



Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

June 14, 2005

Interpretive Letter #1057
May 2006

Dear []:

This response is to your letter of March 21, 2005 that requests confirmation of an interpretation of the appropriate capital treatment for a multipurpose loan commitment. You characterize a multipurpose loan commitment as an arrangement where the borrower has the option to utilize the commitment in one of several ways, including a standby letter of credit (SBLC). For this type of arrangement, you believe that the credit conversion factor (CCF) for the unused portion of the multipurpose commitment should be the same as the CCF for a standard loan commitment, notwithstanding the option to issue a SBLC under the commitment. Based on the facts presented, the OCC has determined this application of regulatory risk-based capital treatment for the multipurpose loan commitment is consistent with current OCC regulations.

Background

Multipurpose loan commitments are commitments under which credit can be extended to a borrower in several forms at the option of the borrower. Under this type of arrangement, the borrower may utilize the commitment to obtain, for example, a revolving loan, a term loan, or an SBLC. The borrower may draw down the commitment, in full, in any of the various options, unless the commitment specifies a sublimit for particular forms of credit. Multipurpose loan commitments are used by borrowers to satisfy a broad range of corporate purposes such as working capital, acquisition of capital assets, and refinancing.

Discussion

According to the OCC's capital rules, the risk-based capital charge for a commitment, which is an off-balance sheet activity, is determined by a two-step process.¹ The amount of the commitment is multiplied by the appropriate CCF and the resulting amount is assigned a risk weight based on the relevant obligor, guarantor, and/or collateral. The OCC's risk-based capital rules assign unused loan commitments a CCF of zero percent if the original maturity is one year

¹ 12 C.F.R. Part 3, appendix A, § 3(b).

or less and 50 percent CCF if the maturity is greater than one year.² By contrast, an off-balance sheet commitment in the form of an SBLC is considered a direct credit substitute and is assigned a 100 percent CCF.³ The rules include an SBLC in the definition of a “direct credit substitute” because it “supports financial claims on a third party that exceed a bank’s *pro rata* share in that financial claim.”⁴

Your letter states that the current OCC regulations are unclear about the appropriate CCF for a multipurpose loan commitment that includes an option for an SBLC. As you note, the OCC’s regulations do not explicitly say that a commitment to issue an SBLC should be treated as an SBLC for risk-based capital purposes. In addition, the definition of a direct credit substitute refers explicitly to the credit exposure of a third party asset but, in the case of a multipurpose loan commitment, the third party asset is not yet identified. Accordingly, you conclude that it is not possible to determine the *pro rata* share of risk for a third party asset. Based on the structure of a multipurpose loan commitment, it is also possible that an SBLC may never be issued. Thus, you believe the appropriate CCF for a multipurpose loan commitment where an SBLC is one drawdown option should be the same as the CCF for a loan commitment as long as no specific third party asset is identified for the SBLC commitment. More specifically, you suggest that the CCF should be zero for an original maturity of one year or less and 50 percent for an original maturity greater than one year.

Conclusion

Based on your description of the multipurpose loan commitment and the absence of a third party asset for which an SBLC might be issued under the commitment, the OCC has determined that the appropriate CCF for risk-based capital purposes would be the CCF applicable to a loan commitment with the same original maturity. In the event where the borrower notifies the bank about a pending transaction, i.e., a third party asset is identified, then the part of the commitment that would be drawn down as an SBLC would be subject to a 100 percent CCF. This determination is made specifically based on the facts presented for the transactions described above, and may not be relied upon for determining the risk-based capital treatment of any other transaction. Finally, the capital treatment at the holding company level is subject to the requirements set forth by the Federal Reserve, which may differ from this interpretation. Should you have additional questions, please contact Nancy Hunt, Risk Expert, OCC at 202-874-5070.

Sincerely,

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Tommy Snow
Director, Capital Policy

² 12 C.F.R. Part 3, appendix A, § 3(b)(2)(ii) and (4)(i).

³ 12 C.F.R. Part 3, appendix A, § 4(a)(4) and (b)(1).

⁴ 12 C.F.R. Part 3, appendix A, § 4(a)(4).