

CFTC Expands CPO Registration Exemption for ABS Issuers under No-action Letter

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On December 7, 2012, the CFTC issued an interpretation and no-action letter expanding the exemption for securitization vehicles from the CEA's "commodity pool" definition. The letter also extends until March 31, 2013 the deadline for registration as commodity pool operators (CPOs) for operators of nonconforming securitization vehicles.

On December 7, 2012, the CFTC's Division of Swap Dealer and Intermediary Oversight (Division) issued an [interpretation and no-action letter](#) (No-action 12-45) that:

- Excludes from commodity pool regulations securitization vehicles that generally do not use derivatives as a way to obtain investment exposure but rather use them for credit support and/or use derivatives such as interest rate and currency swaps to alter the payment characteristics of the cash flows from the issuer. These exclusions are in addition to those excluded under [No-action Letter 12-14](#), issued on October 11, 2012 (No-action 12-14) (see [Legal Update, Dodd-Frank CPO Registration Delayed for ABS Issuers](#)).
- Provides permanent no-action relief from commodity pool regulations to operators of most securitization vehicles that issued securities only before October 12, 2012.
- Issues no-action relief until March 31, 2013 to operators of securitization vehicles that do not meet the criteria specified in either No-action 12-45 or No-action 12-14.

In No-action 12-14, the Division clarified that if a securitization vehicle met certain conditions (see [Securitization Vehicles Excluded under the 12-14 Letter](#)), it would be excluded from the definition of "commodity pool" under the Commodity Exchange Act (CEA). No-action 12-14 therefore excludes these vehicles from the CFTC's commodity pool regulations, including registration and reporting requirements, and operators of the vehicles are exempt from registration as commodity pool operators (CPOs).

However, No-action 12-14 was a non-exclusive list of criteria for exemption from the "commodity pool" definition for securitization vehicles. No-action 12-45 adds to that list securitization vehicles that do not strictly meet the criteria listed in No-action 12-14.

Securitization Vehicles Excluded under No-action Letter 12-14

In No-action 12-14, the Division determined that certain securitization vehicles would not be included within the definition of "commodity pool" under Section 1a(10)1 of the CEA and under Commission Regulation 4.10(d), if they meet all of the following conditions:

- The issuer of the [asset-backed securities](#) (ABS) is operated consistent with the conditions specified in SEC [Regulation AB](#) or Rule 3a-7 under the [Investment Company Act of 1940](#), whether or not the issuer's security offerings are in fact regulated under either regulation, such that the issuer, the pool assets and the issued securities satisfy the requirements of either regulation.
- The issuer's activities are limited to passively owning or holding a pool of receivables or other financial assets, which may be either fixed or revolving, that by their terms convert to cash within a finite time period plus any rights or other assets designed to assure the servicing or timely

distributions of proceeds to security holders.

- The issuer's use of derivatives is limited to the uses of derivatives permitted under the terms of Regulation AB, which include credit enhancements and the use of derivatives such as interest rate and currency swaps to alter the payment characteristics of the cash flows from the issuing entity.
- The issuer makes payments to securities holders only from cash flow generated by its pool assets and other permitted rights and assets, and not from or otherwise based upon changes in the value of the entity's assets.
- The issuer is not permitted to acquire additional assets or dispose of assets for the primary purpose of realizing gain or minimizing loss due to changes in market value of the vehicle's assets.

Entities satisfying these criteria receive only limited types of support from swaps and qualify to use an alternative disclosure regime under Regulation AB or an exemption from regulation under the Investment Company Act of 1940. However, if an issuer's operating or trading activities are more active than contemplated by No-action 12-14, the issuer does not limit its investments to financial assets that are used to pay the issuer's securities, or the issuer uses swaps to create synthetic investment exposure, the issuer would not be entitled to claim the exclusion provided in No-action 12-14.

Note that while No-action 12-14 itself does not explicitly mention [No-action Letter 12-15](#), it effectively extended the deferrals granted in No-action 12-15.

Securitization Vehicles Excluded under No-action Letter 12-45

No-action 12-45 further excludes from the "commodity pool" definition those securitization vehicles that do not satisfy the operation or trading limitations of Regulation AB or Rule 3a-7 of the Investment Company Act of 1940 (first criterion listed above from No-action 12-14) but:

- That continue to satisfy the second criterion above from No-action 12-14 regarding the ownership of financial assets.
- Whose use of swaps is no greater than that contemplated by Regulation AB and Rule 3a-7.
- Whose swaps are not used in any way to create investment exposure.

No-action 12-45 specifies the following examples of securitization vehicles that would qualify for the exemption from the "commodity pool" definition under No-action 12-45:

- Traditional asset-backed (ABCP) conduits.
- Traditional [collateralized debt obligation](#) (CDO) asset pools.
- Covered bond pools that contain no commodity interests.
- Vehicles that, absent other factors, use swaps to provide credit support to financial assets in a securitization or to notes issued by the issuer in a securitization to the extent contemplated under Item 1114 of Regulation AB, unless the use of swaps is commercially unreasonable as credit support with respect to that asset pool.

No-action 12-45 specifies, however, that the following are not excluded from the "commodity pool" definition because they include derivatives (typically [credit default swaps](#)) in the asset pool or use derivatives as part of the investment in the pool:

- [Synthetic](#) securitizations such as synthetic CDOs.
- Repackaging vehicles that issue credit-linked or equity-linked notes where the vehicle owns high quality financial assets but sells credit protections on a broad based index through use of a swap.

Further Relief Provided by No-action Letter 12-45

Permanent Relief for 'Legacy Vehicles'

No-action 12-45 also provides permanent no-action relief from commodity pool regulations to operators of most securitization vehicles that issued securities before October 12, 2012 (sometimes referred to as "legacy vehicles"). The Division concluded that certain legacy vehicles might face significant operational difficulties if the commodity pool compliance regime under the commodity pool regulations were imposed on them. To be eligible for the no-action relief, the following criteria must be currently satisfied and remain satisfied:

- The issuer issued fixed income securities before October 12, 2012 that are backed by and structured to be paid from payments on or proceeds received from, and whose creditworthiness primarily depends on, cash or synthetic assets owned by the issuer.
- The issuer did not and will not issue new securities on or after October 12, 2012.
- The issuer will provide, upon request by the CFTC, within five business days (unless it shows that it cannot obtain the required documents through reasonable commercial efforts):
 - the most recent disclosure document used in connection with the offering of the securities issued by the vehicle in question;
 - all amendments to the principal documents since issuing the securities;
 - the most recent distribution statement furnished to investors; and
 - a copy of the information that would be provided to prospective investors to satisfy [Rule 144A](#)(d)(4), if applicable.

No-action Relief for Investors in Legacy Securitization Vehicles

Further, on December 21, 2012, the Division issued [No-action Letter 12-67](#), which extends the no-action relief discussed above to fund operators that invest in legacy vehicles. In No-action 12-67, the Division recommends that the CFTC take no action against operators of funds that invest in legacy securitization vehicles for failure to register as CPOs if:

- The legacy securitization vehicle operator is entitled to no-action relief under the terms of No-action 12-45.
- The fund operator investing in a legacy securitization vehicle is not otherwise required to register as a CPO.

This no-action relief supplements the no-action relief previously provided by the Division, discussed above.

Temporary Relief for Nonconforming Securitization Vehicles

Finally, No-action 12-45 temporarily exempts from CPO registration operators of securitization vehicles that are unable to rely on the relief provided in No-actions 12-14 or 12-45. This no-action relief extends until March 31, 2013, which is now the deadline for CPO registration for operators of these securitization vehicles.

No-action 12-45 also states that the Division remains open to considering whether securitization vehicles that do not meet the criteria set out in No-actions 12-14 and 12-45 might ultimately be exempted permanently from the definition of "commodity pool" or might otherwise be treated as an exempt pool.

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