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# Guideline

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**Subject: Accounting For Transfers of Receivables Including  
Securitizations**

**Category: Accounting**

**No: D-8**

**Date: October 2002**

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## Introduction

This Guideline provides federally regulated financial institutions (FRFIs) with certain application guidance to the Accounting Guideline, AcG-12, *Transfers of Receivables*, issued by the Accounting Standards Board of the Canadian Institute of Chartered Accountants (CICA). AcG-12 supersedes the CICA Abstracts: EIC-9, *Transfers of Receivables* and EIC-54, *Transfers of Receivables – Definition of Recourse*, and OSFI's Guidelines D-3, *Accounting for NHA Mortgage-backed Securities*, and D-4, *Transfers of Financial Assets with Recourse*. Certain transactions will continue to be addressed by this older guidance (see the *Status* and *Scope* sections of the amended Guidelines D-3 and D-4 for further details).

OSFI Guideline B-5, *Asset Securitization*, addresses the capital issues relating to transfers of receivables including securitizations.



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## Isolation of Transferred Assets and Recourse

In order that FRFIs, in a transfer of receivables, appropriately address all issues relating to the isolation of transferred assets from, and recourse to, the transferor, OSFI expects FRFIs to ensure that:

- (a) the transfer meets the isolation criterion in paragraph 9 of AcG-12, and
- (b) all aspects of recourse to the transferor are fully documented, and recognized, measured and disclosed in the financial statements.

### *Meeting the Isolation Criterion for Sale Accounting*

OSFI wishes to ensure, in a transfer of receivables, that FRFIs give adequate consideration to such factors as the type and extent of involvement by the transferor in arrangements to protect investors from credit and other risks, and that the transferred assets are truly isolated from the transferor and its creditors before the transfer is accounted for as a sale.

OSFI expects that, as a general rule, a FRFI will have obtained a legal opinion to ensure that a transfer has met the isolation criterion in paragraph 9 of AcG-12. If a legal opinion has not been obtained for any transfer, alternative competent evidential matter should exist to support management's assertion that the isolation criterion has been met.

Where a legal opinion is relied upon to support the accounting conclusion for multiple transfers under a single structure (e.g., revolving credit card structure), and such transfers occur regularly over an extended period of time, FRFIs should obtain annual legal updates of that opinion in order to confirm that:

- (a) the receivables continue to be isolated from the transferor, and
- (b) there have been no subsequent changes in the relevant law that may change the applicability of previous opinions to such transfers.

Isolation of transferred receivables beyond the reach of the transferor and its creditors is achieved more easily in the case of transfers of NHA mortgage-backed securities (NHA-MBS) to third parties than with other transferred assets because neither the transferor nor the transferee bear any credit risk, and there is limited continuing involvement with the transferee. There is no need for the transferor to enter into special arrangements assuming credit risk and, in turn, running a risk of not isolating the receivables. In addition, the transferor has extremely limited continuing involvement (e.g., servicing only) with the third party transferee compared with the continuing involvement the transferor would have with a transferee that is a special purpose entity (SPE). Therefore, OSFI would not require a FRFI to obtain a "deal specific" true sale opinion. However, OSFI would expect a FRFI to check (every 2 years or so) with the Canada Mortgage and Housing Corporation to ensure that modifications have not been made to, or contemplated for, existing MBS programs that would impact the isolation criterion for future transfers.

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## ***Recourse Related to Retained Interests and Recourse Obligation***

### *Recognition and Measurement*

OSFI reminds each FRFI that at the date it implemented AcG-12, it should have performed a thorough and comprehensive review of all contracts, agreements and transactions to which AcG-12 applies.

FRFIs should continue to undertake such a review for all future contracts, agreements and transactions related to a securitization. In the case of routine weekly or monthly replenishments of receivables in a revolving structure, the reviews should be performed on a quarterly basis.

A transferor bears losses provided for under recourse arrangements through a retained interest and/or assumption of a recourse obligation:

A transferor may provide credit enhancement for the senior interests by retaining an interest in the transferred assets against which credit and other losses from the transferred assets would be applied. In these circumstances, the transferor should not recognize a separate obligation for such potential credit losses because they would be factored into the determination of the cash flows to be included in the initial and subsequent measurement of the retained interest. In this case, OSFI expects that the FRFI will maintain appropriate documentation regarding the related recourse provisions and any associated losses. This documentation should be kept on file for examination purposes.

In addition, where the recourse provisions obligate the transferor to make specific payments for the repurchase of assets sold and to indemnify other parties to the securitization, typically for defaults, the transferor should estimate and recognize a separate recourse obligation at the date of transfer. This “write a cheque” approach would reimburse the transferee or others for losses on the underlying assets.

Special attention should be paid to paragraph 51 of AcG-12, which, if for any reason it is not practical to estimate the fair value of the recourse obligation, requires a value to be recorded that is equal to the greater of: (a) the gain on sale that would otherwise be recognized, and (b) the amount that would be calculated with reference to CICA Handbook Section 3290, *Contingencies*.

The balance of the recourse (whether recorded as a liability or as a contraction of a retained interest) should include credit and other losses expected to occur from the time of sale until the recourse period ends.

Since, in all but rare circumstances, the amount of the recourse should be measurable, OSFI expects that FRFIs will keep support for the measurement on file for examination purposes.

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*Disclosure*

AcG-12 does not require any disclosure of the recourse obligation, other than a description of recourse and, if it is not practical to estimate its fair value, a statement of the relevant reasons.

OSFI recommends that the accounting policies for initially and subsequently measuring the fair and present values of the recourse obligation, including the methodology and the associated assumptions, be disclosed in the notes to the financial statements.

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