



Advisory

Subject: Capital Treatment of Asset-Backed Commercial Paper
Conduit Programs

Category: Capital

Date: December 2004

This Advisory sets out the capital treatment for asset-backed commercial paper (ABCP) conduit programs that are consolidated as a result of the implementation by the Accounting Standards Board of Accounting Guideline 15 - *Consolidation of Variable Interest Entities* (AcG-15). This Advisory is effective from November 1, 2004 and is applicable to banks. It complements OSFI guidelines:

- [B-5 - Asset Securitization \(revised November 2004\)](#), and
- [D-8 - Accounting for Transfers of Receivables Including Securitizations](#).

The treatment is effective from November 1, 2004 through April 31, 2005 (**Note: extension of Advisory to October 31, 2005**), at which time OSFI will re-evaluate its position taking into account developments in the industry, the status of restructuring efforts by conduit sponsors and rulings from the accounting standard setters and auditors.

AcG-15, which is effective for fiscal years beginning on or after November 1, 2004, requires the consolidation of particular variable interest entities (VIEs) by the organization identified as the primary beneficiary. In many instances, this may result in banks' consolidating ABCP conduits (third-party asset structures) that previously were not consolidated.

While the accounting treatment has changed, the risks to the bank have not. In particular, risks are limited by operational controls placed on the conduit structures, legal agreements within the transaction, and the selling of positions to third parties. As a result, OSFI will assign a zero per cent risk weight to consolidated third-party assets from ABCP conduits that previously had not been on the institution's balance sheet or would not be in the absence of AcG-15. This risk-weight applies to conduits that contain only third-party assets.

OSFI will require that capital be held against securitization exposures such as first loss facilities, credit enhancements, liquidity facilities and investments in issued securities that are eliminated on consolidation.

This Advisory does not change the balance sheet presentation for an institution, which should be produced in accordance with Canadian Generally Accepted Accounting Principles (GAAP). The assets-to-capital multiple calculation remains unchanged. It will continue to use balance sheet asset as calculated by GAAP.

OSFI encourages banks to work with their auditors and to restructure conduit structures as required to ensure that the accounting for these structures meets GAAP and reflects their true risk. Many institutions in Canada and the United States have successfully restructured their ABCP conduits to comply with the accounting standards.

Banks should report consolidated ABCP conduits as follows:

1. In the regulatory consolidated Balance Sheet (M4) -
 - Assets and liabilities of ABCP conduit VIE's should be recorded in accordance with GAAP.
2. In the Capital Adequacy Return (G3) -
 - Securitization facilities as they would have been accounted for, in the absence of AcG-15, will continue to be recorded on schedules CAR 3 and CAR 4.
 - In the Assets to Capital section of CAR 1, institutions will be required to record the increase in balance sheet assets resulting from the ABCP conduit consolidations.
 - o This increase will represent the conduit's gross assets less the pre-consolidation exposures to the conduit recorded as on-balance sheet assets and off-balance sheet direct credit substitutes.
 - o Institutions are to record this net increase in assets under the line item "Other" in the Deductions section as a negative number.

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