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**MEMORANDUM**

February 12, 2018

To Our Clients and Friends

Re: Court of Appeals Strikes Down Credit Risk Retention Rules as Applied to CLO Managers

The U.S. Court of Appeals for the D.C. Circuit has ruled that the rules adopted by the Federal Reserve Board and Securities and Exchange Commission which require a securitizer of an asset-backed security to retain a portion of the credit risk of any asset transferred to a third party do not apply to investment managers of open-market collateralized loan obligations (CLOs).

Section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act directs the SEC and the Federal banking agencies to adopt rules to require a securitizer of an asset-backed security to retain not less than 5 percent of the credit risk for any asset that the securitizer transfers, sells or conveys to a third party. Only the SEC and the Federal Reserve adopted rules relating to credit retention. The agencies' rules treated CLO managers as securitizers, asserting that the failure to do so would result in a loophole whereby securitizations could be structured using third party managers to avoid the rules. The court concluded that, given the nature of the transactions performed by CLO managers, the language of the statute does not encompass their activities because CLO managers never possess the assets being transferred. The court further determined that the agencies' interpretation "seems to stretch the statute beyond the natural meaning of what Congress wrote; it turns 'retain' a credit risk into 'obtain' a credit risk."

A copy of the court's decision in *Loan Syndications and Trading Association v. SEC and Federal Reserve Board* (USCA DC Circuit No. 17-004) is available on our website at <http://www.schwartzandballen.com/news.html>

If you have any questions, please call Gilbert Schwartz, Robert Ballen, Tom Fox, Heidi Wicker, or Magda Gathani at (202) 776-0700.