt securities). To address this issue, the Board is issuing this statement to confirm that the Board intends to exercise the authority granted by section 13 of the BHC Act to extend beyond July 21, 2015 the period provided to banking entities to conform their ownership interests in and sponsorship of covered funds that are CLOs.

Background

In keeping with the statute, the final rule excludes from the definition of covered fund "loan securitizations" that are comprised solely of loans and related servicing assets, as well as entities that are similar to loan securitizations, such as qualifying asset-backed commercial paper conduits and qualifying covered bonds.[2] These securitizations of loans are excluded in part because the statute itself provides that it is not to be construed to limit or restrict the ability of a banking entity to sell or securitize loans in a manner otherwise permitted by law.[3] A securitization, including a CLO that holds some non-conforming non-loan assets, may be a covered fund under the rule. A banking entity

[2] See final rule § __.10(c)(8)-(c)(10), 77 FR at 5788-89. The final rule defines "loan" to include any loan, lease, extension of credit, or secured or unsecured receivable that is not a security or a derivative. See final rule § __.2(s), 77 FR at 5780.

[3] See 12 U.S.C. § 1851(g)(2).

must conform or divest its ownership interests in and sponsorship of these CLOs that are covered funds by the end of the conformance period.

As noted above, under the statute, the Board may, by rule or order, extend the conformance period for not more than one year at a time, for a total of not more than three years, if in the judgment of the Board, an extension is consistent with the purposes of section 13 and would not be detrimental to the public interest.[4] The Board already extended the conformance period for one year, until July 21, 2015, when the final implementing rules were adopted in December, 2013.

As noted in the legislative history of section 13, the conformance period for banking entities is intended to give markets and firms an opportunity to adjust to the prohibitions and requirements of that section and any implementing rules adopted by the Agencies.[5] Consistent with this purpose and the statute, the Board intends to grant two additional one-year extensions of the conformance period under section 13 of the BHC Act that allow banking entities additional time to conform to the statute ownership interests in and sponsorship of CLOs in place as of December 31, 2013, that do not qualify for the exclusion in the final rule for loan securitizations. The Board intends to act on these extensions in August of this year and next year.

During the conformance period, a banking entity is not required to include ownership interests in CLOs for purposes of determining compliance with the investment limits of § __.12 of the final rule. Similarly, a banking entity is not required to deduct its

---

[4] See 12 U.S.C. § 1851(c)(2). Section 13 also permits the Board, upon application of a banking entity, to provide up to an additional 5 year transition period for certain illiquid funds. See 12 U.S.C. § 1851(c)(3).

[5] See 156 Cong. Reg. S5898 (daily ed. July 15, 2010) (statement of Sen. Merkley)).

CLO investments from its tier 1 capital as required under § __.12(d) of the final rule until the end of the relevant conformance period.

The other agencies charged with enforcing the requirements of section 13 of the BHC Act and the final rule will apply section 13 and the final rule in accordance with the Board's conformance rule, including any extension of the conformance period applicable to CLOs.

Nothing in this guidance restricts in any way the authority of any agency to use its supervisory or other authority to limit any activity the agency determines to be unsafe or unsound or otherwise in violation of law.