



# OCC BULLETIN

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Comptroller of the Currency  
Administrator of National Banks

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Subject: Risk-Based Capital - Recourse, Direct Credit  
Substitutes and Residual Interests

Description: Final Rule

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Washington, DC 20219

**TO:** Chief Executive Officers of National Banks, Department and Division Heads, Examining Personnel and Other Interested Parties

## PURPOSE

This bulletin transmits the final rule on Recourse, Direct Credit Substitutes and Residual Interests in Asset Securitizations that was published in the *Federal Register* on November 29.

## SUMMARY

The final rule amends the agencies' regulatory capital standards to align more closely the risk-based capital treatment of recourse obligations and direct credit substitutes. It also varies the capital requirements for positions in securitized transactions and certain other exposures according to their relative credit risk and requires capital commensurate with the risks associated with residual interests.

The final rule is a result of the combination of two separate notices of proposed rulemaking: a proposed rule on Recourse and Direct Credit Substitutes (65 FR 12320, March 8, 2000), and a proposed rule on Residual Interests in Asset Securitizations or Other Transfers of Financial Assets (65 FR 57993, September 27, 2000). The two proposals overlapped in scope in that both addressed leveraged credit risk. Recognizing the overlap and interaction between the two proposals, a single final rule that combines aspects of the two proposals has been developed.

The final rule amends the regulatory capital standards as follows:

- It defines the terms "recourse", "residual interest" and related terms, and revises the definition of "direct credit substitute";
- It provides more consistent risk-based capital treatment for recourse obligations and direct credit substitutes;
- It varies the capital requirements for positions in securitization transactions according to their relative risk exposure, using credit ratings from rating agencies to measure the level of risk;
- It permits the limited use of a banking organization's qualifying internal risk rating system to determine the capital requirement for certain unrated direct credit substitutes;
- It permits the limited use of a rating agency's review of the credit risk of positions in

structured programs and qualifying software to determine the capital requirement for certain unrated direct credit substitutes and recourse exposures (but not residual interests);

- It requires a banking organization to deduct credit-enhancing interest-only strips, whether retained or purchased, that are in excess of 25 percent of Tier 1 capital from Tier 1 capital and from assets;
- It requires a banking organization to maintain risk-based capital in an amount equal to the face amount of a residual interest that does not qualify for the ratings-based approach; and
- It permits the modification of a stated risk weight, credit conversion factor or credit equivalent amount, if warranted, on a case-by-case basis.

The rule is effective January 1, 2002. Any transactions settled on or after that date are subject to the final rule. Banking organizations that have settled transactions before January 1, 2002 that result in increased capital requirements under the rule may delay the application of the rule to those transactions until December 31, 2002. Banking organizations may elect early adoption, as of November 29, 2001, of any provision of the final rule.

**FOR FURTHER INFORMATION CONTACT:**

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Attachment 66 FR 59614