Securitization

Contents

A. Scope and definitions of transactions covered under the securitization framework

538. Banking corporations must apply this Directive for determining regulatory capital requirements on exposures arising from traditional and synthetic securitizations or similar structures that contain features common to both. Since securitizations may be structured in many different ways, the capital treatment of a securitization exposure must be determined on the basis of its economic substance rather than its legal form. Similarly, the Supervisor will look to the economic substance of a transaction to determine whether it should be subject to the securitization framework for purposes of determining regulatory capital. Banking corporations are encouraged to consult with the Supervisor of Banks when there is uncertainty about whether a given transaction should be considered a securitization.

539. *A traditional securitization* is a structure where the cash flow from an underlying pool of exposures is used to service at least two different stratified risk positions or tranches reflecting different degrees of credit risk. Payments to the investors depend upon the performance of the specified underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures. The stratified/tranched structures that characterize securitizations differ from ordinary senior/subordinated debt instruments in that junior securitization tranches can absorb losses without interrupting contractual payments to more senior tranches, whereas subordination in a senior/subordinated debt structure is a matter of priority of rights to proceeds of liquidation.

540. *A synthetic securitization* is a structure with at least two different stratified risk positions or tranches that reflect different degrees of credit risk where credit risk of an underlying pool of exposures is transferred, in whole or in part, through the use of funded (e.g., credit-linked notes) or unfunded (e.g., credit default swaps) credit derivatives or guarantees that serve to hedge the credit risk of the portfolio. Accordingly, the investors' potential risk is dependent upon the performance of the underlying pool. In synthetic securitization, the

exposures included in the underlying pool remain on the originating banking corporation's balance sheet.

541. Banking corporations' exposures to a securitization are hereafter referred to as "**securitization exposures**". Securitization exposures can include but are not restricted to the following: asset-backed securities, mortgage-backed securities, credit enhancements, liquidity facilities, interest rate or currency swaps, credit derivatives, and tranched cover as described in Section 199 of Proper Conduct of Banking Business Directive number 203. Reserve accounts, such as cash collateral accounts, recorded as an asset by the originating banking corporation must also be treated as securitization exposures.

541(i) A resecuritization exposure is a securitization exposure in which the risk associated with an underlying pool of exposures is tranched into levels of risk, and at least one of the underlying exposures is itself a securitization exposure. In addition, an exposure to one or more resecuritization exposures is also a resecuritization exposure.

542. Underlying instruments in the pool being securitized may include but are not restricted to the following: loans, commitments, asset-backed and mortgage-backed securities, corporate bonds, equity securities, and private equity investments. The underlying pool may include one or more exposures.

B. Definitions and general terminology

1. Originating banking corporation

543. For risk-based capital purposes, a banking corporation is considered to be an originator with regard to a certain securitization if it meets either of the following conditions:

a. The banking corporation originates directly or indirectly underlying exposures included in the securitization; or

b. The banking corporation serves as a sponsor of an asset-backed commercial paper (ABCP) conduit or similar program that acquires exposures from third-party entities. In the context of such programs, a banking corporation would generally be considered a sponsor and, in turn, an originator if it, in fact or in substance, manages or advises the program, places securities into the market, or provides liquidity and/or credit enhancements.

2. Asset-backed commercial-paper program

544. An asset-backed commercial paper (ABCP) program predominately issues commercial paper with an original maturity of one year or less that is backed by assets or other exposures held in a bankruptcy-remote special-purpose entity.

3. Clean-up call

545. A clean-up call is an option that permits the securitization exposures (e.g., asset-backed securities) to be called before all of the underlying exposures or securitization exposures have been repaid. In the case of traditional securitizations, this is generally accomplished by repurchasing the remaining securitization exposures once the pool balance or outstanding securities have fallen below some specified level. In the case of a synthetic transaction, the clean-up call may take the form of a clause that extinguishes the credit protection.

4. Credit enhancement

546. A credit enhancement is a contractual arrangement in which the banking corporation retains or assumes a securitization exposure and, in substance, provides some degree of added protection to other parties to the transaction.

5. Credit-enhancing interest-only strip

547. A credit-enhancing interest-only strip (I/O) is an on-balance sheet asset that (1) represents a valuation of cash flows related to future margin income, and (2) is subordinated.

6. Early amortization

548. Early amortization provisions are mechanisms that, once triggered, allow investors to be paid out prior the originally stated maturity of the securities

issued. For risk-based capital purposes, an early amortization provision will be considered either controlled or non-controlled.

A controlled early amortization provision must meet all of the following conditions:

a. The banking corporation must have an appropriate capital/liquidity plan in place to ensure that it has sufficient capital and liquidity available in the event of an early amortization.

b. Throughout the duration of the transaction, including the amortization period, there is the same pro-rata sharing of interest, principal, expenses, losses and recoveries based on the banking corporation's and investors' relative shares of the receivables outstanding at the beginning of each month.

c. The banking corporation must set a period for amortization that would be sufficient for least 90% of the total debt outstanding at the beginning of the early amortization period to have been repaid or recognized as in default; and

d. The pace of repayment should not be any more rapid than would be allowed by straight-line amortization over the period set out in criterion c.

549. An early amortization provision that does not satisfy the conditions for a controlled early amortization provision will be treated as a non-controlled early amortization provision.

7. Excess spread

550. Excess spread is generally defined as gross finance charge collections and other income received by the trust or special-purpose entity (SPE—see definition in Section 552 below), minus certificate interest, service fees, charge-offs, and other senior trust or SPE expenses.

8. Implicit support

551. Implicit support arises when a banking corporation provides support to a securitization in excess of its predetermined contractual obligation.

9. Special-purpose entity—SPE

552. An SPE is a corporation, trust, or other entity organized for a specific purpose, the activities of which are limited to those appropriate to accomplish the purpose of the SPE, and the structure of which is intended to isolate the SPE from the credit risk of an originator or seller of exposures. SPEs are commonly used as financing vehicles in which exposures are sold to a trust or similar entity in exchange for cash or other assets funded by debt issued by the trust.

C. Operational requirements for the recognition of risk transference

553. The following operational requirements are applicable to the standardized approach of securitization.

1. Operational requirements for traditional securitizations

554. An originating banking corporation may exclude securitized exposures from the calculation its risk-weighted assets only if all of the following conditions have been met. Banking corporations meeting these conditions must still hold regulatory capital against all securitization exposures they retain.

a. Significant credit risk associated with the securitized exposures has been transferred to third parties.

b. The transferor does not maintain effective or indirect control over the transferred exposures. The assets are legally isolated from the transferor in such a way (e.g. through the sale of assets or through subparticipation) that the exposures are put beyond the reach of the transferor and its creditors, even in bankruptcy or receivership. These conditions must be supported by an opinion provided by a qualified legal counsel.

The transferor is deemed to have maintained effective control over transferred credit risk exposures if it:

1) is able to repurchase from the transferee the previously transferred exposures in order to realize their benefits; or

2) is obligated to retain the risk of the transferred exposures.

The transferor's retention of servicing rights to the exposures will not necessarily constitute indirect control of the exposures.

c. The securities issued are not obligations of the transferor. Thus, investors who purchase the securities only have claim to the underlying pool of exposures.

d. The transferee is an SPE and the holders of the beneficial interests in that entity have the right to pledge or exchange them without restriction.

e. Clean-up calls must satisfy the conditions set out in Section 557.

f. The securitization does not contain clauses that:

1) require the originating banking corporation to alter the underlying exposures systematically such that the pool's weighted average credit quality is improved, unless this is achieved by selling assets to independent and unaffiliated third parties at market prices;

2) allow for increases in a retained first-loss position or credit enhancement provided by the originating banking corporation after the transaction's inception; or

3) increase the yield payable to parties other than the originating banking corporation, such as investors and third-party providers of credit enhancements, in response to a deterioration in the credit quality of the underlying pool.

2. Operational requirements for synthetic securitization

555. For synthetic securitization transactions, the use of CRM techniques (i.e., collateral, guarantees, and credit derivatives) for hedging the underlying exposure may be recognized for risk-based capital purposes only if the conditions outlined below are satisfied:

a. Credit-risk mitigants must comply with the requirements set out in Sections 109–210 (Chapter D of Proper Conduct of Banking Business Directive number 203).

b. Eligible collateral is limited to that specified in Sections 145 and 146. Eligible collateral pledged by SPEs may be recognized.

c. Eligible guarantors are defined in Section 195. Banking corporations may not recognize SPEs as eligible guarantors in the framework of the Securitization Directive.

d. Banking corporations must transfer significant credit risk associated with the underlying exposure to third parties.

e. The instruments used to transfer credit risk may not contain terms or conditions that limit the amount of credit risk transferred, such as those provided below:

- Clauses that materially limit the credit protection or credit risk transference (e.g., significant materiality thresholds below which credit protection is deemed not to be triggered even if a credit event occurs or those that allow for the termination of the protection due to deterioration in the credit quality of the underlying exposures);
- Clauses that require the originating banking corporation to alter the underlying exposures to improve the pool's weighted average credit quality;
- Clauses that increase the banking corporation’s cost of credit-protection in response to deterioration in the pool's quality;
- Clauses that increase the yield payable to parties other than the originating banking corporation, such as investors and third-party providers of credit enhancements, in response to a deterioration in the credit quality of the reference pool; and
- Clauses that provide for increases in a retained first loss position or credit enhancement provided by the originating banking corporation after the transaction's inception.

f. An opinion must be obtained from a qualified legal counsel that confirms the enforceability of the contracts in all relevant jurisdictions.

g. Clean-up calls must satisfy the conditions set out in Section 557.

556. For synthetic securitizations, the effect of applying CRM techniques for hedging the underlying exposure are treated according to Sections 109–210 of Proper Conduct of Banking Business Directive number 203. In case there is a maturity mismatch, the capital requirement will be determined in accordance with Sections 202–205. When the exposures in the underlying pool have different maturities, the longest maturity must be taken as the maturity of the pool. Maturity mismatches may arise in the context of

synthetic securitizations when, for example, a banking corporation uses credit derivatives to transfer part or all of the credit risk of a specific pool of assets to third parties. When the credit derivatives unwind, the transaction will terminate. This implies that the effective maturity of the tranches of the synthetic securitization may differ from that of the underlying exposures. Originating banking corporations of synthetic securitizations must treat such maturity mismatches in the following manner: A banking corporation using the standardized approach for securitization must weight all retained positions that are unrated or rated below investment grade at 1250%. Accordingly, when a weight of 1250% is required, maturity mismatches are not taken into account. For all other securitization exposures, banking corporations must apply the maturity mismatch treatment set forth in Sections 202–205.

3. Operational requirements in clean-up calls

557. For securitization transactions that include a clean-up call, no capital will be required due to the presence of a clean-up call if the following conditions are met:

1) The exercise of the clean-up call must not be mandatory, in form or in substance, but rather must be at the discretion of the originating banking corporation;
2) The clean-up call must not be structured to avoid allocating losses to credit enhancements or positions held by investors or otherwise structured to provide credit enhancement; and
3) The clean-up call must only be exercizable when 10% or less of the original underlying portfolio, or securities issued remain, or, for synthetic securitizations, when 10% or less of the original reference portfolio value remains.

558. Securitization transactions that include a clean-up call that does not meet all of the criteria stated in Section 557 result in a capital requirement for the originating banking corporation.

For a traditional securitization, the underlying exposures must be treated as if they were not securitized. Additionally, banking corporations must not recognize in regulatory capital any gain-on-sale, as defined in Section 562.

For synthetic securitizations, the banking corporation purchasing protection must hold capital against the entire amount of the securitized exposures as if they did not benefit from any credit protection.

If a synthetic securitization incorporates a call option (other than a clean-up call) that effectively terminates the transaction and the purchased credit protection on a specific date, the banking corporation must treat the transaction in accordance with Section 556 and Sections 202–205 of Proper Conduct of Banking Business Directive number 203.

559. If a clean-up call, when exercised, is found to serve as a credit enhancement, the exercise of the clean-up call must be considered a form of implicit support provided by the banking corporation and must be treated in accordance with the supervisory guidance pertaining to securitization transactions.

D. Treatment of securitization exposures

1. Calculation of capital requirements

560. Banking corporations are required to hold regulatory capital against all their securitization exposures, including those arising from the provision of credit risk mitigants to a securitization transaction, investments in asset-backed securities, retention of a subordinated tranche, and extension of a liquidity facility or credit enhancement, as set forth in the following sections. Repurchased securitization exposures must be treated by a banking corporation as retained securitization exposures.

(i) Risk weight of 1250% / Deduction

561. Securitization exposures that have previously been deducted from regulatory capital shall be risk weighted at a rate of 1250%, as detailed in the tables below. Credit-enhancing I/Os (net of the amount that must be deducted from Tier 1 as specified in Section 562) shall be risk weighted at a rate of 1250%.

The risk weighting of 1250% may be done net of any specific provision taken against the relevant securitization exposures.

562. Banking corporations must deduct from Tier 1 any increase in equity capital resulting from securitization transactions, such as that associated with expected future margin income (FMI) resulting in a gain-on-sale that is recognized in regulatory capital. Such an increase in capital is referred to as a "gain-on-sale" for the purposes of the Securitization Framework.

563. Repealed.

(ii) Implicit support

564. When a banking corporation provides implicit support to a securitization, it must, at a minimum, hold capital against all of the exposures associated with the securitization transaction as if they had not been securitized. Additionally, banking corporations would not be permitted to recognize in regulatory capital any gain-on-sale, as defined in Section 562. Furthermore, the banking corporation is required to disclose publicly (a) that it has provided non-contractual support and (b) the capital impact of doing so.

2. Operational requirements for use of external credit assessments

565. The following operational criteria concerning the use of external credit assessments apply in the standardized approach of the Securitization Framework:

a. To be eligible for risk-weighting purposes, the external credit assessment must take into account and reflect the entire amount of credit risk exposure the banking corporation has with regard to all payments owed to it. For example, if a banking corporation is owed both principal and interest, the assessment must fully take into account and reflect the credit risk associated with timely repayment of both principal and interest.

b. The external credit assessments must be from an eligible External Credit Assessment Institute (ECAI) that is recognized by the Supervisor of Banks under Sections 91–108 of Proper Conduct of Banking Business

Directive number 203, with the following exception: In contrast with bullet three of Section 91, an eligible credit assessment must be publicly available. In other words, a rating must be published in an accessible form and included in the ECAI's transition matrix. Consequently, ratings that are made available only to the parties to a transaction do not satisfy this requirement.

c. Eligible ECAIs must have demonstrated expertise in assessing securitization transactions, which may be evidenced by strong market acceptance.

d. A banking corporation must apply credit assessments from eligible ECAIs consistently across a given type of securitization exposure. Furthermore, a banking corporation cannot use the credit assessments issued by one ECAI for one or more tranches and those of another ECAI for other positions (whether retained or purchased) within the same securitization structure that may or may not be rated by the first ECAI. Where two or more eligible ECAIs can be used and these assess the credit risk of the same securitization exposure differently, Sections 96–98 will apply.

e. When CRM is provided directly to an SPE by an eligible guarantor as defined in Section 195 and is reflected in an external credit assessment assigned to a securitization exposure(s), the risk weight associated with that external credit assessment should be used. In order to avoid any double counting, no additional capital recognition is permitted. If the CRM provider is not recognized as an eligible guarantor as defined in Section 195, the covered securitization exposures should be treated as unrated.

f. In the situation where a credit risk mitigant is not obtained directly by the SPE but rather applied to a specific securitization exposure within a given structure (e.g., ABS tranche), the banking corporation must treat the exposure as if it is unrated and then use the CRM treatment outlined in Sections 109–210 of Proper Conduct of Banking Business Directive number 203, to recognize the hedge.

g. (i) A banking corporation is not permitted to use any external credit assessment for the purpose of weighting risk if the assessment is at least partly based on unfunded support provided by the banking corporation. For example, if a banking corporation purchases ABCP (asset-backed commercial paper), where it provides unfunded support to that ABCP program (such as a liquidity facility or credit enhancement), and that support plays a role in determining the credit assessment on the ABCP, the banking corporation shall treat the ABCP as if it is not rated. The banking corporation shall continue to hold capital against the other securitization exposures it provides (for example, against the liquidity facility and/or credit enhancement).

(ii) The treatment described in Section 565g(i) is also applicable to exposures held in the trading book. The capital requirements for such exposures held in the trading book shall be no less than the amount required under the banking book treatment.

(iii) Banking corporations are permitted to recognize overlap in their exposures, consistent with that stated in Section 581. For example, a banking corporation that provides a liquidity facility supporting 100% of the ABCP issued by an ABCP program, and purchases 20% of the outstanding ABCP of that program, may recognize an overlap of 20% (100% liquidity facility + 20% commercial paper held – 100% commercial paper issued = 20%). If a banking corporation provides a liquidity facility that covers 90% of the outstanding ABCP, and purchases 20% of the ABCP, the two exposures would be treated as if there is a 10% overlap between the two exposures (90% liquidity facility + 20% commercial paper held – 100% commercial paper issued = 10%). If a banking corporation provides a liquidity facility that covers 50% of the outstanding ABCP, and purchases 20% of the ABCP, the two exposures would be treated as if there were no overlap. Such overlap may also be recognized between specific risk capital charges for exposures in the trading book and the capital charges for exposures in the banking book, provided that the banking corporation can calculate the capital charges in respect of the relevant exposures and compare them.

2.1 Information on the underlying collateral supporting securitization exposures

565(i) In order for the banking corporation to be able to use the securitization framework, it must hold the information that is detailed in Sections 565(ii) – 565(iv). A banking corporation that does not meet the requirements set forth in these Sections shall reduce its exposure from capital.

565(ii) As a general rule, a banking corporation must, on an ongoing basis, have a comprehensive understanding of the risk characteristics of each of its individual securitization exposures, whether on balance sheet or off balance sheet, as well as the risk characteristics of the exposure pools underlying its securitization exposures.

565(iii) A banking corporation must be able to access performance information on the underlying exposure pools on an ongoing basis and in a timely manner. This information may include the following details, as appropriate: exposure type; percentage of loans 30, 60 and 90 days past due; default rates; prepayment rates; loans in foreclosure; property type; occupancy; average credit score or other measures of creditworthiness; average Loan-to-Value (LTV) ratio; and industry and geographic diversification. For resecuritizations, a banking corporation shall have information not only on the underlying securitization tranches, such as the issuer name and credit quality, but also on the characteristics and performance of the pools underlying the securitization tranches.

565(iv). A banking corporation must have a thorough understanding of all structural features of a securitization transaction that would materially impact the performance of the banking corporation's exposures to the transaction, such as the contractual waterfall and waterfall-related triggers, credit enhancements, liquidity enhancements, market value triggers, and deal-specific definitions of default.

3. Standardized approach for securitization exposures

(i) Scope

566. Banking corporations that apply the standardized approach to credit risk for the type of underlying exposure(s) securitized must use the standardized approach under the Securitization Framework.

(ii) Risk weights

567. The risk-weighted asset amount of a securitization exposure is computed by multiplying the amount of the position (balance-sheet value) by the appropriate risk weight determined in accordance with the following tables. For off-balance-sheet exposures, banking corporations must multiply the exposure (nominal value) by credit conversion factors (CCF) and then risk weight the resultant credit equivalent amount. If such an exposure is rated, a CCF of 100% must be applied. For positions with long-term ratings of B+ and below and short-term ratings other than A-1/P-1, A-2/P-2, or A-3/P-3, a risk weight of 1250% is required. A risk weight of 1250% is also required for unrated positions, with the exception of the circumstances described in Sections 571–575.

Long-Term Rating Categories[95]
Securitization Exposures

[95] The rating designations used in the following tables are for illustrative purposes only and do not indicate any preference for, or endorsement of any particular external assessment system.

External credit assessment	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to BB-		B+ and below or unrated
Risk weight	20%	50%	100%	For originator—1250%	For investor—350%	1250%

Resecuritization Exposures

External credit assessment	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to BB-		B+ and below or unrated
Risk weight	40%	100%	225%	For originator—1250%	For investor—650%	1250%

Short-Term Rating Categories

Securitization Exposures

External credit assessment	A-1/P-1	A-2/P-2	A-3/P-3	All other ratings or unrated
Risk weight	20%	50%	100%	1250%

Resecuritization Exposures

External credit assessment	A-1/P-1	A-2/P-2	A-3/P-3	All other ratings or unrated
Risk weight	40%	100%	225%	1250%

568. The capital treatment of positions retained by originators, liquidity facilities, credit-risk mitigants, and securitizations of revolving exposures is identified separately. The treatment of clean-up calls is provided in Sections 557–559.

Investors may recognize ratings on below-investment grade exposures.

569. Only third-party investors, as opposed to banking corporations that serve as originators, may recognize external credit assessments that are equivalent to BB+ and BB– for risk weighting purposes of securitization exposures.

Originators to weight below-investment grade exposures

570. Originating banking corporations, as defined in Section 543, must weight all retained securitization exposures rated below investment grade (i.e. exposures rated below BBB–) at 1250%.

(iii) Exceptions to general treatment of unrated securitization exposures

571. As noted in the tables above, unrated securitization exposures must be weighted at 1250% with the following exceptions:

(1) the most senior exposure in a securitization;

(2) exposures that are in a second loss position or better in ABCP programs and that meet the requirements outlined in Section 574; and

(3) eligible liquidity facilities.

all of which as specified in Sections 572–576 below.

Treatment of unrated most senior securitization exposures

572. If the most senior exposure in a traditional or synthetic securitization is unrated, a banking corporation that holds or guarantees such an exposure may determine the risk weight by applying the “look-through” treatment, provided the composition of the underlying pool is known at all times. Banking corporations are not required to consider interest rate or currency swaps when determining whether an exposure is most senior in a securitization for the purpose of applying the “look-through” approach.

573. In the look-through treatment, the unrated most senior position receives the average risk weight of the underlying exposures subject to supervisory review. Where the banking corporation is unable to determine the risk weights assigned to the underlying credit risk exposures, the unrated position must be weighted at 1250%.

Treatment of exposures in a second loss position or better in ABCP programs

574. A weight of 1250% is not required for those unrated securitization exposures provided by sponsoring banking corporations of ABCP programs that satisfy the following requirements:

(a) The exposure is economically in a second loss position or better and the first loss position provides significant credit protection to the second loss position;

(b) The associated credit risk is the equivalent of investment grade or better; and

(c) The banking corporation holding the unrated securitization exposure does not retain or provide the first loss position.

575. Where the conditions in Section 574 are satisfied, the risk weight is the greater of (1) 100% or (2) the highest risk weight assigned to any of the underlying individual exposures covered by the facility.

Risk weights for eligible liquidity facilities

576. For eligible liquidity facilities as defined in Section 578, and where the conditions for use of external credit assessments in Section 565 are not met, the risk weight applied to the exposure's credit equivalent amount is equal to the highest risk weight assigned to any of the underlying individual exposures covered by the facility.

(iv) Credit conversion factors for off-balance-sheet exposures

577. For risk-based capital purposes, banking corporations must determine whether, according to the criteria outlined below, an off-balance sheet securitization exposure qualifies as an "eligible liquidity facility" or an "eligible servicer cash advance facility". All other off-balance-sheet securitization exposures will receive a 100% CCF.

Eligible liquidity facilities

578. Banking corporations are permitted to treat off-balance-sheet securitization exposures as eligible liquidity facilities if the following minimum requirements are satisfied:

(a) The facility documentation must clearly identify and limit the circumstances under which it may be drawn. Draws under the facility must be limited to the amount that is likely to be repaid fully from the liquidation of the underlying exposures and any seller-provided credit enhancements. In addition, the facility must not cover any losses incurred in the underlying pool of exposures prior to a draw, or be structured such that draw-down is certain (as indicated by regular or continuous draws);

(b) The facility must be subject to an asset quality test that precludes it from being drawn to cover credit risk exposures that are in default as defined in Sections 452–459. In addition, if the exposures that a liquidity facility is required to fund are externally rated securities, the facility can only be used to fund securities that are externally rated investment grade at the time of funding;

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

(d) Repayment of draws on the facility (i.e. assets acquired under a purchase agreement or loans made under a lending agreement) must not be subordinated to any interests of any note holder in the program (e.g. ABCP program) or subject to deferral or waiver.

579. Where these conditions are met, the banking corporation may apply a 50% CCF to the eligible liquidity facility regardless of the maturity of the facility. However, if an external rating of the facility itself is used for risk-weighting the facility, a 100% CCF must be applied.

Eligible liquidity facilities available only in the event of market disruption

580. Repealed.

Treatment of overlapping exposures

581. A banking corporation may provide several types of off-balance-sheet facilities (e.g. liquidity facilities or credit enhancements) that can be drawn under various conditions. The same banking corporation may be providing two or more of these facilities. Given the different triggers found in these facilities, it may be the case that a banking corporation provides duplicative coverage to the underlying exposures. In other words, the facilities provided by a banking corporation may overlap since a draw on one facility may preclude (in part) a draw under the other facility. In the case of overlapping facilities provided by the same banking corporation, the banking corporation does not need not to hold additional capital for the overlap. Rather, it is only required to hold capital once for the position covered by the overlapping facilities (whether they are liquidity facilities or credit enhancements). Where the overlapping facilities are subject to different conversion factors, the banking corporation must attribute the overlapping part to the facility with the highest conversion factor. However, if overlapping facilities are provided by different banking corporations, each banking corporation must hold capital for the maximum amount of the facility.

Eligible servicer cash advance facilities

582. A servicer cash advance facility, contractually provided for, will be eligible for a 0% CCF, provided all following conditions are met:
   (a) All conditions in Section 578 are fully met.
   (b) The facility may be unconditionally cancellable without prior notice.
   (c) The servicer is entitled to full reimbursement for advances drawn under the facility.
   (d) Reimbursements of amounts drawn under the facility are senior to other claims on cash flows from the securitized exposures.

(v) Treatment of credit risk mitigation for securitization exposures

583. The treatment below applies to a banking corporation that has obtained a credit-risk mitigant on a securitization exposure. Credit risk mitigants include guarantees, credit derivatives, collateral, and on-balance-sheet netting. Collateral in this context refers to that used to hedge the credit risk of a securitization exposure rather than the underlying exposures of the securitization transaction.

584. When a banking corporation other than the originator provides credit protection to a securitization exposure, it must calculate a capital requirement on the covered exposure as if it were an investor in that securitization. If a banking corporation provides protection to an unrated credit enhancement, it must treat the credit protection provided as if it were directly holding the unrated credit enhancement.

Collateral

585. Eligible collateral is limited to that recognized under the standardized approach for CRM (Sections 145 and 146 of Proper Conduct of Banking Business Directive number 203). Collateral pledged by SPEs may be recognized.

Guarantees and credit derivatives

586. Guarantees and credit derivatives provided by the entities listed in Section 195 of Proper Conduct of Banking Business Directive number 203 may be recognized. SPEs cannot be recognized as eligible guarantors.

587. Where guarantees or credit derivatives fulfill the minimum operational conditions as specified in Sections 189 to 194 of Proper Conduct of Banking Business number 203, banking corporations can take account of such credit protection in calculating capital requirements for securitization exposures.

588. Capital requirements for the guaranteed/protected portion will be calculated according to CRM for the standardized approach as specified in Sections 196 to 201.

Maturity mismatches

589. For the purpose of setting regulatory capital against a maturity mismatch, the capital requirement will be determined in accordance with Sections 202 to 205 of Proper Conduct of Banking Business Directive number 203. When the exposures being hedged have different maturities, the longest maturity must be used.

(vi) Capital requirement for early amortization provisions

Scope

590. As specified below, an originating banking corporation is required to hold capital against all or a portion of the investors' interest (i.e. against both the drawn and undrawn balances related to the securitized exposures) when:
   (a) It sells exposures into a structure that contains an early amortization feature; and
   (b) The exposures sold are of a revolving nature. These involve exposures where the borrower is permitted to vary the drawn amount and repayments within an agreed limit under a line of credit (e.g. credit card receivables and corporate loan commitments).

591. The capital requirement should reflect the type of mechanism through which an early amortization is triggered.

592. For securitization structures wherein the underlying pool comprises revolving and term exposures, a banking corporation must apply the relevant early amortization treatment (outlined below in Sections 594 to 605) to that portion of the underlying pool containing revolving exposures.

593. Banking corporations are not required to calculate capital requirements for early amortization in the following situations:

(a) Replenishment structures where the underlying exposures do not revolve and the early amortization ends the ability of the banking corporation to add new exposures;

(b) Transactions of revolving assets containing early amortization features that mimic term structures (i.e. where the risk on the underlying facilities does not return to the originating banking corporation);

(c) Structures where a banking corporation securitizes one or more credit line(s) and where investors remain fully exposed to future draws by borrowers even after an early amortization event has occurred;

(d) The early amortization clause is solely triggered by events not related to the performance of the securitized assets or the selling banking corporation, such as material changes in tax law or regulations.

Maximum capital requirement

594. For a banking corporation subject to the early amortization treatment, the total capital charge for all of its positions will be subject to a maximum capital requirement (i.e. a "cap") equal to the greater of (1) that required for retained securitization exposures, or (2) the capital requirement that would apply had the exposures not been securitized. In addition, banking corporations must deduct the entire amount of any gain-on-sale and credit enhancing I/Os arising from the securitization transactions in accordance with Sections 561 to 563.

Mechanism

595. The originator's capital charge for the investor’s interest is determined as the product of (a) the investor’s interest, (b) the appropriate CCF (as discussed below), and (c) the risk weight appropriate to the underlying exposure type, as if the exposures had not been securitized. As described below, the CCFs depend upon the whether the early amortization repays investors through a controlled or non-controlled mechanism. They also differ according to whether the securitized exposures are uncommitted retail credit lines (e.g. credit card receivables) or other credit lines (e.g., revolving corporate facilities). A line is considered uncommitted if it is unconditionally cancellable without prior notice.

(vii) Determination of CCFs for controlled early amortization features

596. An early-amortization feature is considered controlled when the definition specified in Section 548 is satisfied.

Uncommitted retail exposures

597. For uncommitted retail credit lines (e.g. credit card receivables) in securitization containing controlled early amortization features, banking corporations must compare the three-month average excess spread defined in Section 550 to the point at which the banking corporation is required to trap excess spread as economically required by the structure (i.e. the excess spread trapping point).

598. In cases where such a transaction does not require excess spread to be trapped, the trapping point is deemed to be 4.5 percentage points.

599. The banking corporation must divide the excess spread level (three-month average) by the transaction's excess spread trapping point to determine the appropriate segments and apply the corresponding conversion factors, as outlined in the following table:

Controlled early amortization features

<table>
<tr><th></th><th>Uncommitted</th><th>Committed</th></tr>
<tr><td rowspan="7">Retail credit lines</td><td>3-month average excess spread Credit Conversion Factor (CCF)</td><td rowspan="7">90% CCF</td></tr>
<tr><td>133.33% of trapping point or more—0% CCF</td></tr>
<tr><td>Less than 133.33% and more than 100% of trapping point—1% CCF</td></tr>
<tr><td>Less than 100% and more than 75% of trapping point—2% CCF</td></tr>
<tr><td>Less than 75% and more than 50% of trapping point—10% CCF</td></tr>
<tr><td>Less than 50% and more than 25% of trapping point—20% CCF</td></tr>
<tr><td>Less than 25%—40% CCF</td></tr>
<tr><td>Non-retail credit lines</td><td>90% CCF</td><td>90% CCF</td></tr>
</table>

600. Banking corporations are required to apply the conversion factors set out in the table above for controlled mechanisms to the investor's interest referred to in Section 595.

Other exposures

601. All other securitized revolving exposures (i.e. those that are committed and non-retail exposures) with controlled early amortization features will be subject to a CCF of 90% against the off-balance-sheet exposures.

(viii) Determination of CCFs for non-controlled early-amortization features

602. Early amortization features that do not satisfy the definition of controlled early amortization as specified in Section 548 will be considered non-controlled and treated as follows.

Uncommitted retail exposures

603. For uncommitted retail credit lines (e.g. credit-card receivables) in securitizations containing non-controlled early amortization features, banking corporations must make the comparison described in Sections 597 and 598.

604. The banking corporation must divide the excess spread level by the transaction's excess spread trapping point to determine the appropriate segments and apply the corresponding conversion factors, as outlined in the following table:

Non-controlled early amortization features

	Uncommitted	**Committed**
Retail credit lines	**3-month average excess spread Credit Conversion Factor (CCF)**	100% CCF
	133.33% of trapping point or more—0% CCF	
	Less than 133.33% and more than 100% of trapping point—5% CCF	
	Less than 100% and more than 75% of trapping point—15% CCF	
	Less than 75% and more than 50% of trapping point—50% CCF	
	Less than 50% of trapping point—100% CCF	
Non-retail credit lines	100% CCF	100% CCF

Other exposures

605. All other securitized revolving exposures (i.e. those that are committed and all non-retail exposures) with non-controlled early amortization features will be subject to a CCF of 100% against the off-balance-sheet exposures.

606–643. Repealed.[96]

[96] Repealed.