

**CFTC EXCLUDES CERTAIN SECURITIZATION VEHICLES
FROM DEFINITION OF COMMODITY POOL AND EXTENDS REGISTRATION
DEADLINE FOR CERTAIN CPOs AND CTAs**

In two separate interpretive letters regarding certain securitization vehicles and real estate investment trusts, the CFTC Division of Swap Dealer and Intermediary Oversight has published guidance exempting such entities from regulation as commodity pools and their operators from regulation as commodity pool operators. In addition, for operators and advisors of vehicles that would be subject to regulation by the CFTC as a result of the swaps activity of such vehicles, the CFTC extended until December 31, 2012 the deadline to apply for registration as a commodity pool operator or commodity trading advisor.

Background

The Commodity Exchange Act (the “CEA”) as amended by the Dodd-Frank Act added “swaps” to the list of “commodity interests” in the definition of “commodity pool.”¹ As a result, securitization vehicles and real estate investment trusts (“REITs”) that enter into swaps (including interest rate or currency swaps used solely for hedging purposes) will be holding “commodity interests,” and accordingly could be considered commodity pools under the CEA. As a result, transaction parties—including sponsors, servicers, collateral managers, trustees and administrative agents—could be required to register with the CFTC as commodity pool operators (“CPOs”) or commodity trading advisors (“CTAs”) in respect of such commodity pools. In addition, absent future relief from the CFTC or other regulators, entities that are commodity pools would be “covered funds” under the Volcker Rule, and financial institutions would be subject to restrictions in respect of their sponsorship and ownership of such entities.

Scope of Exemptive Relief for Certain Securitizations

In its interpretive letter issued on October 11, 2012, the Division of Swap Dealer and Intermediary Oversight determined that certain securitization vehicles will be excluded from the definition of commodity pool and any operator of such vehicle will be excluded from the definition of CPO so long as the following criteria are met:

1. The issuer of the asset-backed securities is operated consistent with the conditions set forth in Regulation AB² or Rule 3a-7 of the Investment Company Act of 1940, whether or not the issuer’s security offerings are in fact regulated pursuant to either regulation, such that the issuer, pool assets and issued securities satisfy the requirements of either regulation.

¹ The definition reads, in relevant part: “any investment trust, syndicate, or similar form of enterprise operated for the purpose of trading in commodity interests, including any . . . swap.” 7 U.S.C. § 1a(10). The definitions of “commodity pool operator” and “commodity trading advisor” were also amended to add the word “swap.” 7 U.S.C. §§ 1a(11), 1a(12).

² 17 CFR 229.1100, *et seq.*

2. The entity's activities are limited to passively owning or holding a pool of receivables or other financial assets (other than synthetic financial assets), which may be either fixed or revolving, that by their terms convert to cash within a finite time period (including residual value realized upon disposition of leased assets), plus any rights or other assets designed to assure the servicing or timely distributions of proceeds to security holders.
3. The entity's use of derivatives is limited to the uses of derivatives permitted under the terms of Regulation AB, which include credit enhancement and the use of derivatives such as interest rate and currency swap agreements to alter the payment characteristics of cash flows from the issuing entity.
4. The issuer makes payments to security holders only from cash flows 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.
5. 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 the market value of the vehicle's assets.

The foregoing criteria grant exemptive relief most clearly to (i) ABS transactions registered pursuant to Regulation AB, and (ii) Rule 144A and private placement securitizations that are exempt from the Investment Company Act of 1940 pursuant to Rule 3a-7 promulgated thereunder, in each case that meets the criteria set forth in items 2 through 5 above. Rule 144A and private placement securitizations that meet the definition of "asset-backed security" under Regulation AB, but that are not otherwise exempt under Rule 3a-7, will need to be analyzed based on their own facts.

Examples of nonexempt securitization vehicles may include asset-backed commercial paper conduits, covered bonds, CLO and CDO transactions, whole business securitizations, certain timeshare and tax lien securitizations, and other esoteric securitizations.

The CFTC stated, however, that it remains open to discussions regarding the facts and circumstances of other securitization vehicles and whether additional relief may be appropriate.

Scope of Exemptive Relief for Certain REITs

In a separate interpretive letter issued on October 11, 2012, the Division of Swap Dealer and Intermediary Oversight excluded certain REITs from the definition of "commodity pool," and any operator of such entity will not be a CPO with respect to such entity so long as the following criteria are met:

1. The REIT derives its income primarily from the ownership and management of real estate and uses derivatives for the limited purpose of mitigat[ing] their exposure to changes in interest rates or fluctuations in currency;

2. The REIT is operated so as to comply with all of the requirements of a REIT election under the Internal Revenue Code, including 26 U.S.C. § 856(c)(2) (the 75 percent test) and 26 U.S.C. § 856(c)(3) (the 95 percent test); and
3. The REIT has identified itself as an equity REIT in Item G of its last U.S. income tax return on Form 1120-REIT and continues to qualify as such, or, if the REIT has not yet filed its first tax filing with the Internal Revenue Service, the REIT has stated its intention to do so to its participants and effectuates its stated intention.

Extension of Registration Deadline

In a separate no-action letter, the CFTC also extended to December 31, 2012 the deadline for CPOs and CTAs to apply for registration, where the requirement to be registered arises from the swaps activity of the CPO or CTA. The CPO or CTA must make a good faith effort to comply with the CEA and applicable CFTC regulations on and after December 31, 2012. The temporary relief also extends to introducing brokers, floor brokers, floor traders, and associated persons of a futures commission merchant.

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