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## Collins Amendment Carve Out

### *Volcker Rule Relief for Investments in Bank TruPS CDOs*

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In response to industry pressure, the OCC, Board, FDIC, SEC and CFTC (collectively, “the Agencies”) announced on January 14, an Interim Final Rule<sup>1</sup> effective April 1, 2014 that would permit banking entities to retain investments in collateralized debt obligations (CDOs) that have a majority of their assets invested in Qualifying Trust Preferred Securities (TruPS) Collateral defined as TruPS or subordinated debt that was:

- issued prior to May 19, 2010, by a depository institution holding company with less than \$15 billion in consolidated assets as of the end of any reporting period in the 12 months immediately preceding the issuance of such instrument; or
- issued prior to May 19, 2010, by a mutual holding company.

The definition of Qualifying TruPS Collateral is consistent with the requirements of section 171 of the Dodd-Frank Act (DFA), which is commonly referred to as the Collins Amendment. This Amendment permanently grandfathers as tier 1 capital TruPS issued before May 19, 2010 by bank holding companies with less than \$15 billion in assets as of December 31, 2009. As such, the Collins Amendment Carve Out would allow bank investors to avoid the Volcker Rule (section 619 of the DFA) restrictions on investments in CDOs if majority of the underlying collateral consisted of bank TruPS CDOs. It should be noted that TruPS CDOs with a majority of collateral issued by REITs or insurance companies would not benefit from the Collins Amendment Carve Out and would be subject to divestiture by July 21, 2015.

The logic behind the Collins Amendment Carve Out is straightforward. Under section 171 of the DFA, Congress intended for community banks below \$15 billion in assets to have efficient access to tier 1 capital and grandfathered TruPS issued prior to May 19, 2010 as a source of tier 1 capital. These community banks generally did not have direct access to the capital markets and relied on pooled investment structures such as CDOs as the primary method to access the TruPS market. Under section 619 of the DFA, an investment in the debt tranche of a CDO structure could be considered an Ownership Interest in a

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<sup>1</sup> Interim Final Rule, the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), the Securities and Exchange Commission (SEC) and Commodity Futures Trading Commission (CFTC), January 14, 2014.

Covered Fund that must be divested before July 21, 2015. This created an inconsistency between supporting TruPS as tier 1 capital for community banks through section 171, while penalizing the CDO structure which was the means by which most community banks issued TruPS. The Collins Amendment Carve Out reconciles this inconsistency between section 619 and section 171 of the DFA by allowing banking entities to invest in CDOs primarily consisting of Qualifying TruPS Collateral. This relief also extends to the activities of a banking entity acting as a sponsor for one of these securitization vehicles.

The Agencies expect the Collins Amendment Carve Out to apply to substantially all bank TruPS CDOs. To reduce the burden of each bank having to analyze CDO transactions that closed many years ago, the Agencies have provided a non-exclusive list of issuers that meet the requirements of the Collins Amendment Carve Out, which are summarized in Appendix A.<sup>2</sup>

While the Collins Amendment Carve Out provides regulatory relief from the potential forced sale of bank TruPS CDOs, the Agencies specifically noted that nothing in the interim final rule “limits or restricts the ability of the appropriate agency to place limits on any activity conducted or investment held pursuant to the exemption in a manner consistent with their safety and soundness...”<sup>3</sup> In other words, investors in bank TruPS CDOs may have avoided an explicit sale requirement, but safety and soundness standards may lead banks to reduce their overall exposure. Importantly, the Collins Amendment Carve Out does not address the Volcker Rule’s restriction on bank investment in collateralized loan obligations, which may be the next regulatory shoe to drop.<sup>4</sup>

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<sup>2</sup> Joint Press Release, Board of Governors of the Federal Reserve System, Commodity Futures Trading Commission, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and Securities and Exchange Commission, Non-exclusive List of TruPS CDOs, pgs. 3-4.

<sup>3</sup> Interim Final Rule, the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), the Securities and Exchange Commission (SEC) and Commodity Futures Trading Commission (CFTC), January 14, 2014, pg 9.

<sup>4</sup> For a broader discussion of the impact of the Volcker Rule prepared by the author please refer to “*The Volcker Rule’s Impact on Regional and Community Banks*,” December 13, 2013.  
<http://www.sandleroneill.com/Collateral/Documents/English-US/Volcker%20Rule%20Impact.pdf>

## APPENDIX A

ISSUER	#
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ALESCO	4
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ALESCO	10
ALESCO	11
ALESCO	12
ALESCO	13
ALESCO	14
ALESCO	15
ALESCO	16
ALESCO	17
MMCAPS	1
MMCAPS	17
MMCAPS	18
MMCAPS	19
MMCOMMUNITY	1
MMCOMMUNITY	2
MMCOMMUNITY	3
MMCOMMUNITY	9
Preferred CPO	1
PRETSL	1
PRETSL	2
PRETSL	3
PRETSL	4
PRETSL	5
PRETSL	6
PRETSL	7
PRETSL	8
PRETSL	9
PRETSL	10
PRETSL	11

ISSUER	#
PRETSL	12
PRETSL	13
PRETSL	14
PRETSL	15
PRETSL	16
PRETSL	17
PRETSL	18
PRETSL	19
PRETSL	20
PRETSL	21
PRETSL	22
PRETSL	23
PRETSL	24
PRETSL	25
PRETSL	26
PRETSL	27
PRETSL	28
REG DIV	1
REG DIV	2004-1
REG DIV	2005-1
SOLOSO	1
SOLOSO	2
TPREF Funding	1
TPREF Funding	2
TPREF Funding	3
TRAPEZA CDO	1
TRAPEZA CDO	2
TRAPEZA CDO	3
TRAPEZA CDO	4
TRAPEZA CDO	5
TRAPEZA CDO	6
TRAPEZA CDO	7
TRAPEZA CDO	9
TRAPEZA CDO	10
TRAPEZA CDO	11
TRAPEZA CDO	12
TRAPEZA CDO	13
TRAPEZA EDGE	1

ISSUER	#
TROPIC CDO	1
TROPIC CDO	2
TROPIC CDO	3
TROPIC CDO	5
TROPIC CDO	4
USCAP FUNDING	1
USCAP FUNDING	2
USCAP FUNDING	3
USCAP FUNDING	4
USCAP FUNDING	5
USCAP FUNDING	6

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*At Sandler O'Neill, Mr. Killian has managed the successful execution of 13 M&A transactions representing over \$2.4 billion in deal value and \$8.5 billion of capital raising transactions. He has co-managed the Sandler O'Neill team responsible for successfully completing 17 pooled trust preferred transactions that raised over \$7 billion for approximately 650 financial institutions. Included in Mr. Killian's capital raising transactions are eight recapitalization and restructuring transactions that involved complex capital structures designed to preserve tax benefits for the issuing institutions. He functions as a primary resource in structuring and implementing complex capital markets transactions for financial institutions.*

*Mr. Killian holds a Bachelor of Science from the University of North Carolina at Chapel Hill, where he was a John Motley Morehead Merit Scholar, and a Masters in Business Administration from Northwestern University's J.L. Kellogg Graduate School of Management. He has represented Sandler O'Neill in conferences with the Federal Financial Institutions Examination Council, the Federal Reserve, the Federal Deposit Insurance Corporation, and SNL Financial to discuss capital structure, Dodd-Frank and Basel III related issues. His articles have appeared in Bank Accounting & Finance, U.S. Banker and Modern Bankers, a publication of the Peoples Bank of China.*

*Mr. Killian is also a founding board member of Students Bridging the Information Gap, a 501(c)(3) charity that provides computers, books and other support to African schools and orphanages.*

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