Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

January 17, 2006

Interpretive Letter #1049
January 2006
12 CFR 3

Dear **[ ]**:

This letter responds to your e-mails of April 26 and September 15, 2005 requesting confirmation of your interpretation of the appropriate capital treatment for a commitment to make a commercial or trade letter of credit. You characterize the arrangement as a multipurpose loan commitment in which the borrower has the option to use the commitment in one of several ways, including a trade letter of credit. For this type of arrangement, you believe that the credit conversion factor (CCF) for the unused portion of the multipurpose commitment allocated exclusively to a trade letter of credit should be zero percent under a short-term commitment and 20 percent under a commitment greater than one year. Based on the facts presented, the OCC has determined that the regulatory risk-based capital treatment you describe for the trade letter of credit portion of a multipurpose loan commitment is consistent with current OCC regulations.

Background

Multipurpose loan commitments are commitments under which credit can be extended to a borrower in several forms at the option of the borrower. The borrower may use the commitment, in full, in any of the various options, unless the commitment specifies sub limits for the available forms of credit. In the situation you describe, a portion of the multipurpose loan commitment may be drawn only as a trade letter of credit, a trade-related contingency that is short-term, self-liquidating, and collateralized by goods.

Discussion

To determine the risk-based capital charge for an off-balance sheet exposure, the OCC's capital rules require a two-step process.[1] First, to determine an on-balance sheet equivalent amount, the amount of the off-balance sheet exposure is multiplied by the applicable CCF. Then the resulting on-balance sheet amount is assigned a risk weight based on the relevant obligor, guarantor, and/or collateral.

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[1] 12 CFR 3, appendix A, 3(b).

The capital rules assign a zero percent CCF to unused commitments if the original maturity of the commitment is one year or less and a 50 percent CCF if the original maturity is greater than one year.[2] When a trade letter of credit is issued, the resulting exposure is also an off-balance sheet exposure. The capital rules assign a CCF of 20 percent to this type of exposure.[3]

The OCC's capital rules, however, do not explicitly state how a commitment to make a trade letter of credit should be treated for risk-based capital purposes. You believe that the appropriate CCF for the portion of a multipurpose loan commitment that may be drawn only as a trade letter of credit should be zero for a short-term commitment and 20 percent for a commitment over one year, i.e., a commitment to make a trade letter of credit would receive the lower of the CCFs applicable to an issued trade letter of credit or a commitment to make a trade letter of credit. Because a trade letter of credit is a short-term exposure that self-liquidating, a trade letter of credit is generally considered to be a relatively low-risk transaction. Accordingly, a short-term commitment to make a trade letter of credit should not have a higher CCF than a short-term commitment to make a loan. Similarly, a commitment with a maturity greater than one year to make a trade letter of credit should not incur a higher CCF than the CCF for an issued trade letter of credit.

Conclusion

Based on your description of the multipurpose loan commitment with an option to draw a part of the commitment only as a trade letter of credit, the OCC has determined that the appropriate CCF for risk-based capital purposes would be the lower of the CCFs applicable to a loan commitment with the same original maturity or to the issued trade letter of credit. Furthermore, in the case in which the sub limits for the types of credit available under the multipurpose commitment overlap and the types of credit have different CCFs, the highest CCFs are applied to the maximum draws for risk-based capital purposes. Should you have additional questions, please contact Nancy Hunt, risk expert, Capital Policy Division at (202) 874-5070.

Sincerely,

/s/ *Tommy Snow*

Tommy Snow
Director, Capital Policy

[2] 12 CFR 3, appendix A, 3(b)(2)(ii) and (4)(i).
[3] 12 CFR 3, appendix A, 3(b)(3)(i).