January 10, 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 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 Gruenberg, and Chair White:

The Loan Syndications and Trading Association ("LSTA") and the Securities Industry and Financial Markets Association ("SIFMA") are grateful to the staffs of the Federal Reserve Board ("Federal Reserve"), Federal Deposit Insurance Corporation ("FDIC"), Office of the Comptroller of the Currency ("OCC"), and Securities and Exchange Commission ("SEC") for

taking the time to meet with us on Thursday.[1] We submit this letter on behalf of the undersigned organizations as a follow-up to the meetings and to our letters of December 24, 2013 and December 31, 2013 (the "December Letters"),[2] to clarify certain aspects of those letters and the discussions in the January 9 Meetings, and to propose language that would confirm, in a FAQ or other appropriate interpretive guidance, that the term "ownership interest" as defined in §__.10(d)(6) of the final rule implementing the Volcker Rule[3] does not include debt securities of collateralized loan obligation ("CLO") issuers that are covered funds, as described below, solely because they have the creditor-protective rights described below, whether or not an event of default or acceleration event exists under the CLO indenture.

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)."

As discussed in the December Letters, 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.[4]

We have confirmed that most existing controlling class CLO debt security holders have the contingent right to participate in the removal and replacement of the CLO manager, but only for cause pursuant to the transaction documents. The definition of "cause" that would trigger the right of removal includes, for example, a willful breach by the manager of its obligations under the CLO transaction documents, the dissolution or insolvency of the manager, a material failure of a representation or warranty that is not timely cured, or fraud or criminal activity by the manager in connection with its investment management business.

Most existing controlling class CLO debt security holders also have the right to participate in the replacement of a manager after the manager's resignation. 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.

In the event of a removal of the manager for cause by the debt security or equity holders,[5] or the manager's resignation, typically the equity holders and/or the controlling class of debt security holders each have the right to propose to the other a successor manager. If the parties

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[1] Representatives of the LSTA and SIFMA met with Federal Reserve, FDIC, and OCC staff on the morning of January 9, 2014, and with SEC staff that afternoon (the "January 9 Meetings").

[2] The undersigned organizations are the LSTA, SIFMA, the Structured Finance Industry Group ("SFIG"), and the Financial Services Roundtable ("FSR"). The December Letters, including the description of each of our organizations, are incorporated herein by reference.

[3] 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").

[4] Since CLO debt securities are paid serially, any class of these debt securities can become the controlling class after the more senior classes have been paid in full.

[5] The equity holders also typically have the right to remove the manager for cause.

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.

As discussed in the December Letters and the January 9 Meetings, these "for cause" and resignation 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.

Importantly, CLO debt securities typically do not have any of the other indicia of ownership interest described in subsections (6)(i)(B) through (G) of Section __.10(d) of the Final Rule.[6]

We thus request confirmation from the Agencies in a FAQ or other appropriate interpretive guidance 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 only a contingent right to remove a manager "for cause" or to nominate or vote on or consent to 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.

We believe that adoption by the Agencies of either proposed Alternative 1 or 2 below would allay the concerns of banking entities as to whether their debt securities represent ownership interests solely because of the removal and replacement rights described herein. These proposals are substantively identical but we have offered alternative constructions for your consideration.

Based on our meeting with the Federal Reserve, FDIC, and OCC, we are also offering a third alternative, which would require that the CLO collateral consist predominantly of loans. We continue to believe, however, that the creditor-protective rights described herein, standing alone (*i.e.*, without any of the other indicia of "ownership interest" in the Final Rule), should not qualify as an "other similar interest" regardless of the makeup of the covered fund. Indeed, the contingent right to remove a manager for cause generally needs action by a majority (or super majority) of a controlling class of CLO debt security holders.

Proposed language

Alternative 1:

> The Agencies confirm that the rights of a holder of debt securities of a CLO that is a covered fund to participate in the removal of a manager solely "for cause," as defined in the CLO transaction documents (CLO management agreement, indenture or other related

[6] While the full impact of the final rule is still being assessed, we understand that banking entities believe that, if necessary, they likely will be able to obtain an opinion of counsel that the ownership interest indicia set forth in subsections (6)(i)(B)-(F) and subsection (6)(i)(G), except as it relates to subsection (6)(i)(A), will not apply to most CLO debt securities. However, they almost certainly will not be able to obtain a similar opinion of counsel in connection with subsection (6)(i)(A). Our request does not extend to any CLO debt security that would meet any of the indicia of ownership interest other than in subsection (6)(i)(A).

documents governing the issuance and management of the CLO), and to nominate or vote on or consent to a nominated replacement manager upon a manager's removal for cause or resignation, constitute "rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event" under section __.10(d)(6)(1)(A) of the Final Rule, whether or not an event of default or acceleration event exists under the CLO indenture, as long as the debt security does not meet any of the other indicia of "other similar interest" set forth in subsections (6)(i)(A) through (F) or subsection (6)(i)(G), except as it relates to subsection 6(i)(A) in the limited manner set forth above.

Alternative 2:

The Agencies confirm that the clause: "rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event" under section __.10(d)(6)(1)(A) of the Final Rule includes, whether or not an event of default or acceleration event exists under the CLO indenture, rights of a holder of debt securities of a CLO that is a covered fund to participate in the removal of a manager solely "for cause," as defined in the CLO transaction documents (CLO management agreement, indenture or other related documents governing the issuance and management of the CLO), and to nominate or vote on or consent to a nominated replacement manager upon a manager's removal for cause or resignation, as long as the debt security does not meet any of the other indicia of "other similar interest" set forth in subsections (6)(i)(A) through (F) or subsection (6)(i)(G), except as it relates to subsection 6(i)(A) in the limited manner set forth above.

Alternative 3:

The Agencies confirm that the clause: "rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event" under section __.10(d)(6)(1)(A) of the Final Rule includes, whether or not an event of default or acceleration event exists under the CLO indenture, rights of a holder of debt securities of a CLO that is a covered fund to participate in the removal of a manager solely "for cause," as defined in the CLO transaction documents (CLO management agreement, indenture or other related documents governing the issuance and management of the CLO), and to nominate or vote on or consent to a nominated replacement manager upon a manager's removal for cause or resignation, as long as:

(i) the debt security does not meet any of the other indicia of "other similar interest" set forth in subsections (6)(i)(A) through (F) or subsection (6)(i)(G), except as it relates to subsection 6(i)(A) in the limited manner set forth above; and

(ii) the CLO must be comprised predominantly of loans.

Once again, we are grateful for the staffs' time and consideration of this important issue. As we discussed in the January 9 Meetings, there is significant urgency to our request. Not only does the uncertainty as to treatment of CLO debt securities raise a number of complex and time-

sensitive accounting issues, but, absent a timely resolution, we are concerned about a substantial market disruption.

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 Syndication and Trading Association [LSTA]

Christopher Killian
Managing Director
Securities Industry and Financial Markets Association [SIFMA]

Richard Johns
Executive Director
Structured Finance Industry Group [SFIG]

Richard Foster
Senior Counsel for Regulatory &
Legal Affairs
Financial Services Roundtable [FSR]

cc: The Honorable Mark Wetjen
Acting Chairman
Commodity Futures Trading Commission

Federal Reserve
Christopher Paridon, Legal Division
Anna Harrington, Legal Division

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