

program.²⁹ If a banking organization is not deemed an originator of a securitization transaction, then it would be considered an investor in the securitization.

There are several methods for determining the A-IRB capital requirement for a securitization exposure: the Ratings-Based Approach (RBA), the Alternative RBA, the Supervisory Formula Approach (SFA), the Look-Through Approach, deduction from Tier 1 capital, and deduction from total capital. The following table summarizes conditions under which a banking organization would apply each of these methods. In this table, KIRB denotes the ratio of (a) the pool's A-IRB capital charge to (b) the notional or loan equivalent amount of underlying exposures in the pool.

Steps for Determining A-IRB Capital Requirements for Securitization Exposures

For an investing banking organization:

1. Deduct from total capital any credit-enhancing interest-only strips

2. When an external or inferred rating exists, apply the RBA

3. When an external or inferred rating does not exist, do the following:

a. Subject to supervisory review and approval, if the investing banking organization can determine KIRB, then calculate required capital as would an originating banking organization using the steps described in 2.a. below

b. Otherwise, deduct the exposure from total capital

For an originating banking organization:*

1. Deduct from Tier 1 capital any increase in capital resulting from the securitization transaction and deduct from total capital any credit-enhancing interest-only strips (net of deductions from Tier 1 capital due to increases in capital)

2. When an A-IRB approach exists for the underlying exposures do the following:

a. If KIRB can be determined:

i. For a securitization exposure (or portion thereof) that is at or below KIRB, deduct the exposure from total capital

ii. For a securitization exposure (or portion thereof) that is above KIRB:

1. Apply the RBA whenever an external or inferred rating is available

2. Otherwise, apply the SFA

b. If KIRB cannot be determined:

i. Apply the Look-Through Approach if the exposure is an eligible liquidity facility, subject to supervisory approval

ii. Otherwise, deduct the exposure from total capital

3. When an A-IRB approach does not exist for the underlying exposures do the following:

a. Apply the Look-Through Approach if the exposure is an eligible liquidity facility, subject to supervisory approval

b. Otherwise, apply the Alternative RBA

Deductions of Gain-on-Sale or Other Accounting Elements That Result in Increases in Equity Capital

Any increase in equity capital resulting from a securitization transaction (for example, a gain resulting from FAS 140 accounting treatment of the sale of assets) would be deducted from Tier 1 capital. Such deductions are intended to offset any gain on sale or other accounting treatments ("gain on sale") that result in an increase in an originating banking organization's shareholders' equity and Tier 1 capital. Over time, as banking organizations, from an accounting perspective, realize the increase in equity that was booked at origination of a securitization transaction through actual receipt of cash flows, the amount of the required deduction would be reduced accordingly.

Banking organizations would have to deduct from total capital any on-balance-sheet credit-enhancing interest-only strips (net of any increase in the shareholders' equity deducted from Tier 1 capital as described in the previous paragraph).³⁰ Credit-enhancing interest-only strips are defined in the general risk-based capital rules and include items, such as excess spread, that represent subordinated cash flows of future margin income.

Maximum Capital Requirement

Where an A-IRB approach exists for the underlying exposures, an originating banking organization's total A-IRB capital charge for exposures associated with a given securitization transaction would be subject to a maximum or ceiling. This maximum A-IRB capital charge would equal the pool's A-IRB capital charge plus any required deductions, as described in the preceding paragraphs. The aim of this treatment is to ensure that an institution's effective A-IRB capital

charge generally would not be greater after securitization than before, while also addressing the Agencies' safety and soundness concerns with respect to credit-enhancing interest-only strips and other capitalized assets.³¹

The proposed maximum A-IRB capital requirement effectively would reverse one aspect of the general risk-based capital rules for securitization exposures referred to as residual interests. Under the general risk-based capital rules, banking organizations are required to hold a dollar in capital for every dollar in residual interest, regardless of the capital requirement on the underlying exposures. One of the reasons the Agencies adopted the "dollar-for-dollar" capital treatment for residual interests is that in many instances the relative size of the exposure retained by the originating banking organization reveals additional market information about the quality of the underlying exposures and deal structure that may not have been captured in the capital requirement on the underlying exposures, had those exposures remained on the banking organization's balance sheet. The Agencies will continue to review the proposal for safety and soundness considerations and may consider retaining the current dollar-for-dollar capital treatment for residual interests, especially in those instances where an originator retains first loss and other deeply subordinated interests in amounts that significantly exceed the pool's A-IRB capital charge plus required deductions.

Comments are invited on the circumstances under which the retention of the treatment in the general risk-based capital rules for residual interests for banking organizations using the A-IRB approach to securitization would be appropriate.

Should the Agencies require originators to hold dollar-for-dollar capital against all retained securitization exposures, even if this treatment would result in an aggregate amount of capital required of the originator that exceeded the pool's A-IRB capital charge plus any applicable deductions? Please provide the underlying rationale.

Investors

Third-party investors generally do not have access to detailed, ongoing information about the credit quality of the underlying exposures in a securitization. In such cases, investors often rely upon credit assessments made by external rating agencies. For a securitization exposure held by an investing banking organization, and

²⁹ A banking organization is generally considered a sponsor of an ABCP conduit or similar program if, in fact or in substance, it manages or advises the conduit program, places securities into the market for the program, or provides liquidity support or credit enhancements to the program.

* In addition to the capital treatments delineated, an originating banking organization's total A-IRB capital charge with regard to any single securitization transaction is subject to a maximum or ceiling, as described later in this section.

³⁰ Deductions other than of increases in equity capital are to be taken 50 percent from Tier 1 capital and 50 percent from Tier 2 capital.

³¹ The maximum capital, requirement also applies to investing banking organizations that receive approval to use the SFA.