May 31, 2001

The Bank for International Settlements
Basel Committee on Banking Supervision
Centralbahnplatz.2
4022 Basel
Switzerland

Re: Consultative Document: The New Basel Capital Accord—Multi-Seller Conduit Comment 1

Ladies and Gentlemen:

The banking organizations listed on Schedule I (the "*Commenting Banks*" or "*we*") wish to thank the Basel Committee on Banking Supervision (the "*Committee*") for this opportunity to comment on its January 2001 Consultative Document (the "*Consultative Paper*") on the New Basel Capital Accord (the "*Accord"*). We are submitting our comments to the Consultative Paper in two separate letters. In this letter we comment on certain aspects of the Consultative Paper specified below that would affect the various Commenting Banks as a result of their participation in an important segment of the international capital markets: the asset-backed commercial paper ("*ABCP*") markets. In a second comment letter being submitted concurrently herewith, we comment on an internal ratings based approach ("*IRB")* and on the appropriate risk weights to be applied under both a standardized approach and under an IRB, in each case, to the extent applicable to the ABCP markets. Many of the Commenting Banks also intend to submit one or more additional comment letters addressing other aspects of the Consultative Paper.

Approximate overall outstandings in the international ABCP markets as of December 31, 2000 were $623.5 billion. Approximately $410.7 billion (66%) of that ABCP was issued by multi-seller ABCP programs ("*Multi-Seller Conduits*"). The table on the next page details outstandings as of September 30, 2000, the most recent date for which such detailed information has been published. Approximate overall outstandings in the international ABCP markets as of September 30, 2000 were $586.1 billion. Approximately $325.0 billion (55%) of that ABCP was issued by Multi-Seller Conduits. Of the overall outstandings of Multi-Seller Conduits in the ABCP markets, approximately $260.8 billion (80%) was issued by Multi-Seller Conduits administered by the Commenting Banks and their affiliates. The table on the next page shows outstanding ABCP as of September 30, 2000 issued by all Multi-Seller Conduits, broken out by the country where the administering bank's head office is located. While the Commenting Banks and their respective affiliates also account for a significant percentage of the other ABCP outstanding as well as term asset-backed securities issued by banks, this comment addresses only the potential impact of the ideas discussed in the Consultative Paper upon Multi-Seller Conduits and the banks that provide liquidity commitments and credit enhancement to them.

ABCP Market as of September 30, 2000

(1)	(2)	(3)	(4)
Country	Number of Commenting Banks domiciled in Country	ABCP Outstandings of Multi-Seller Conduits Administered by all Banks domiciled in Country (in billions)	ABCP Outstandings from Column (3) as a percentage of Overall Multi-Seller ABCP Outstandings
Canada	2	$ 35,819	11.00%
France	2	$ 13,773	4.20%
Germany	3	$ 40,458	12.40%
Japan	0	$ 11,322	3.50%
Netherlands	2	$ 36,420	11.20%
Switzerland	0	$ 6,249	1.90%
United Kingdom	1	$ 12,234	3.80%
United States	10	$166,300	51.20%
others	0	$ 2,397	0.70%

While we have appreciated the opportunity to work with staff as they draft proposals for the Committee's consideration, we do not believe that this adequately substitutes for a formal comment process on fully developed proposals. With outstandings of more than $600 billion, the ABCP market represents both a safe and profitable line of business for banks and an important financing option for corporate clients. If the final Accord were to require banks to hold more capital than warranted by the risk of positions in securitizations, not only would banks be put at a competitive disadvantage to unregulated institutions but corporate clients could lose access to this form of financing if the costs were to become prohibitive. Because of the importance of the ABCP market and potential ramifications posed by revisions to the Accord, we strongly urge the Committee to revise its time frame to allow a formal comment period on a fully developed IRB approach for securitizations.

Executive Summary

The Commenting Banks continue to support the Committee's goal of modifying capital requirements to better reflect the relative risk associated with various assets. In particular, we continue to support the adoption of a workable IRB approach to be implemented in the same time frame as an external ratings-based approach ("*ERB*").

In this comment letter, we will address two principal areas addressed in the Consultative Paper as they apply to banks' securitization activities, particularly their exposures to Multi-Seller Conduits: credit enhancements and liquidity commitments. Our comments on each are summarized below.

- *Treatment of Credit Enhancement.*

  Second Loss Credit Enhancement Positions

  - While we appreciate the Committee's inclusion of an approach for calculating the applicable risk weight for second loss credit enhancement by reference to the related underlying asset pools, we believe that an IRB approach should be available for these typically unrated positions.

  - If an IRB were unavailable to a bank for any reason, we believe that a bank should nevertheless be able to internally assign a rating to a second loss credit enhancement position using a qualified rating agency's methodology.

  - If no internal rating approach is available to a bank, we believe that the standardized approach should assign an unrated program credit enhancement position a risk weight based on the weighted average of the risk weights of the transactions that position supports.

  - We have the following comments related to how underlying positions are assigned risk weights in order to determine the risk weight for program credit enhancement under a standardized approach:

    - when assigning a risk weight to an unrated asset-backed position, a bank should be able to look-through to the risk weight of the asset pool supporting that asset-backed position, and
    - that unrated pools with corporate obligors should be assigned a 100% risk weight.

- As implied in the Consultative Paper, we seek clarification that seller-provided and other transaction level enhancement constitutes a first loss position.

First Loss Credit Enhancement Positions

- We believe that an IRB approach should be applicable to first loss credit enhancement positions in addition to second loss positions. We further believe that an IRB approach should be available to a bank in all circumstances, regardless of the role in which the bank is providing a credit enhancement position.

- If an IRB were unavailable to a bank for any reason, we believe that a bank should be able to internally assign a rating to a first loss credit enhancement position using a qualified rating agency's methodology.

- We believe that any potential deduction to capital for program credit enhancement positions provided by a sponsor that securitizes its own assets should only apply to the extent which that credit enhancement could be used to cover losses on that sponsor/originator's securitized assets.

- *Treatment of Liquidity Commitments.*

  - We support the continuation of the current method of calculating required capital for liquidity commitments which apply the conversion factor to the risk-weighted off-balance sheet item and we seek clarification that this is the Committee's intent.

  - We believe that an IRB approach should be available for liquidity commitments. If an IRB were unavailable to a bank for any reason, we believe that a bank should be able to internally assign a rating using a qualified rating agency's methodology.

  - We have two comments on the application of the "look through" approach proposed by the Committee for unrated securitization positions:

    - we believe that unrated pools with corporate obligors should be assigned a 100% risk weight, and
    - we believe that program liquidity commitments should be assigned a risk weight based on the long-term equivalent rating of the short-term rating on the ABCP issued by a conduit.

- Because of the low frequency of draws and low risk of default once drawn, as evidenced by the performance data discussed in *Section 2.B.*, we believe that the assignment of a 20% conversion factor for commitments of one year or less overstates the risk of these commitments and believe that a more appropriate conversion factor for these commitments is 10%.

- We believe that the presence of asset quality tests in liquidity commitments sufficiently safeguards these commitments from being used as credit enhancement and therefore believe that further criteria as proposed by the Committee for a commitment to be treated as liquidity would be inappropriate.

- We seek clarification as to the scope of the application of liquidity treatment rules to include comparable treatment for syndication banks that are not conduit sponsors and to include parallel purchase commitments, which are more fully described in *Section 2.D*.

Additionally, we are concerned that the proposed disclosure requirements are excessive when applied to Multi-Seller Conduits and believe that reporting requirements should be significantly limited.

Section 4 of this Comment Letter sets forth several additional comments on the Consultative Paper.

The remainder of this Multi-Seller Conduit Comment is organized as indicated in the following outline and discusses the Commenting Banks' key areas of concern in more detail.

1. Comments on Proposed Treatment of Credit Enhancement.

A. Treatment of Second Loss Program Enhancements that are not Externally Rated.

The Commenting Banks thank the Committee for including an approach for calculating the applicable risk weight for program credit enhancement by reference to the risk weights of the related underlying asset pools. We continue to believe that a full IRB is an appropriate and preferred method for establishing minimum capital levels.[1/] However, the approach that the Committee has proposed appropriately recognizes the substantial first loss protections enjoyed by most program credit enhancements and provides an acceptable interim alternative to an IRB for these exposures, subject to the following comments.

The approach proposed by the Committee may require a two-step look-through process:

- the risk weight of the second loss credit enhancement is determined by looking through to the underlying assets (we call this the "*program level look-through*"); and
- often those underlying assets will be unrated securitization positions, and their risk weights may (depending upon the Committee's reaction to our comments) be determined using the general look through treatment that the Committee has proposed for unrated positions (we call this the "*transaction level look-through*").

We have comments about both of these look-through steps. These comments will be easier to communicate with the aid of an example. Please assume that a new multi-seller conduit has just two transactions:

- The first transaction is a $90 million senior interest in a $100 million pool of business-to-business trade receivables (with corporate obligors). The remaining $10 million is a first loss subordinated position retained by the conduit's customer.

[1/] While we believe that the Committee's intent to permit an IRB approach for assigning risk weights to unrated program credit enhancement positions is implicit in the specifics of the January proposal, we note that the discussion of IRBs in the Consultative Document on Asset Securitization (the "*Securitization Paper*") does not specifically mention banks in their role as program credit enhancement providers. We believe the final Accord should make this point clear.

- The second transaction is a $90 million A-rated Class B asset-backed security which was issued as part of a series that included Class C securities that are subordinated to the Class B security and Class A securities that are senior to the Class B security.

- The conduit's sponsor provides a program level letter of credit that can be drawn upon to support such conduit's ABCP if losses on any of the conduit's transactions exceed the applicable first loss protections. In the case of the first transaction described above, the program letter of credit would be drawn if losses on the underlying pool exceeded $10 million. In the case of the second transaction, the program letter of credit would be drawn upon to support such conduit's ABCP if losses on the underlying pool exceeded the amount of the subordinated Class C securities (and any other amounts available to cover losses before impairment of the Class B securities).

First Comment. As to the program level look-through, we believe that even before a sponsor bank qualifies for a true IRB, the sponsor should be permitted to generate internal ratings of unrated conduit positions by following published rating agency criteria. So long as banks are able to input certain key factors that are typically developed as part of the structuring process but are not necessarily fixed model inputs (*e.g.* discounts associated with maturity mismatches between the life of the vehicle and the life of the underlying pool), we believe this could be a reasonable approach that would be manageable from an implementation standpoint. These internally generated ratings should then be used to assign the various positions to the risk weights corresponding to an identical external rating.

In the example described above, the sponsor should be able to apply rating agency criteria to determine a rating for the $90 million unrated senior interest. If the rating so determined was BBB, then the program letter of credit would have two underlying assets: one internally rated BBB and one externally rated A.

Second Comment. Also with respect to the program level look-through, rather than assigning a risk weight to a second loss credit enhancement based upon the highest risk weight of any underlying asset, we believe that it is more appropriate to assign a risk weight that equals the weighted average of the underlying risk weights, as this better reflects the risk of that pool.

In the example described above, we believe the appropriate risk weight for the second loss enhancement would be 75%, since one-half of the underlying assets have an external rating of A and thus a risk weight of 50%, while the other half of the underlying assets have an internal rating of BBB and thus a risk weight of 100%.

Third Comment. If the Committee does not accept our first comment above, then the Committee's proposal will only be practicable if transaction level look-throughs are permitted for unrated asset-backed positions that are covered by the second loss enhancement that is under consideration. The Consultative Paper did not expressly state that transaction-level look-throughs are permitted, and we request that the Accord remedy that omission.

In the example above, if the Committee did not permit the sponsoring bank to use an internally derived rating on the $90 million unrated senior interest, then the sponsoring bank would need to apply a transaction level look-through to that transaction.

Fourth Comment. Also with respect to the transaction level look-through, when the underlying assets are exposures to corporate obligors, we believe a 100% risk weight should be applied to the pool. Credit and risk analysis is done at the pool level as opposed to the individual obligor level in securitizations. Essentially, the unrated corporate risk in a securitization is that of the pool. Therefore, we believe that the 100% risk weight for unrated corporate exposures should be assigned to the pool. Additionally, we believe this limitation is appropriate because virtually all conduit transactions are structured to an investment grade level in order to maintain the rating of a conduit's ABCP, and 100% is the highest risk weight category applied to investment grade corporate positions.[2/]

In the example above, the sponsoring bank should be permitted to assign a 100% risk weight to the $90 million senior position, rather than having to determine risk weights for each and every underlying corporate obligor.

Fifth Comment. Finally, although we think it is clear that the Committee considered seller-provided and other transaction level enhancement to count as a first loss position in determining whether an enhancement provided by a conduit sponsor is in a second loss position,[3/] some readers have been uncertain about this. We would appreciate a clear statement to this effect in the final Accord.

B. Treatment of First Loss Program Enhancements.

We do not believe that an automatic deduction from capital is appropriate for first loss positions provided by sponsor banks. Rather, we believe that the minimum capital requirements for first loss credit enhancement positions provided by conduit sponsors should be established based on the credit quality of those positions, not on the fact they are being provided by a bank as a conduit sponsor. Furthermore, we do not see any reason to treat sponsor-provided first loss

---

[2/] This same methodology should also be available for exposures to sovereigns and banks (*i.e.* the risk weight applicable at the investment grade level for those types of exposures should be applied pools consisting of those exposures).

[3/] See in particular the discussion set forth in paragraphs 39 through 42 of the Securitization Paper.

positions differently than first loss positions provided by investors or, for that matter, originators.[4/]

We believe that if a first loss position is rated by an external rating agency, the ERB should apply. If a position is not rated, but a bank is qualified for the IRB approach, its internal rating of the position should apply. If the Committee were not willing to allow a full IRB approach for first loss positions, we believe that the final Accord should permit a bank to use the methodology of a qualifying external rating agency to internally determine the applicable rating for a first loss position. Finally, we believe, at a minimum, the "look through" approach available for investors providing credit enhancement should also be available as an alternative for sponsor banks providing first loss credit enhancement.

First, linking the capital requirements to the credit risk of a position under an ERB or IRB approach directly serves the goal of aligning required capital to actual risk. While the role a bank plays in providing credit enhancement may raise other areas of concern for regulators (*e.g.* the reputation risk for an originator in a transaction or the ability of a investor to conduct adequate due diligence of the underlying assets), we do not believe these additional concerns in any way change the fundamental proposition that the risk of the underlying position remains the same no matter who provides that position.

We believe that other areas of the regulatory framework provide safeguards to address non-credit related risk. For instance, were an originator to provide implicit recourse to prevent a transaction from defaulting, a regulator would have the ability to require that originator to return some or all securitized assets to its risk-based capital calculation. Prior to applying an IRB, a bank will be required to satisfy its regulators that its internal ratings system is sufficiently developed to assess the risks of potential investments. We believe that regulatory tools such as these are the more appropriate means of addressing additional "role" risks.

Second, we do not believe that the integrity of the capital system will be compromised by allowing reliance on an ERB or an IRB for the calculation of required capital for first loss credit enhancement positions. Under either approach, regulators must approve the entity that will be rating a particular position prior to that entity's being permitted to calculate the credit risk of that position. Furthermore, regulators will have the ability to satisfy themselves of the continued integrity of the system through supervisory review.

Third, we believe both rating agencies and banks take into account the relative subordination of a position when assigning a rating to that position. Thus, the increased risk of a

---

[4/] Although we are not directly commenting on the treatment of credit enhancement provided by investors and originators, we concur with the comments on these proposals set forth in the comment letter submitted by the MBS/ABS Capital Adequacy Task Force of the Bond Market Association (the "*BMA Comment*").

first loss position will be reflected in the rating assigned to that position. We therefore do not believe that the level of subordination of a position should serve as an additional distinction for determining regulatory capital as it will be addressed in the ratings assigned to that position.

For these reasons, we believe that if a position is rated by an external rating agency, the capital requirement should be derived from the standard risk weights assigned in the ERB. If a position is not rated, but a bank is qualified for the IRB approach, its internal rating of the position should apply.

If the Committee were not willing to allow a full IRB approach, we also propose an alternative that would allow a bank to use a qualified external rating agency's methodology to internally assign a rating to a first loss position which would be used to determine the required capital under the standardized approach. Most first loss positions are not assigned a rating by an external rating agency. Thus, to avoid higher capital requirements if an IRB approach were not permitted, a bank would have to incur additional costs and delays to have its first loss positions externally rated. We do not feel that such costs or delays need to be incurred if a bank itself is willing to apply an external rating agency's methodology to determine an assigned rating. We feel that there would be sufficient protection to the system provided through regulatory review of the proper application of this methodology by a bank's supervisors.

Additionally, we believe, at a minimum, the "look through" approach available for investors providing credit enhancement should also be available as an alternative for sponsor banks providing first loss credit enhancement.

C. Treatment of Sponsor Putting its own Assets into a Conduit.

While we agree that a sponsor assumes the role of originator when it transfers its own assets into a conduit sponsored by it, we do not believe that the role in which a bank provides a credit enhancement position should affect the required capital for that position as it does not affect the risk of that position. Therefore, for the same reasons discussed in *Section B* above, we believe that sponsor/originator's should not be required to automatically deduct from capital credit enhancement positions related to securitizations of its own assets. Instead we believe both an ERB and IRB approach should be fully applicable to these positions.[5/]

If the Committee were to reject this position, we believe that the final Accord should clarify that a sponsor/originator should only be required to deduct from capital that portion of credit enhancement that is available to cover losses on assets securitized by it. This would, of

---

[5/] We acknowledge that to the extent new assets are created in connection with a securitization of our own assets, we should be required to hold capital against these new assets. We concur with the comments set forth in Section 2.2.2 of the BMA Comment Letter as to how to calculate this additional capital requirement.

course, include any retained interest in the assets and any other transaction-specific credit enhancement positions of the sponsor/originator. We want to emphasize, however, that it should not include all program credit enhancement provided to the conduit by the sponsor. Rating agencies that rate the ABCP of the Multi-Seller Conduit will require that originator/sponsor securitizations be structured to the same ratings level as all other transactions in the Multi-Seller Conduit. Therefore, because a program credit enhancement provider will have the same benefit of this first loss protection in a securitization of its own assets as with any other transaction, we do not believe that the treatment of program enhancement should be affected by the fact that the sponsor has put its own assets into the conduit. If the Committee disagrees, we believe that the deduction from capital should only relate to that portion of the program credit enhancement available to be drawn for losses on the sponsor/originator's securitized assets. For instance, if the sponsor provides a $10 million letter of credit as program enhancement but only $1 million could be applied to cover losses on its securitized assets, we believe that only $1 million should be deducted from capital. The balance should continue to be treated as though the sponsor had not securitized its own assets.

2. Comments on Proposed Treatment of Liquidity Commitments.

A. Calculation of Required Capital for Liquidity Commitments.

We have several comments relating to the calculation of required capital for liquidity commitments. First, we support the continuation of the current method of calculating required capital for liquidity commitments under which the credit equivalent amounts of off-balance sheet items are multiplied by their applicable risk weight before the application of the related conversion factor. Second, we believe that an IRB approach should be available when determining the risk weight for the applicable off-balance sheet item. Finally, we have three comments on the application of the "look through" approach proposed by the Committee for unrated securitization positions. First, rather than assigning a risk weight based on the highest risk weight of an obligor in a pool, we believe that it is more appropriate to assign a risk weight that equals the weighted average of the underlying risk weights. Second, we believe that a 100% risk weight should be applied for a pool of assets with corporate obligors. Third, we believe that program liquidity commitments should be assigned a risk weight based on the long-term equivalent rating of the short-term rating on the ABCP issued by a conduit.

Under the current accord, the credit equivalent amounts of off-balance sheet items are multiplied by the applicable risk weight in determining the minimum capital associated with the off-balance sheet item. For example, assume a 2-year commitment to make loans aggregating up to $1,000 to an OECD bank. Under the current regulatory scheme, the capital requirement calculation would be 50% x 20% x 8% x $1,000 = $8.00 (credit conversion factor x risk weight x minimum capital requirement x stated commitment). Although the Securitization Paper implies

the continuation of this approach,[6/] some readers have been uncertain as to whether the Committee is proposing to eliminate the risk weight factor from this calculation. If this were the case, using the same assumed commitment discussed above, the capital requirement calculation would be 50% x 8% x $1000 = $40.00 (credit conversion factor x minimum capital requirement x stated commitment).

The Commenting Banks strongly believe that the regulatory capital requirement for commitments must continue to take into consideration both the likelihood of draw under a commitment (the conversion factor) and the risk of default if drawn (the risk weight). Assume a 1-year commitment to a Multi-Seller Conduit to fund $1000. Further assume that this commitment relates to an asset pool that is rated AAA. The on-balance sheet position of this commitment would be assigned a risk weight of 20% under the proposed rules. Therefore, the regulatory capital requirement calculation for the unfunded commitment under the Committee's proposal would be 20% x 20% x 8% x $1000 = $3.20 (conversion factor x risk weight x minimum capital requirement x stated commitment). Assuming the Committee accepts our proposed 10% conversion factor discussed in *Section 2.B.* below, under the Commenting Bank's proposal this calculation would be 10% x 20% x 8% x $1000=$1.60.

Eliminating the risk weight factor from the calculation for regulatory capital for commitments eliminates the mechanism for assessing the underlying credit risk of loss to a bank associated with funding a liquidity commitment to a Multi-Seller Conduit. This results in a regulatory capital requirement that could be significantly higher than the overall risk of the bank's position, for positions rated A- or above, and significantly lower than the overall risk of the bank's position, for positions rated BB+ and below. Either result moves the regulatory system in the opposite direction from its stated goal of aligning minimum capital with the risk of a position.

Finally, we believe that an IRB approach should be available for determining required capital for liquidity commitments. If a full IRB approach is not available to a bank for any reason, then a two-step look-through process should apply, similar to the one described above for second loss credit enhancements:

- the risk weight of the liquidity is determined by looking through to the underlying conduit position(s) (the "*liquidity level look-through*"); and

---

[6/] For instance, paragraph 55 of the Asset Securitization Paper says that liquidity enhancements may be "converted at 20% and **generally** risk-weighted at 100%." (emphasis added). The use of the term "generally" clearly implies that sometimes these commitments would not be risk-weighted at 100%. The only reason we can see why that would happen is because the risk-weighting on the underlying assets would apply.

- often the underlying conduit position(s) will be unrated securitization positions, and their risk weights may (depending upon the Committee's reaction to our comments) be determined using the general look through treatment that the Committee has proposed for unrated positions (the "*asset level look-through*").

As with second loss program credit enhancements, we believe that:

- Even before a sponsor bank qualifies for a true IRB, the sponsor should be permitted to generate internal ratings of unrated conduit positions by following published rating agency criteria, and these internally generated ratings should be used to assign positions to the risk weights corresponding to an identical external rating.

- If the Committee does not accept the recommendation immediately above, then the Committee should permit asset level look-throughs, and when the underlying assets are exposures to corporate obligors, a general 100% risk weight should be applied to the pool.

Finally, we would suggest the following modification to the look through approach when used to determine the appropriate risk weight for a program liquidity facility. One requirement for a commitment to be treated as a liquidity commitment under the proposed Accord is that the facility is not subordinate to the interests of the ABCP holders—in other words, its interest must at least be a *pari passu* interest. Because the credit risk for both rated and unrated positions that are *pari passu* is identical, we believe that the unrated program liquidity facility should be "deemed" to have the same risk weight applicable to the long-term equivalent rating of the short-term rating on the ABCP for purposes of calculating required capital.[7/]

B. Appropriate Conversion Factor for Commitments

For reasons discussed below, the Commenting Banks believe that the assignment of a 20% conversion factor for Short Term Commitments overstates the risk of these commitments and believe that a more appropriate conversion factor for Short Term Commitments would be

---

[7/] We acknowledge that the rating of the ABCP is in part based on the availability of the liquidity commitment to cover market disruptions and payment mismatches. However, the presence of asset quality tests in the liquidity commitments will limit their availability to being drawn only when sufficient performing assets are available to back their funding. Therefore, although a liquidity commitment bears ABCP market disruption risk and cash flow mismatch risk, it does not bear the risk of providing credit enhancement to support the ABCP. The credit risk of both positions, once drawn, is the same.

10%. [8/] While the Commenting Banks feel that a 20% conversion factor is too high for even corporate exposures, we particularly feel that the structure and purpose of liquidity commitments to Multi-Seller Conduits reduce substantially the risk that these commitments will actually be drawn in a particular transaction. In particular, asset-quality tests built into liquidity commitments and structural components of related underlying securitization transactions serve to protect commitments from funding against non-performing assets. Thus, the risk of exposure of a commitment is effectively reduced to the extent that the underlying assets default. In the unlikely event that a commitment to a Multi-Seller Conduit is ever drawn, the funded commitment would be generally supported by performing assets. Additionally, at the time of draw, capital would be maintained against the amount of the drawn commitment.

First, liquidity commitments[9/] are unlikely to be drawn in the ordinary course as they are back-up funding sources for the highly stable ABCP market, which is the primary funding source for Multi-Seller Conduit transactions. Because the ABCP market has historically been very stable, the likelihood of draws under an outstanding liquidity commitment to address market disruptions is minimal. Even in the turbulent capital market conditions in the fourth quarter of 1998 and the period of investor concerns over potential Year 2000 issues, the Commenting Banks are not aware of any draws on liquidity commitments to Multi-Seller Conduits due to market disruption or general inability to access the ABCP market even when some highly rated corporate borrowers were unable to access the corporate commercial paper market.

Additionally, liquidity commitments are not generally susceptible to draws for economic reasons when commercial paper rates spike as the conduit administrator, not the customer, determines when to draw on liquidity commitments in accordance with the terms of a transaction. Because increased commercial paper costs are generally passed through to the customer, the conduit administrator, who is also typically a liquidity provider, does not have the same incentive that a customer would to fund through the liquidity commitment. Because customers are typically charged an increased margin for fundings under a liquidity facility, this option represents an unattractive funding source which, if utilized by a bank, would likely cause a client to seek alternative forms of financing.

Second, Multi-Seller Conduit transactions have structural features designed to allow an administering bank to maintain the stability of a receivables pool and mitigate the effect of defaults. These structural features include frequent pool reporting requirements, amortization triggers for revolving facilities that permit the liquidation of a receivables pool once it fails to meet specified performance requirements, audit mechanisms that allow an administering bank to

---

[8/] We are not commenting on the conversion factor for commitments of longer than a year in this paper.

[9/] References to "liquidity commitments" in this section should be interpreted to apply equally to "parallel purchase commitments" discussed more fully in *Section 2.C.* below.

inspect its customer's operations and ensure proper servicing of the receivables pool and the ability when warranted of an administrator to take control of payment systems to provide for direct payments to the Multi-Seller Conduit, alleviating bankruptcy and fraud risk of its customers.

Third, liquidity commitments to Multi-Seller Conduits employ asset-quality tests designed to ensure that the level of an outstanding commitment at any time does not exceed the availability of performing assets. Such tests typically involve a comparison of the level of commitment to all or a specified percentage of the dollar amount of eligible non-defaulted receivables and cash proceeds balances. As defaults on a receivables pool increase, the availability under the committed facility decreases. In essence, these commitments are based on the quality of the underlying assets and effectively reduce the risk exposure of a commitment to the extent that they relate to the non-performing portion of the related pool.

Fourth, the credit quality of the assets that would actually be funded under a draw on a liquidity commitment is enhanced by the diversity and isolation of the underlying receivables pools. If called upon to fund a commitment to a Multi-Seller Conduit, repayment to a bank will be made from payments on a pool of receivables with a number of obligors, concentrations of which are typically limited in a given pool. Thus the deterioration of the credit quality of any one obligor typically has a minimal impact on the credit quality of the related receivables pool. Banks are also generally isolated from the credit risk related to the originator of receivables by their transfer to a bankruptcy-remote entity prior to funding through the Multi-Seller Conduit. Furthermore, because the underlying receivables pools often liquidate quickly, the length of exposure to any one obligor is often minimal. Although we understand from discussions with staff that they are concerned about the presence of greater systemic risk in securitization positions, we agree with the BMA Comment Letter in that credit enhancement is sized to absorb any potential increased systemic risk.[10/]

Fifth, liquidity commitments in Multi-Seller Conduits have the benefit of the first loss position provided at the customer level. Credit enhancement is sized to absorb losses in securitization transactions. Even under a new regulatory capital scheme, banks will continue to hold capital against program credit enhancement (whether funded or unfunded) at the required risk weight. Thus capital is already being maintained in the system for the credit risk of securitization transactions.

Finally, a distinction between commitments generally (including back-up commitments for corporate commercial paper back-up lines) and pure ABCP liquidity commitments is also supported by differences in the relationship between the amount of the commitment and the related outstanding commercial paper. Corporate back-up lines are not required to cover 100% of the corporate's outstanding commercial paper, but ABCP liquidity commitments are required to

---

10/ See section 3.1 of the BMA Comment for further clarification on this point.

cover at least 100% of the related ABCP. As a result, in the unusual circumstance where an ABCP liquidity commitment is drawn, the amount drawn is likely to be a smaller percentage of the commitment than is the case for corporate back-up lines.

The utilization history of liquidity commitments (including parallel purchase commitments) of the Multi-Seller Conduits administered by the Commenting Banks supports the argument in favor of a continued exemption from capital requirements for Short Term Commitments. While preparing this comment letter, 19 of 20 Commenting Banks[11/], which administer 60 Multi-Seller Conduits, responded to a survey by Mayer, Brown & Platt of liquidity commitment utilization by their Multi-Seller Conduits. Results of our survey are set forth below:

- Multi-Seller Conduits for which information was reported have been in operation for periods ranging from 0.5 years to 18 years, with the mean period of operation being 8.4 years.

- These Multi-Seller Conduits have funded securitization transactions with an aggregate principal balance of $652.1 billion.

- For all transactions, only 43 liquidity draws have been made, for an aggregate amount of $5.282 billion.

- The aggregate amount of drawn commitments represented 0.81% of the aggregate amount of funding for the receivables pools.

- The mean ratio of aggregate draws to total originations for a Commenting Bank was 0.60%. Only 5 Commenting Banks had a draw ratio higher than the average. The highest draw ratio was 1.87%. 6 Commenting Banks have experienced no liquidity draws for conduits they administer, making a zero draw experience the mode of our study. The median draw ratio was 0.21%. The standard deviation on the draw rates was 1.09%.

- Only $206 million in losses have been experienced on liquidity draws in transactions for which the Commenting Banks act as sponsor of a Multi-Seller Conduit, representing less than 0.03% of all originations.

Because of their short term and structural features that effectively reduce the credit risk and risk of draw under these commitments, as supported by the historical draw information presented above, the Commenting Banks believe that the assignment of a 20% conversion factor

---

[11/] One Commenting Bank, while active in the ABCP markets, does not administer any Multi-Seller Conduits.

for Short Term Commitments overstates the risk of these commitments and believe that a more appropriate conversion factor for Short Term Commitments would be 10%.

C. Draw Limitation Requirement for Liquidity Commitments.

The Commenting Banks believe that the requirements limiting the circumstances under which a commitment can be drawn that are set forth clause (d) of paragraph 54 of the Securitization Paper are unnecessary and sufficiently vague as to cause confusion and should be eliminated. Despite making this comment, we want to make clear that we support what we believe to be the intent behind the inclusion of this provision—that there should be a distinction between liquidity, on the one hand, and credit enhancement and direct credit substitutes, on the other hand.

First, we would appreciate if the final Accord would clarify that the limitation that a facility "not act as a permanent revolving facility" is not meant to preclude liquidity treatment for Short Term Commitments that are renewed annually. We believe that so long as this commitment is subject to full credit review prior to annual renewal, it would be inappropriate to consider it a "permanent revolving facility". The fact that one or even multiple renewal requests are granted does not mean that anything less than a full credit review was done prior to such renewal. Nor does that fact suggest that the next such request will automatically be granted. In fact, banks do refuse to extend their liquidity commitments from time to time. As the Committee acknowledges in paragraph 47 of the Securitization Paper, a commitment of one year or less, as opposed to a longer term commitment, genuinely reduces a bank's potential credit risk by reducing the duration of its commitment. At a minimum, if a regulator does not feel that a bank is conducting an appropriate annual review of the credit risk of a commitment, the end result should be that the commitment be treated as a long term commitment not as credit enhancement, as paragraph 54 of the Securitization Paper could be read to suggest.

Second, we are also concerned that the draw limitation requirement could be interpreted to mean that only commitments that permit a draw in the event of a general ABCP market disruption could be considered liquidity commitments. We do not think that would be an appropriate interpretation. Rather, we believe that commitments so limited could be considered unconditionally cancellable as the Committee suggests in paragraph 46 of the Securitization Paper, thus theoretically qualifying for a 0% conversion factor. Thus, any draw limitation requirement for liquidity commitments must be broader than this limited circumstance but narrow enough to distinguish between liquidity, on the one hand, and credit enhancement, on the other hand. We believe that the appropriate distinguishing limitation is the presence of a reasonable asset quality test that assures against drawing funding against bad or deteriorating assets as specified in clause (f) of paragraph 54 of the Securitization Paper.

We note that there are a number of reasons for drawing on a liquidity commitment that are not related to pool performance issues which should not cause the ineligibility of a commitment as liquidity. These include conduit management, administrative convenience and

client and investor relationship issues, including permitting temporary funding to cover small exposures, providing short term (typically one day) swingline funding for exposures, and permitting reallocation of commercial paper maturities.

Also, we believe that any limitations on draws beyond the asset quality test limitation unfairly discriminate against asset-backed liquidity commitments. First, so long as a liquidity commitment does not provide credit enhancement, it is, generally speaking, the functional equivalent of a corporate back stop facility. We note that there are no comparable criteria for usage of corporate commercial paper back stop facilities. Second, given that corporate back stop facilities have a higher historical draw rate than conduit liquidity facilities, we do not understand the more restrictive criteria proposed for liquidity commitments. We note that regulators will continue to have the ability to require greater capital to be held for those commitments that they view to be disguised credit enhancement.

For these reasons, we believe that the requirements limiting the circumstances under which a facility may be drawn and requiring that a facility may not act as permanent revolving funding more fully specified in clause (d) of paragraph 54 of the Securitization Paper should be eliminated from the proposed rules governing the characterization of a commitment as liquidity.

D. Scope of Treatment for Liquidity Commitments.

The Commenting Banks would like to have the scope of treatment for liquidity commitments clarified in two respects in the final Accord. First, we note that the discussion of liquidity commitments in the Consultative Document occurs solely in the context of commitments of a bank as a conduit sponsor. As a matter of course, a portion of a liquidity commitment for a particular transaction may be syndicated to several banks other than the conduit sponsor. To avoid any confusion as to the scope of the application of the rules governing liquidity commitments, we believe that the final Accord should make clear that liquidity treatment applies to all banks providing liquidity to a conduit.

Second, it is also a common market practice that a bank providing a liquidity commitment for a particular transaction enter into two interrelated commitments. The first commitment is the liquidity commitment as contemplated in the Consultative Paper. The second commitment is an equal parallel commitment that runs directly to the transferor of the assets into the conduit. The parallel commitment is entered into so that the conduit itself does not have to make a commitment to fund additional purchases of assets from time to time in a particular transaction. Instead, it is given the option to have the liquidity provider fund those draws directly.

The inclusion of a parallel commitment allows a conduit to do directly (fund through a liquidity provider) what it otherwise would do indirectly (draw on liquidity). The decision as to whether to fund through liquidity or a conduit is generally at the conduit's discretion, not the

client's. Further, like a liquidity commitment, a parallel purchase commitment will fund only against performing assets and will represent a *pari passu* interest with liquidity draws on the cash flows from a particular transaction. Finally, to the extent that a bank's liquidity commitment is drawn, the availability under the parallel commitment is correspondingly reduced. Functionally, the dual liquidity/parallel commitment is essentially one commitment to a transaction that can be drawn in two different ways. We believe that the final Accord should make clear that (x) liquidity treatment applies to parallel purchase commitments that function in the same way as liquidity commitments and (y) a bank need only hold capital against the stated amount of the liquidity commitment since at no time does available commitment amount under these related commitments exceed the stated amount of the liquidity commitment.

3. Proposed Disclosure Requirements.

We read the Consultative Document's disclosure requirements for SPVs as potentially applying to Multi-Seller Conduits. If this is the intent of the Committee, we feel strongly that the level of detail not only greatly exceeds that which is necessary to assure transparency or currently required by the market, but also could serve to overshadow the material information relevant to investors in ABCP. Overall parameters, such as credit and investment criteria and structure requirements for transactions done in a conduit are the relevant material disclosure for ABCP investors. The sheer volume of material that would be generated with the level of deal-by-deal disclosure proposed could actually serve to reduce rather than increase transparency. Furthermore, we feel that current bank and securities regulations, accounting and other required disclosures provide investors and other interested parties with all material information on the activities of a Multi-Seller Conduit. Finally, we note that Multi-Seller Conduits function like a bank or other lending institution that provides funding to a number of customers. We believe that more general disclosure such as that required for a bank is therefore more appropriate than the specific disclosure required for a particular originating entity.

4. Additional Comments

A. Proposed "Clean Break" Requirements

While we agree with the proposition that there must be a "clean break" between an originator and securitized assets before an originating bank can remove these assets from the calculation of its risk-based capital ratio, we agree with the comments on this issue set forth in *Section 2.1* of the BMA Comment seeking clarification on several points in the Accord's "clean break"requirements.

B. Time frame for Adoption of Final Accord

First, we would like to commend the Committee and the staff for the time and effort that went into delivering the Consultative Document and accompanying papers—we recognize the tremendous effort involved in moving the regulatory system toward the stated goals of the

Commission. Second, we are extremely grateful for the opportunity to work directly with staff members in developing an IRB approach for asset securitizations.

Despite everyone's continued efforts, we believe that the current December deadline actually threatens to hinder the finalization of proposed capital regulations for asset securitizations, most particularly the finalization of a workable IRB. Under the current time frame, members of the staff were forced to publish an incomplete proposal in the Consultative Document for comment. At the same time that industry participants and other interested parties are considering and commenting on these proposals, we understand that revised drafts are being prepared by the staff for submission to the Committee shortly after the comment submission deadline. We quite frankly do not see any time in the proposed schedule for the staff to review and incorporate, as applicable, formal comments submitted on the Consultative Document. Further, we see no provision that would provide us with a revised final proposal with sufficient time to analyze that proposal and comment on it. While we appreciate the opportunity to work with the staff as they further develop proposals, we do not believe that this adequately substitutes for a formal comment process. We feel that the December deadline must be set aside and that the Committee and staff need to look forward at what time is needed to publish a fully developed proposal and allow time for thoughtful analysis and input from industry participants and set a goal for adoption based on this time frame. While this process may delay the adoption of a revised Accord, we actually believe that it will speed up the development and finalization of the rules to be included in that Accord.

C. Transition Period upon Adoption of Final Accord

The Commenting Banks believe that the Accord should require a minimum two-year transition period from the date that an individual country adopts regulations based on the final Accord until those revised regulations become effective. Banks will need this amount of time to review and revise transaction structures to the extent required by changes in regulations. Further, both banks and regulators will need time to have their internal systems approved for an IRB approach. It will be important for banks to be able to qualify for at least the foundation IRB approach upon effectiveness of revised regulations so as not to be put at a competitive disadvantage against non-bank credit providers.

D. No Deferral of Liquidity Fees for Liquidity Commitments.

We do not feel that the inclusion of a provision in a liquidity facility that a conduit is only obligated to make payments thereunder, including payments of fees to liquidity banks, to the extent it has cashflows available should be considered a "deferral" of such fees, thus causing that facility not to meet the criteria set forth in clause (e) of paragraph 54 of the Securitization Paper. The provision is meant to clarify the structured nature of a conduit, in that its creditors are relying on the cash flows from the asset interests held by the conduit, and to preserve the bankruptcy remoteness required for maintaining the rating on its ABCP. We would appreciate clarification on this point in the final Accord.

5. Conclusion.

The Commenting Banks support the Committee's continuing efforts to modify capital requirements to truly reflect the relative risk associated with various assets. We look forward to continuing to work with the Committee and its staff on the proposals set forth in the Consultative Document. We believe that our continuing dialogue will result in regulatory requirements that provide for the maintenance of prudent levels of capital without disadvantaging banks in the fiercely competitive global capital markets.

With your permission, we would appreciate the opportunity to add to the institutions included as Commenting Banks as additional institutions have an opportunity to obtain internal approval for support of the positions discussed in this letter.

* * *

Respectfully submitted.

Schedule 1

List of Commenting Banks

ABN AMRO BANK N.V.
BANK OF AMERICA, NATIONAL ASSOCIATION
BANK OF MONTREAL
BANK ONE CORPORATION
BARCLAYS BANK PLC
BNP PARIBAS
CIBC WORLD MARKETS CORP.
CITIBANK, N.A.
COMMERZBANK AG
DRESDNER BANK AG
FIRST UNION NATIONAL BANK
FLEET NATIONAL BANK
JP MORGAN CHASE & CO.
MBNA AMERICA BANK, NA
PNC BANK, NATIONAL ASSOCIATION
RABOBANK NEDERLAND
SOCIÉTÉ GÉNÉRALE
STATE STREET CAPITAL MARKETS, LLC
WACHOVIA BANK, N.A.
WESTDEUTSCHE LANDESBANK GIROZENTRALE