

Bond Case Briefs

Municipal Finance Law Since 1971

Moody's Rates First TOB that Passes Volcker Rule.

Fears that a \$75 billion corner of the municipal bond market for Tender Option Bonds would be closed down by the Volcker Rule may have been squashed with a new deal from Bank of America Merrill Lynch. The tiny \$8.545 million deal has been structured to comply with Volcker Rule restrictions by using two loopholes in the Investment Company Act of 1940.

BofA's new Tender Option Bonds (TOB) creation has received Moody's Aaa/VMIG imprimatur. If regulators approve the new structure, it could be a template to restart the dormant TOB market.

Here is an example of a general TOB structure from Nuveen. The Volcker Rule does not apply to Nuveen, but the TOB structure is roughly equivalent to all muniland issuers.



Bank of America and its investment arm Merrill Lynch have altered the way the TOB trust (green box in the chart above) is organized to satisfy Volcker Rule restrictions on a bank owning hedge funds or trusts.

Rather than being separate parties in a TOB, Merrill Lynch combined all the deal participants into a joint venture trust between BofA and the investors in the trust. This structure takes advantage of the joint venture exception in the 40 Act. Moody's says:

Merrill Lynch's transaction relies on the joint venture exemption from 40 Act registration. Unlike a typical TOB where Merrill Lynch would have acted as the issuer of the TOB trust, in the new structure, Merrill Lynch sold the bonds via a sale agreement to a joint venture trust. The joint venture agreement is between Bank of America, N.A. (A2/ P-1) as trustor and liquidity provider and the floating and inverse floating rate investors (the parties purchasing the interests in the joint venture).

BofA established the joint venture trust and Merrill Lynch sold the underlying bonds (State of Maryland General Obligation Bonds, State and Local Facilities Loan of 2013, First Series B Tax-Exempt Bonds due August 1, 2019 and the Cusip for the TOB is 46641N) into the trust.

The other parties in the joint venture trust will be money market and closed-end funds that buy the cash flow portions of the deal. The new structure limits the number of these outside parties in the trust to take advantage of another 40 Act registration exemption related to the number of parties in a trust (or hedge fund). Moody's again:

The agreement limits participation to 10 parties. Joint ventures among 10 or fewer participants are exempt from registration under the 40 Act. TOBs structured as joint ventures do not fit the definition of hedge funds included in the Volcker Rule, making it possible for banks to sponsor and invest in them.

Here are the parties in the deal, according to Moody's:

Liquidity provider and Trustor – Bank of America NA

Trustee – US Bank Trust NA

Venturers (that’s what they call it instead of “investors”) – to be determined but limited to 10

Remarketing agent – Merrill Lynch

This is muniland structured finance at its best. There are many other nuances to the deal that you can find in the [Moody’s rating announcement](#). Stay tuned for reactions from regulators. Moody’s foresees current TOBs possibly altering its legal structure if the new BofA trust structure meets regulator approval.

By Cate Long JUNE 13, 2014

Copyright © 2026 Bond Case Briefs | bondcasebriefs.com