AGENCIES ADOPT RE COURSE, DIRECT CREDIT SUBSTITUTES AND RESIDUAL INTERESTS FINAL RULE

The federal bank and thrift regulatory agencies today announced the publication of a final rule that changes their regulatory capital standards to address the treatment of recourse obligations, residual interests and direct credit substitutes that expose banks, bank holding companies, and thrifts (collectively, banking organizations) to credit risk.

The final rule, published in today’s Federal Register, synthesizes the capital treatment outlined in two notices of proposed rulemakings issued in 2000—“Recourse and Direct Credit Substitutes” and “Residual Interests in Asset Securitizations or Other Transfers of Financial Assets.” The final rule treats recourse obligations and direct credit substitutes more consistently than the agencies’ current risk-based capital standards, and introduces a credit ratings-based approach to assigning risk weights within a securitization. The final rule also imposes a “dollar-for-dollar” capital charge on residual interests and a concentration limit on credit-enhancing interest-only strips, a subset of residual interests.

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

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