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NR 2000-9

February 17, 2000

AGENCIES PROPOSE REVISION OF RISK-BASED CAPITAL RULES'
TREATMENT OF RECOURSE AND DIRECT-CREDIT SUBSTITUTES

The four federal banking agencies today released proposed revisions to their risk-based capital requirements for certain obligations related to securitized transactions.

The proposal by the Federal Reserve Board, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency and Office of Thrift Supervision is intended to produce more consistent capital treatment for credit risks associated with exposures arising from securitization transactions. It would amend the risk-based capital requirements for asset-backed securities as well as recourse obligations and direct credit substitutes.

Public comment is requested by May 26, 2000.

In securitizations, assets such as residential and commercial mortgages, credit-card receivables and automobile loans are pooled and reconstituted into securities. Securitizations typically carve up the credit risks from underlying assets and redistribute them to different parties. Sellers of assets into a securitization may retain part of the risk of credit loss through recourse arrangements. Sellers also may arrange for a third party, such as a banking organization, to accept some of the credit risk through guarantees, referred to as direct credit substitutes.

The proposed revisions would:

- Assign a risk-based charge to positions in securitized transactions according to the relative credit risk of those positions, as measured by credit ratings received from nationally recognized rating agencies.
- Treat recourse obligations and direct credit substitutes more consistently under risk-based capital rules.
- Define "recourse" and revise the definition of "direct credit substitute."
- Permit the limited use of an institution's internal risk-rating system and other alternative approaches in determining the risk-based capital requirement for unrated direct credit substitutes associated with asset-backed commercial paper programs and other structured finance programs.
- Require banking organizations to hold additional risk-based capital against risks presented by the early amortization feature of revolving asset securitizations.

(more)

The interagency proposal published today incorporates many of the industry comments received in response to an earlier version published in November 1997. A consultative paper issued in June 1999 by the Basel Committee on Banking Supervision considers a similar approach to that contained in this proposal.

The preamble of the agencies' notice of proposed rulemaking is attached. The full notice will be published in the Federal Register.

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