

Simplified method for computing N and LGD. Under the conditions provided below, banking organizations would be able to employ simplified methods for calculating N and the exposure-weighted average LGD. When

the underlying exposures are retail exposures, the SFA may be implemented by setting $h = 0$ and $v = 0$, subject to supervisory approval and review. When the share of the pool associated with the largest exposure, C_1 ,

is no more than 0.03 (or 3 percent of the pool), the banking organization would be able to set $LGD = 0.50$ and N equal to:

$$N = \left(C_1 C_m + \left(\frac{C_m - C_1}{m - 1} \right) \max\{1 - m C_1, 0\} \right)^{-1},$$

provided that the banking organization can measure C_m , which denotes the share of the pool corresponding to the largest “m” exposures (for example, a 15 percent share corresponds to a value of 0.15).⁴⁶ Alternatively, when only C_1 is available and this amount is no more than 0.03, then the banking organization would be able to set $LGD = 0.50$ and $N = 1 / C_1$.

The Agencies seek comment on the proposed SFA. How might it be simplified without sacrificing significant risk sensitivity? How useful are the alternative simplified computation methodologies for N and LGD

The Look-Through Approach for Eligible Liquidity Facilities

ABCP conduits and similar programs sponsored by U.S. banking organizations are major sources of funding for financial and non-financial companies. Liquidity facilities supporting these programs are considered to be securitization exposures of the banking organizations providing the liquidity, and generally would be treated under the rules proposed for originators. As a general matter, the Agencies expect that banking organizations using the A-IRB approach would apply the SFA when determining the A-IRB capital requirement for liquidity facilities provided to ABCP conduits and similar programs. However, if it would not be practical for a banking organization to calculate KIRB for the underlying exposures using a top-down or a bottom-up approach, the banking organization may be allowed to use the Look-Through Approach, described below, for determining the A-IRB capital requirement, subject to supervisory approval and only for a temporary period of time to be determined in consultation with the organization's primary Federal supervisor.

Because the Look-Through Approach has limited risk sensitivity, the Agencies

propose that its applicability be restricted to liquidity facilities that are structured to minimize the extent to which the facilities provide credit support to the conduit. The Look-Through Approach would only be available to liquidity facilities that meet the following criteria:

(a) The facility documentation clearly identifies and limits the circumstances under which it may be drawn. In particular, the facility must not be able to cover losses already sustained by the pool of underlying exposures (for example, to acquire assets from the pool at above fair value) or be structured such that draw-down is highly probable (as indicated by regular or continuous draws);

(b) The facility is subject to an asset quality test that prevents it from being drawn to cover underlying exposures that are in default;

(c) The facility cannot be drawn after all applicable (specific and program-wide) credit enhancements from which the liquidity facility would benefit have been exhausted;

(d) Repayment of any draws on the facility (that is, assets acquired under a purchase agreement or loans made under a lending agreement) may not represent a subordinated obligation of the pool or be subject to deferral or waiver; and

(e) Reduction in the maximum drawn amount, or early termination of the facility, occurs if the quality of the pool falls below investment grade.

Under the Look-Through Approach, the liquidity facility's A-IRB capital charge would be computed as the product of (a) 8 percent, (b) the maximum potential drawdown under the facility, (c) the applicable credit conversion factor (CCF), and (d) the applicable risk weight. The CCF would be set at 50 percent if the liquidity facility's original maturity is one year or less, and at 100 percent if the original maturity is more than one year. The

Agencies propose that the risk weight be set equal to the risk weight applicable under the general risk-based capital rules for banking organizations not using the A-IRB approach (that is, to the underlying assets or obligors after consideration of collateral or guarantees or, if applicable, external ratings).

The Agencies seek comment on the proposed treatment of eligible liquidity facilities, including the qualifying criteria for such facilities. Does the proposed Look-Through Approach—to be available as a temporary measure—satisfactorily address concerns that, in some cases, it may be impractical for providers of liquidity facilities to apply either the “bottom-up” or “top-down” approach for calculating KIRB? It would be helpful to understand the degree to which any potential obstacles are likely to persist.

Feedback also is sought on whether liquidity providers should be permitted to calculate A-IRB capital charges based on their internal risk ratings for such facilities in combination with the appropriate RBA risk weight. What are the advantages and disadvantages of such an approach, and how might the Agencies address concerns that the supervisory validation of such internal ratings would be difficult and burdensome? Under such an approach, would the lack of any maturity adjustment with the RBA be problematic for assigning reasonable risk weights to liquidity facilities backed by relatively short-term receivables, such as trade credit?

Other Considerations

Capital Treatment Absent an A-IRB Approach—The Alternative RBA

For originating banking organizations when there is not a specific A-IRB treatment for an underlying exposure or group of underlying exposures, the Agencies propose that a securitization exposure's A-IRB capital charge be based exclusively on the exposure's external or inferred credit rating using

LGd may be conservative for other types of ABSs. However, the Agencies believe that the complexity and burden associated with a more refined treatment of LGDs would outweigh any improvement in the overall risk sensitivity of A-

IRB capital charges for originators, owing to the combined effects of (a) the dollar-for-dollar A-IRB capital charge on positions at or below KIRB, and (b) the maximum or cap on an originator's total A-IRB capital charge.

⁴⁶ The level of m is to be set by each banking organization.

⁴⁷ The Alternative RBA does not apply to eligible liquidity facilities, which may use the Look-