Proposed Rules

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This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 709

Involuntary Liquidation of Federal Credit Unions and Adjudication of Creditor Claims Involving Federally-insured Credit Unions in Liquidation

AGENCY: National Credit Union Administration.

ACTION: Notice of proposed rulemaking.

SUMMARY: The National Credit Union Administration (NCUA) is publishing for notice and comment a proposed rule regarding the treatment by the NCUA Board (Board), as conservator or liquidating agent, of financial assets transferred by a federally-insured credit union to another party: in connection with a securitization; or in the form of a participation. The proposal also addresses the treatment by the Board, as conservator or liquidating agent, of agreements entered into by a federally-insured credit union to collateralize public funds. The proposal generally provides that the Board will not, by exercise of its statutory power to repudiate contracts, recover, reclaim, or recharacterize as property of the credit union or the liquidation estate financial assets that were transferred by the credit union to another party in connection with a securitization or in the form of a participation. The proposal also establishes that the Board will not seek to avoid an otherwise legally enforceable and perfected security interest in collateral for public funds solely because the collateral was not acquired contemporaneously with the approval and execution of the security agreement. The Board will also not seek to avoid a security interest solely because the collateral was changed, increased or subject to substitution from time to time.

DATES: Written comments must be received by the NCUA on or before April 3, 2000.

ADDRESSES: Direct comments to Becky Baker, Secretary of the Board. Mail or hand-deliver comments to: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428. You may also fax comments to (703) 518–6319. Please send comments by one method only.

FOR FURTHER INFORMATION CONTACT: Chrisanthy J. Loizos or Mary F. Rupp, Staff Attorneys, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

Background

Section 709.10

Under generally accepted accounting principles, a transfer of financial assets is accounted for as a sale if the transferor surrenders control over the assets. One of the conditions for determining whether the transferor has surrendered control is that the assets have been isolated from the transferor, i.e., put presumptively beyond the reach of the transferor, its creditors, a trustee in bankruptcy, or a receiver. This is known as the ''legal isolation'' condition.

Where the transferor is a federally-insured credit union for which the Board may be appointed conservator or liquidating agent, the issue arises whether financial assets transferred in connection with a securitization or in the form of a participation would be put beyond the reach of the Board as conservator or liquidating agent. The issue arises because of the Board's statutory authority to repudiate credit union contracts and, also, sections 207(b)(9) and 208(a)(3) of the Federal Credit Union Act (the Act) regarding the enforceability of agreements against the NCUA. 12 U.S.C. 1787(b)(9), 1788(a)(3). The specific issues are: whether the Board might exercise its authority to repudiate contracts, and avoid a transfer of financial assets in connection with a securitization or a participation to recover assets; and whether the Board, with respect to an agreement executed in relation to a transfer of financial assets in connection with a securitization or a participation, might assert the requirements of sections 207(b)(9) and 208(a)(3) of the Act. Those sections provide, that, to be enforceable against the NCUA, any agreement that tends to diminish or defeat the NCUA's interest in an asset must be executed contemporaneously with the acquisition of the asset by the credit union (the ''contemporaneous'' requirement).

The Federal Deposit Insurance Corporation (FDIC) published a Notice of Proposed Rulemaking, 64 FR 48968, Sept. 9, 1999, to resolve the issues raised above in the Statement of Financial Accounting Standards No. 125 (SFAS 125), issued by the Financial Accounting Standards Board. FDIC addressed whether its statutory authority to repudiate contracts under section 11(e) of the Federal Deposit Insurance Act (12 U.S.C. 1821(e)) would prevent a transfer of financial assets by an insured depository institution in connection with a securitization or in the form of a participation from satisfying the ''legal isolation'' condition of SFAS 125. The Federal Credit Union Act contains provisions substantially similar to 12 U.S.C. 1821(e) that apply when the Board is appointed conservator or liquidating agent for a federally-insured credit union. *See* 12 U.S.C. 1787, 1788. As such, this preamble and proposed rule track the language of the FDIC's proposed rule, 12 CFR 360.6.

Under 12 U.S.C. 1787(c)(1), the Board, when acting as conservator or liquidating agent of any federally-insured credit union, has the power to disaffirm or repudiate any contract or lease (i) to which the credit union is a party; (ii) the performance of which the conservator or liquidating agent, in the conservator's or liquidating agent's discretion, determines to be burdensome; and (iii) the disaffirmance or repudiation of which the conservator or liquidating agent determines, in the conservator's or liquidating agent's discretion, will promote the orderly administration of the credit union's affairs. Repudiation of a contract relieves the Board from performing any unperformed obligations remaining under the contract. Repudiation also entitles the other party to the contract to a claim for damages, which are limited by statute to actual direct compensatory damages determined as of the date of the appointment of the liquidating agent or conservator. *See* 12 U.S.C. 1787(c)(3).

Under sections 207(b)(9) and 208(a)(3) of the Act, no agreement that tends to diminish or defeat the NCUA's interest in an asset acquired from a federally-insured credit union is enforceable against the NCUA unless such

agreement meets certain requirements. One of those requirements is that the agreement be executed by the credit union and any person claiming an adverse interest thereunder contemporaneously with the acquisition of the asset by the credit union.

In order for a transfer of financial assets by a federally-insured credit union in connection with a securitization or in the form of a participation to be accounted for as a sale, the proposed rule provides that the Board, by exercise of its authority to disaffirm or repudiate contracts under 12 U.S.C. 1787(c), will not reclaim, recover, or recharacterize as property of the credit union or the liquidation estate any financial assets transferred by a federally-insured credit union to another party in connection with a securitization or in the form of a participation. Although the repudiation of a securitization or participation will not affect transferred financial assets, repudiation will excuse the Board from performing any continuing obligations imposed by the securitization or participation. If the Board, in order to terminate such continuing obligations or duties, seeks to disaffirm or repudiate an agreement or contract under which a federally-insured credit union has transferred financial assets to another party in connection with a securitization or a participation, the Board will not seek to reclaim, recover, or recharacterize as property of the credit union or the liquidation estate such financial assets.

The proposed rule applies only to those securitizations or participations in which the transfer of financial assets meets all of the conditions for sale accounting treatment under generally accepted accounting principles, other than the ''legal isolation'' condition, which the proposed rule is intended to address. While the proposed rule enables a credit union to meet the ''legal isolation'' condition, it does not replace the credit union management's responsibility to establish evidence supporting the isolation criterion of SFAS 125.

As part of the definition of ''participation,'' the proposed rule provides that a participation must be ''without recourse,'' that is, the participation must not be subject to any agreement that requires the lead institution to repurchase the participant's interest or to otherwise compensate the participant upon the borrower's default on the underlying obligation. The term ''without recourse'' does not, however, preclude the lead institution from retaining a subordinated interest in the participated obligation, against which losses are initially allocated.

The proposed rule does not apply unless the federally-insured credit union received adequate consideration for the transfer of financial assets at the time of the transfer. Also, the documentation effecting the transfer of financial assets must reflect the intent of the parties to treat the transaction as a sale, and not as a secured borrowing, for accounting purposes.

The proposed rule will not waive, limit or otherwise affect the rights or powers of the Board to take any action or to exercise any power not specifically limited by this section. This includes any rights, powers or remedies of the Board regarding transfers taken in contemplation of the credit union's insolvency or with the intent to hinder, delay, or defraud the institution or the creditors of the credit union, or that is a fraudulent transfer under applicable law.

The proposed rule further provides that the Board will not seek to avoid an otherwise legally enforceable securitization agreement or participation agreement executed by a federally-insured credit union solely because such agreement does not meet the ''contemporaneous'' requirement of sections 207(b)(9) and 208(a)(3) of the Act. 12 U.S.C. 1787(b)(9), 1788(a)(3).

The Board intends the proposed rule to apply to securitizations and participations engaged in by federally-insured credit unions while the rule is in effect, even if the rule is later amended or repealed. Paragraph (g) of the proposed rule provides that the rule will be effective unless repealed by the NCUA upon 30 days notice and opportunity for comment provided in the **Federal Register**. This paragraph also provides that any repeal or amendment of the rule by the NCUA will not apply to any transfer of financial assets made in connection with a securitization or participation that was in effect before such repeal or amendment. As a result of paragraph (g), where a transfer of financial assets in connection with a securitization or in the form of a participation is made by a credit union and the securitization or participation was in effect before any repeal or amendment of the rule by the NCUA, such transfer will continue to satisfy the legal isolation requirement notwithstanding the repeal or amendment.

Section 709.11

The Act authorizes federally-insured credit unions to become depositories of public money. 12 U.S.C. 1767 and 12 U.S.C. 1789a. Federal credit unions may receive payments, representing equity, on shares, share certificates and share draft accounts from nonmember units of federal, state, local or tribal governments and political subdivisions as enumerated in section 207(k)(2)(A) of the Act. 12 U.S.C. 1757(6). As a public depository, a federal credit union may pledge any of its assets to secure the payment of the public funds. 12 U.S.C. 1767(b).

NCUA received an inquiry as to the enforceability of security interests for public funds in federally-insured credit unions when the granting of security interests to protect public funds is authorized or required by state or federal law. On April 30, 1993, the FDIC addressed this precise issue in its ''Statement of Policy Regarding Treatment of Security Interests After Appointment of the Federal Deposit Insurance Corporation as Conservator or Receiver.'' The FDIC found that, provided the following five assumptions were met, when acting as conservator or receiver, it would not seek to avoid an otherwise legally enforceable and perfected security interest solely because the security agreement granting or creating such security interest did not meet the ''contemporaneous'' requirements of sections 11(d)((), 11(n)(4)(I), and 13(e) of the Federal Deposit Insurance Act.

In its analysis, FDIC assumed the following: (1) the agreement was undertaken in the ordinary course of business, not in contemplation of insolvency, and with no intent to hinder, delay or defraud the depository institution or its creditors; (2) the secured obligation represented a bona fide and arm's length transaction; (3) the secured party or parties were not insiders or affiliates of the depository institution; (4) the grant or creation of the security interest was for adequate consideration; and (5) the security agreement evidencing the security interest was in writing, approved by the depository institution's board of directors or loan committee (which approval is reflected in the minutes of a meeting of the board of directors or committee) and has been, continuously from the time of its execution, an official record of the depository institution. 58 FR 16833, March 31, 1993. Congress enacted the tenor of FDIC's policy statement in section 317 of the Riegle Community Development and Regulatory Improvement Act of 1994. 12 U.S.C. 1823(e)(2).

The Board believes it should limit its extraordinary authority as a conservator or liquidating agent with special provisions for security interests related to public funds. This will allow

federally-insured credit unions to offer governmental depositors the same protections the Federal Deposit Insurance Act provides them for deposits in banks. As such, the proposed rule establishes that the Board, acting as conservator or liquidating agent for a federally-insured credit union, will not seek to avoid an otherwise legally enforceable and perfected security interest in collateral for public funds solely because the security agreement granting or creating such security interest does not meet the contemporaneous requirement of sections 207(b)(9) and 208(a)(3) of the Federal Credit Union Act. The Board will not avoid a security interest because the collateral was not acquired contemporaneously with the approval and execution of the security agreement or because the collateral changed, increased or was subject to substitution from time to time.

Under NCUA's Interpretive Ruling and Policy Statement 87–2, the Board's general policy is to provide a 60-day comment period for a proposed regulation. In this case, the Board believes that a 30-day comment period will be adequate and is appropriate given that the proposal has the effect of providing greater flexibility for federally-insured credit unions.

Regulatory Procedures

Paperwork Reduction Act

NCUA has determined that the proposed amendments do not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget. The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact any final regulation may have on a substantial number of small entities (primarily those under $1 million in assets). For purposes of this analysis, credit unions under $1 million in assets will be considered small entities. As of June 30, 1999, there were 1,690 such entities with a total of $807.3 million in assets, with an average asset size of $0.5 million. These small entities make up 15.6 percent of all credit unions, but only 0.2 percent of all credit union assets.

The proposed rule addresses the manner in which the Board will enforce its rights as a conservator or liquidating agent when evaluating financial assets transferred during a securitization or participation, or reviewing the collateralization of public funds. The proposed rule does not impose additional reporting or recordkeeping burdens that are not already a function of entering into such transactions. Therefore, the Board has determined and certifies that this proposed rule, if adopted, will not have a significant economic impact on a substantial number of small credit unions.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their regulatory actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. This proposed rule, if adopted, will apply to all federally-insured credit unions, but it will not have substantial direct effects on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that the proposed rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this proposed rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Agency Regulatory Goal

NCUA's goal is to promulgate clear and understandable regulations that impose minimal regulatory burden. We request your comments on whether the proposed amendment is understandable and minimally intrusive if implemented as proposed.

List of Subjects in 12 CFR Part 709

Credit unions, Liquidations.

By the National Credit Union Administration Board on February 24, 2000.

Becky Baker,

Secretary of the Board.

For the reasons set out in the preamble, the NCUA proposes to amend 12 CFR part 709 as follows:

PART 709—INVOLUNTARY LIQUIDATION OF FEDERAL CREDIT UNIONS AND ADJUDICATION OF CREDITOR CLAIMS INVOLVING FEDERALLY-INSURED CREDIT UNIONS IN LIQUIDATION

1. The authority citation for part 709 is revised to read as follows:

Authority: 12 U.S.C. 1757; 12 U.S.C. 1766; 12 U.S.C. 1767; 12 U.S.C. 1786(h); 12 U.S.C. 1787; 12 U.S.C. 1788; 12 U.S.C. 1789; 12 U.S.C. 1789a.

2. Amend § 709.0 by revising the first sentence to read as follows:

§ 709.0 Scope.

The rules and procedures set forth in this part apply to charter revocations of federal credit unions under 12 U.S.C. 1787(a)(1)(A), (B), the involuntary liquidation and adjudication of creditor claims in all cases involving federally-insured credit unions, the treatment by the Board as conservator or liquidating agent of financial assets transferred in connection with a securitization or participation, and the treatment by the Board as conservator or liquidating agent of public funds held by a federally-insured credit union. * * *

3. Add § 709.10 to part 709 to read as follows:

§ 709.10 Treatment by conservator or liquidating agent of financial assets transferred in connection with a securitization or participation.

(a) *Definitions.* (1) *Beneficial interest* means debt or equity (or mixed) interests or obligations of any type issued by a special purpose entity that entitle their holders to receive payments that depend primarily on the cash flow from financial assets owned by the special purpose entity.

(2) *Financial asset* means cash or a contract or instrument that conveys to one entity a contractual right to receive cash or another financial instrument from another entity.

(3) *Legal isolation* means that transferred financial assets have been put presumptively beyond the reach of the transferor, its creditors, a trustee in bankruptcy, or a receiver, either by a single transaction or a series of transactions taken as a whole.

(4) *Participation* means the transfer or assignment of an undivided interest in all or part of a loan or a lease from a seller, known as the ''lead,'' to a buyer, known as the ''participant,'' without recourse to the lead, under an agreement between the lead and the participant. *Without recourse* means that the participation is not subject to any agreement that requires the lead to repurchase the participant's interest or to otherwise compensate the participant upon the borrower's default on the underlying obligation.

(5) *Securitization* means the issuance by a special purpose entity of beneficial interests:

(i) The most senior class of which at time of issuance is rated in one of the four highest categories assigned to long-

term debt or in an equivalent short-term category (within either of which there may be sub-categories or gradations indicating relative standing) by one or more nationally recognized statistical rating organizations; or

(ii) Which are sold in transactions by an issuer not involving any public offering for purposes of section 4 of the Securities Act of 1933, as amended, or in transactions exempt from registration under such Act under 17 CFR 230.901 through 230.905 (Regulation S) thereunder (or any successor regulation).

(6) *Special purpose entity* means a trust, corporation, or other entity with a distinct standing at law separate from the federally-insured credit union that is primarily engaged in acquiring and holding (or transferring to another special purpose entity) financial assets, and in activities related or incidental thereto, in connection with the issuance by such special purpose entity (or by another special purpose entity that acquires financial assets directly or indirectly from such special purpose entity) of beneficial interests.

(b) The Board, by exercise of its authority to disaffirm or repudiate contracts under 12 U.S.C. 1787(c), will not reclaim, recover, or recharacterize as property of the credit union or the liquidation estate any financial assets transferred to another party by a federally-insured credit union in connection with a securitization or participation, provided that a transfer meets all conditions for sale accounting treatment under generally accepted accounting principles, other than the ''legal isolation'' condition addressed by this section.

(c) Paragraph (b) of this section will not apply unless the federally-insured credit union received adequate consideration for the transfer of financial assets at the time of the transfer, and the documentation effecting the transfer of financial assets reflects the intent of the parties to treat the transaction as a sale, and not as a secured borrowing, for accounting purposes.

(d) Paragraph (b) of this section will not be construed as waiving, limiting, or otherwise affecting the power of the Board, as conservator or liquidating agent, to disaffirm or repudiate any agreement imposing continuing obligations or duties upon the federally-insured credit union in conservatorship or the liquidation estate.

(e) Paragraph (b) of this section will not be construed as waiving, limiting or otherwise affecting the rights or powers of the Board to take any action or to exercise any power not specifically limited by this section, including, but not limited to, any rights, powers or remedies of the Board regarding transfers taken in contemplation of the credit union's insolvency or with the intent to hinder, delay, or defraud the credit union or the creditors of such credit union, or that is a fraudulent transfer under applicable law.

(f) The Board will not seek to avoid an otherwise legally enforceable securitization agreement or participation agreement executed by a federally-insured credit union solely because such agreement does not meet the ''contemporaneous'' requirement of sections 207(b)(9) and 208(a)(3) of the Federal Credit Union Act.

(g) This section may be repealed by the NCUA upon 30 days notice and opportunity for comment provided in the **Federal Register**, but any such repeal or amendment will not apply to any transfers of financial assets made in connection with a securitization or participation that was in effect before such repeal or modification. For purposes of this paragraph, a securitization would be in effect on the earliest date that the most senior level of beneficial interests is issued, and a participation would be in effect on the date that the parties executed the participation agreement.

4. Add § 709.11 to part 709 to read as follows:

§ 709.11 Treatment by conservator or liquidating agent of collateralized public funds.

An agreement to provide for the lawful collateralization of funds of a federal, state, or local governmental entity or of any depositor or member referred to in section 207(k)(2)(A) of the Act will not be deemed to be invalid under section 208(a)(3) of the Act solely because such agreement was not executed contemporaneously with the acquisition of collateral or with any changes in the collateral made in accordance with such agreement.

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COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 4

RIN 3038–AB37

Exemption for Commodity Pool Operators With Respect to Offerings to Qualified Eligible Participants; Exemption for Commodity Trading Advisors With Respect to Advising Qualified Eligible Clients

AGENCY: Commodity Futures Trading Commission.

ACTION: Proposed rule.

SUMMARY: The Commodity Futures Trading Commission (''Commission'') is proposing to revise Commission Rule 4.7 (''Proposal'').[1] Rule 4.7 provides a simplified regulatory framework for commodity pool operators (''CPOs'') operating commodity pools consisting of certain highly accredited pool participants, termed ''qualified eligible participants'' (''QEPs''), and for commodity trading advisors (''CTAs'') directing or guiding the commodity interest trading accounts of certain highly accredited clients, termed ''qualified eligible clients'' (''QECs''). The Proposal would revise the rule both substantively and technically.

The proposed substantive revisions are intended to make Rule 4.7 available to more CPOs and CTAs and under more situations, by bringing within the scope of the rule those additional persons who the Commission now believes should be included in the QEP and QEC definitions. The Proposal would add, among others, the following persons to the existing QEP and QEC definitions: Principals of the registered investment professionals currently defined as QEPs and QECs; certain registered securities investment advisers and their principals; ''qualified purchasers'' and ''knowledgeable employees'' as those terms are defined under the federal securities laws; certain employees of pools, CPOs and CTAs and certain of those employees' immediate family members; and trusts whose advisors and settlors are QEPs or QECs. In addition, the Proposal would make it easier for certain charitable organizations, trusts and collective investment vehicles to be QEPs and QECs, and, under certain circumstances, it would include persons who are not ''United States persons'' in the QEC definition. Certain of the proposed technical revisions, *i.e.,* those which would reorganize the rule, are intended

[1] Commission rules referred to herein are found at 17 CFR Ch. I.