

facilitate the issuance of the commercial paper.¹

In January 2003, the Financial Accounting Standards Board (FASB) issued interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46), requiring the consolidation of variable interest entities (VIEs) onto the balance sheets of companies deemed to be the primary beneficiaries of those entities.² FIN 46 may result in the consolidation of many ABCP programs onto the balance sheets of banking organizations beginning in the third quarter of 2003. In contrast, under pre-FIN 46 accounting standards, banking organizations normally have not been required to consolidate the assets of these programs. Banking organizations that are required to consolidate ABCP program assets will have to include all of these program assets (mostly receivables and securities) and liabilities (mainly commercial paper) on their September 30, 2003 balance sheets for purposes of the bank Reports of Condition and Income (Call Report), the Thrift Financial Report (TFR), and the bank holding company financial statements (FR Y-9C Report). If no changes were made to regulatory capital standards, the resulting increase in the asset base would lower both the tier 1 leverage and risk-based capital ratios of banking organizations that must consolidate the assets held in ABCP programs.

The agencies believe that the consolidation of ABCP program assets onto the balance sheets of sponsoring banking organizations could result in risk-based capital requirements that do not appropriately reflect the risks faced

by banking organizations that sponsor these programs. The agencies believe that sponsoring banking organizations generally face limited risk exposure to ABCP programs, which generally is confined to the credit enhancements and liquidity facility arrangements that they provide to these programs. In addition, operational controls and structural provisions, along with overcollateralization or other credit enhancements provided by the companies that sell assets into ABCP programs can further mitigate the risk to which sponsoring banking organizations are exposed. Because of the limited risks, the agencies believe that it is appropriate to provide an interim risk-based capital treatment that permits sponsoring banking organizations to exclude from risk-weighted assets, on a temporary basis, assets held by ABCP programs that must be consolidated onto the balance sheets of sponsoring banking organizations as a result of FIN 46.

The period during which the interim rule is in effect will provide the agencies with additional time to develop the appropriate risk-based capital requirements for banking organizations' sponsorship and other involvement with ABCP programs and to receive comments from the industry on a related proposal also published in today's **Federal Register**.

II. Interim Risk-Based Capital and Regulatory Reporting Treatment

The agencies are amending their risk-based capital standards to permit sponsoring banking organizations to exclude the assets of ABCP programs that must be consolidated under FIN 46 from risk-weighted assets when they calculate their tier 1 and total risk-based capital ratios for the quarters ending September 30, 2003, December 31, 2003, and March 31, 2004. Sponsoring banking organizations must continue to assess risk-based capital against any credit enhancements or long-term liquidity facilities that they provide to such ABCP programs. For example, banking organizations that sponsor ABCP programs generally assign any investment-grade equivalent credit enhancements that they provide to these programs to the 100 percent risk weight category.³ Most liquidity facilities

currently provided to ABCP programs are structured with a maturity of less than one year and, under the agencies' current risk-based capital rules, do not incur a capital charge.

Under this interim rule, for the third and fourth quarters of 2003, as well as for the first quarter of 2004, when reporting items 34 through 43 on Schedule RC-R (*Regulatory Capital*) of the Call Report and Schedule HC-R (*Regulatory Capital*) of the FR Y-9C, any consolidated ABCP program assets resulting from application of FIN 46 are to be reported in column A, "Totals (from Schedule RC)," as well as in column B, "Items not Subject to Risk-Weighting." With respect to the TFR, thrifts should not include the subject program assets in any of the lines for assets to risk weight on Schedule CCR that comprise the subtotal on line CCR64.

Reporting in this manner will exclude the ABCP program assets from incorporation into the calculation of the risk-based capital ratios. Banking organizations should continue to report the notional amounts of any credit enhancements and liquidity facilities provided to ABCP programs in the risk-based capital schedule line items in which these exposures would be properly reported as of the June 30, 2003 reporting date. In addition, credit enhancements and liquidity facilities that sponsoring banking organizations provide to their ABCP programs are to be reported in Memorandum items 3.a.(1) and 3.b.(1) of Schedule RC-S (*Servicing, Securitization, and Asset Sale Activities*) of the Call Report and Schedule HC-S (*Servicing, Securitization, and Asset Sale Activities*) of the FR Y-9C consolidated reports, respectively. Thrifts should include any related credit enhancements on Schedule CC, lines CC455, CC465, or CC468, as appropriate.

In addition, any minority interests in ABCP programs that are consolidated as a result of FIN 46 are to be excluded from sponsoring banking organizations' minority interest component of tier 1 capital and, hence, also from total risk-based capital. Exclusion from capital of any minority interests associated with consolidated ABCP programs is required when the programs' assets are not included in an organization's risk-weighted asset base and, thus, are not assessed a risk-based capital charge. When sponsoring banking organizations report item 6, "Qualifying minority interest in consolidated subsidiaries," of

percent risk weight category or effectively deducted from risk-based capital.

¹ For the purposes of this rulemaking, a banking organization is considered the sponsor of an ABCP program if it establishes the program, approves the sellers permitted to participate in the program; approves the asset pools to be purchased by the program; or administers the ABCP program by monitoring the assets, arranging for debt placement, compiling monthly reports, or ensuring compliance with the program documents and with the program's credit and investment policy.

² Under FIN 46, the FASB broadened the criteria for determining when one entity is deemed to have a controlling financial interest in another entity and, therefore, when an entity must consolidate another entity in its financial statements. An entity generally does not need to be analyzed under FIN 46 if it is designed to have "adequate capital" as described in FIN 46 and its shareholders control the entity with their share votes and are allocated its profits and losses. If the entity fails these criteria, it typically is deemed a VIE and each stakeholder in the entity (a group that can include, but is not limited to, legal-form equity holders, creditors, sponsors, guarantors, and servicers) must assess whether it is the entity's "primary beneficiary" using the FIN 46 criteria. This analysis considers whether effective control exists by evaluating the entity's risks and rewards. The stakeholder who holds the majority of the entity's risks or rewards is the primary beneficiary and must consolidate the VIE.

³ Under the agencies' risk-based capital standards, banking organizations may, subject to supervisory approval, use their internal risk ratings system to assess the credit quality of non-rated direct credit substitutes provided to ABCP programs in order to determine the appropriate risk-based capital charge. Direct credit substitutes provided to ABCP programs that are the equivalent of non-investment grade are assigned to either the 200