

FEDERAL RESERVE SYSTEM

12 CFR Part 201

Regulation A; Docket No. R-1371

EXTENSIONS OF CREDIT BY FEDERAL RESERVE BANKS

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: This final rule amends Regulation A to provide a process by which the Federal Reserve Bank of New York may determine the eligibility of credit rating agencies in the Term Asset-backed Securities Loan Facility. The final rule does not apply to discount window lending or other extensions of credit provided by the Federal Reserve System. In addition, the final rule only applies to asset-backed securities that are not backed by commercial real estate. The amendment does not represent a change in the stance of monetary policy.

DATES: Final rule is effective on [INSERT DATE 30 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER].

FOR FURTHER INFORMATION CONTACT: William R. Nelson, Senior Associate Director (202/452-3579), Division of Monetary Affairs; Christopher W. Clubb, Senior Counsel (202/452-3904), Legal Division; for users of Telecommunication Devices for the Deaf (TDD) only, contact 202/263-4869.

SUPPLEMENTARY INFORMATION:

I. Background

Proposed Rule. On October 8, 2009, the Board of Governors of the Federal Reserve System (the “Board”) published for public comment a notice of proposed

rulemaking (“NPRM”) that would amend Regulation A to provide a process by which the Federal Reserve Bank of New York (“FRBNY”) may determine the eligibility of credit rating agencies in the Term Asset-backed Securities Loan Facility (“TALF”).¹ The Board has determined the terms and conditions for TALF borrowing and eligible collateral, including minimum credit ratings and the set of credit rating agencies whose ratings may be accepted for purposes of TALF by FRBNY. Since TALF was established, the Board and FRBNY have accepted credit ratings from three credit rating agencies (Standard & Poor’s, Moody’s Investors Service, and Fitch Ratings). The proposed amendment was designed to provide FRBNY with a consistent framework for determining the eligibility for use in TALF of ratings issued by individual credit rating agencies when used in conjunction with a separate asset-level risk assessment process.

The NPRM proposed an objective minimal experience-based approach specific to the types of assets accepted as collateral in TALF. As a threshold requirement, the proposed rule would permit FRBNY to accept only a credit rating issued by a credit rating agency that is registered with the Securities and Exchange Commission as a “nationally recognized statistical rating organization” (NRSRO) for issuers of asset-backed securities (ABS) pursuant to the Credit Rating Agency Reform Act of 2006 (CRARA).² The proposed rule also would require that the NRSRO had issued ratings on

¹ Proposed rule, 74 *Federal Register* 51806 (Oct. 8, 2009). The TALF is a funding facility to help market participants meet the credit needs of households and businesses by supporting the issuance of new asset-backed securities (ABS) collateralized by loans of various types to consumers and businesses of all sizes. The TALF was established under section 13(3) of the Federal Reserve Act, which permits the Board of Governors of the Federal Reserve Board, in unusual and exigent circumstances, to authorize Reserve Banks to extend credit to individuals, partnerships and corporations that are unable to obtain adequate credit accommodations. For the terms and conditions and frequently asked question of the TALF, refer to <http://www.federalreserve.gov/monetarypolicy/talf.htm>

² CRARA (Pub. L. No. 109-291, 120 Stat. 1327) is primarily codified at 15 U.S.C. § 78o-7.

at least ten transactions within a specified asset category since September 30, 2006. The asset categories are:

- Category 1 – auto loans, floorplan loans, and equipment loans TALF sectors;
- Category 2 – credit card receivables and insurance premium finance loans TALF sectors;
- Category 3 – mortgage servicing advance receivables TALF sector³; and
- Category 4 – student loans TALF sector.

In addition, the proposed rule would allow FRBNY to accept credit ratings only from a credit rating agency that has a current and publicly available rating methodology specific to ABS in the particular TALF asset sector (as defined in the TALF haircut schedule) for which the credit rating agency wishes its ratings to be considered for TALF.

The proposed rule also described the process whereby FRBNY would determine whether an NRSRO becomes eligible to have its ratings accepted for TALF ABS. In addition, under the proposed rule, FRBNY could, at any time, review the continued use of ratings from a credit rating agency in one or more TALF ABS sectors and determine that such credit ratings were no longer acceptable if the credit rating agency no longer met the eligibility requirements or conditions. Finally, the proposed rule set out two conditions that FRBNY would have to ensure were met by an NRSRO in order for the NRSRO to have its credit ratings accepted for TALF ABS. First, the NRSRO would have to agree to discuss with the Federal Reserve its views of the credit risk of any transaction within the TALF asset sector that has been submitted to TALF and upon

³ The proposed rule would permit an NRSRO to aggregate ratings on residential mortgage-backed securities (not currently included in the TALF) for purposes of meeting the ten-transaction requirement for Category 3 (mortgage servicing advance loans TALF sector).

which the NRSRO is being or has been consulted by the issuer. Second, the NRSRO would have to agree to provide any information requested by the Federal Reserve regarding the credit rating agency's continued eligibility under the factors set out in the proposed rule, such as continuing to be properly registered as an NRSRO with the Securities and Exchange Commission and continuing to have a current and publicly available rating methodology specific to ABS in the particular TALF asset sector.

Public comments. The Board received only one comment that was responsive to the NPRM.⁴ The comment was from a credit rating agency that was supportive of the proposed rule. In particular, the commenter supported the objective, experience-based approach adopted by the proposal. The commenter also agreed that registration as an NRSRO for issuers of ABS should be a threshold requirement, but not the sole requirement, for TALF. The commenter also supported the experience and publicly available rating methodology requirements of the proposed rule. Finally, the commenter endorsed the proposed rule's requirement that the NRSRO confer with the Federal Reserve regarding relevant TALF credit risk issues and provide requested information regarding the NRSRO's continuing eligibility with respect to TALF. The commenter did not suggest any changes to the proposed rule.

Final rule. After carefully considering the comments received and other facts of record, and for the reasons discussed herein and in the NPRM, the Board has adopted a final rule in essentially the same form as the proposed rule, except for minor clarifying revisions. An NRSRO may submit the information necessary for FRBNY to make an

⁴ Another comment was filed by a consumer in the NPRM docket, but it did not provide comments responsive to the NPRM. The comment letters are available from the Board's Freedom of Information Office by calling (202) 452-3684, as well as on the Board's public website at: <http://www.federalreserve.gov/generalinfo/foia/index.cfm?>

eligibility determination for the NRSRO under the final rule at any time, including prior to the effective date of the final rule. FRBNY may make the NRSRO eligible for TALF under the final rule as of the effective date or thereafter. The set of NRSROs eligible pursuant to this final rule will take effect commencing with the February 2010 TALF subscription.

II. Administrative Law Matters

A. Final Regulatory Flexibility Analysis

An initial regulatory flexibility analysis (IRFA) was included in the NPRM in accordance with the Regulatory Flexibility Act (RFA).⁵ In the IRFA, the Board specifically solicited comment, including from small entities, on whether the proposed rule would have a significant economic impact on a substantial number of small entities. No small entities submitted comments regarding quantification of their projected costs. The Board expects this rule to affect a number of small entities; however, the cost this rule imposes would not appear to have a significant economic impact on a substantial number of small entities, within the meaning of the RFA.

Even though this rule does not appear to have a significant economic impact on a substantial number of small entities, the Board not formally certified the rule as not having a significant economic impact on a substantial number of small entities, as provided under section 605(b) of the RFA. Instead, the Board has prepared a Final Regulatory Flexibility Analysis (FRFA) as described in the RFA, 5 U.S.C. 604.⁶

The RFA requires each FRFA to contain:

⁵ 5 U.S.C. 601 *et seq.*

⁶ When promulgating a final rule, the RFA requires agencies to prepare a FRFA unless the agency finds that the final rule will not, if promulgated, have a significant economic impact on a substantial number of small entities. 5 U.S.C. 604(a) and 605(b).

- A succinct statement of the need for, and objectives of, the rule;
- A summary of the significant issues raised by the public comments in response to the initial regulatory flexibility analysis, a summary of the assessment of the agency of such issues, and a statement of any changes made in the proposed rule as a result of such comments;
- A description of and an estimate of the number of small entities to which the rule will apply or an explanation of why no such estimate is available;
- A description of the projected reporting, recordkeeping and other compliance requirements of the rule, including an estimate of the classes of small entities which will be subject to the requirement and the type of professional skills necessary for preparation of the report or record; and
- A description of the steps the agency has taken to minimize the significant economic impact on small entities consistent with the stated objectives of applicable statutes, including a statement of the factual, policy, and legal reasons for selecting the alternative adopted in the final rule and why each one of the other significant alternatives to the rule considered by the agency which affect the impact on small entities was rejected.⁷

1. Statement of the need for, and objectives of, the final rule. As discussed in the preamble above, the Board is adopting this rule to govern FRBNY's determination of eligibility of NRSROs and their credit ratings for use in TALF. The objective of the final rule is to provide for an objective, prudent, and reasonably consistent process for FRBNY to determine the eligibility of NRSROs and their credit ratings for purposes of TALF ABS. The Board anticipates that implementation of the final rule will permit an expansion of the set of NRSROs accepted for TALF ABS, while maintaining appropriate protection against credit risk for the U.S. taxpayer in connection with TALF.

2. Significant issues raised by comments in response to the IRFA. Commenters did not raise any issues in response to the IRFA. The Board is adopting the final rule in essentially the same form as the proposed rule.

⁷ 5 U.S.C. 604(a).

3. Description and estimate of classes of small entities affected by the final rule. As noted in the IRFA, there are ten NRSROs registered with the SEC. Of those ten, the Board's review of publicly available information indicates that three NRSROs are not "small entities" under the RFA because their asset size (or the asset size of the NRSRO's parent company) is larger than the level set in the SBA regulation. For purposes of this FRFA, the Board will assume that all seven of the remaining NRSROs would qualify as "small entities" under the SBA regulations.

4. Recordkeeping, Reporting and Other Compliance Requirements. The Board believes that the final rule does not establish any reporting, recordkeeping, or other compliance requirements that are not already part of the NRSRO registration process with the Securities and Exchange Commission or involve records that would not otherwise be created in the normal and customary course of an NRSRO's business. In addition, other than that which is normally required in the credit rating agency industry, special expertise should not be required to compile the information necessary to submit an eligibility request to FRBNY for use of an NRSRO's credit ratings in TALF. Most NRSRO's should have this information readily available in the normal and customary course of business.

The conditions required for FRBNY to accept ratings may similarly require minimal expenditure of resources by an NRSRO, but the Board believes that such information should be readily available in the normal and customary course of the business of a credit rating agency. FRBNY may request information from an NRSRO for the purpose of determining that the NRSRO continues to meet the eligibility requirements under the final rule. Also, an NRSRO that has been consulted on a transaction in TALF

may be requested by FRBNY to discuss its views of the particular transaction, but it would not be required to conduct any more analysis than it had already conducted in the course of its business.

5. Steps Taken to Minimize the Economic Impact on Small Entities. As discussed in the IRFA, the Board considered alternatives to the approach adopted in the proposed rule and selected the approach adopted in the proposed rule for the reasons set out in the IRFA. The Board did not receive any comments suggesting any additional alternatives to the approach adopted in the proposed rule. The Board is adopting the final rule in essentially the same form as the proposed rule.

B. Paperwork Reduction Act Analysis

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. Ch. 3506; 5 CFR 1320 Appendix A.1), the Board reviewed the final rule under the authority delegated to the Board by the Office of Management and Budget (OMB). The Federal Reserve may not conduct or sponsor, and an organization is not required to respond to, this information collection unless it displays a currently valid OMB control number. The OMB control number will be assigned.

The collection of information that is revised by this rulemaking is found in 12 CFR 201.3(e)(1)(ii) and (iii). This information is required to permit FRBNY to determine eligibility of credit rating agencies to have their ratings accepted in TALF in accordance with Board standards. The respondents are NRSROs, which may be small entities. There is no record retention requirement in the final rule.

The estimated burden per response is two hours. It is estimated that there will be ten respondents providing information on a one-time basis. Therefore the total amount of

annual burden is estimated to be 20 hours. No comments specifically addressing the burden estimate were received.

The Federal Reserve has a continuing interest in the public's opinions of our collections of information. At any time, comments regarding the burden estimate, or any other aspect of this collection of information, including suggestions for reducing the burden, may be sent to: Secretary, Board of Governors of the Federal Reserve System, 20th and C Streets, N.W., Washington, DC 20551; and to the Office of Management and Budget, Paperwork Reduction Project (7100-to be assigned), Washington, DC 20503.

C. Plain Language

Each Federal banking agency, such as the Board, is required to use plain language in all proposed and final rulemakings published after January 1, 2000. 12 U.S.C. 4809. The Board has sought to present the final rule, to the extent possible, in a simple and straightforward manner.

III. Statutory Authority

Pursuant to the authority set out in the Federal Reserve Act and particularly section 11 (codified at 12 U.S.C. 248(j)), the Board adopts the rules set out below.

IV. Text of Final Rules

Lists of Subjects in 12 CFR Part 201

12 CFR Part 201

Credit

Authority and Issuance

For the reasons set forth in the preamble, the Board is amending 12 CFR Chapter II to read as follows:

**PART 201 – EXTENSIONS OF CREDIT BY FEDERAL RESERVE BANKS
(REGULATION A)**

1. The authority citation for part 201 continues to read as follows:

Authority: 12 U.S.C. 248(i)-(j), 343 et seq., 347a, 347b, 347c, 348 et seq., 357, 374, 374a, and 461.

2. In § 201.3, paragraph (e) is added to read as follows.

§ 201.3 Extensions of credit generally.

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(e) Credit ratings for Term Asset-Backed Securities Loan Facility (TALF)

(1) If the Board requires that a TALF advance, discount, or other extension of credit be against collateral (other than commercial mortgage-backed securities) that is rated by one or more credit rating agencies, the Federal Reserve Bank of New York may only accept the ratings of any credit rating agency that:

- (i) Is registered with the Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization for issuers of asset-backed securities;
- (ii) Has a current and publicly available rating methodology specific to asset-backed securities in the particular TALF asset sector (as defined in the TALF haircut schedule) for which it wishes its ratings to be accepted; and
- (iii) Demonstrates that it has sufficient experience to provide credit ratings that would assist in the Federal Reserve Bank of New York's risk assessment on the most senior classes of newly issued asset-backed securities in the particular TALF asset sector by having made public or made available to a paying subscriber base, since September 30, 2006, ratings on at least ten transactions denominated in U.S. dollars within the particular category to which the particular TALF asset sector is assigned as set out below –
 - (A) Category 1 – auto, floorplan, and equipment TALF sectors;
 - (B) Category 2 – credit card and insurance premium finance TALF sectors;
 - (C) Category 3 – mortgage servicing advances TALF sector; and
 - (D) Category 4 – student loans TALF sector.

(2) For purposes of the requirement in (e)(1)(iii), ratings on residential mortgage-backed securities may be included in Category 3 (servicer advances).

(3) The Federal Reserve Bank of New York may in its discretion review at any time the eligibility of a credit rating agency to rate one or more types of assets being offered as collateral.

(4) Process

- (i) Credit rating agencies that wish to have their ratings accepted for TALF transactions should send a written notice to the Credit, Investment, and Payment Risk group of the Federal Reserve Bank of New York including information on the factors listed in paragraph (e)(1) with respect to each TALF asset sector for which they wish their ratings to be accepted.
- (ii) The Federal Reserve Bank of New York will notify the submitter within 5 business days of receipt of a submission whether additional information needs to be submitted.
- (iii) Within 5 business days of receipt of all information necessary to evaluate a credit rating agency pursuant to the factors set out in paragraph (e)(1), the Federal Reserve Bank of New York will notify the credit rating agency regarding its eligibility.

(5) Conditions. The Federal Reserve Bank of New York may accept credit ratings under this subsection only from a credit rating agency that agrees to -

- (i) Discuss with the Federal Reserve its views of the credit risk of any transaction within the TALF asset sector that has been submitted to TALF and upon which the credit rating agency is being or has been consulted by the issuer; and
- (ii) Provide any information requested by the Federal Reserve for the purpose of determining that the credit rating agency continues to meet the eligibility requirements under paragraph (e)(1).

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By order of the Board of Governors of the Federal Reserve System, December 4, 2009.

Jennifer J. Johnson (signed)

Jennifer J. Johnson,
Secretary.