

## Corporate & Financial Weekly Digest

December 16, 2011 by [Jeffrey M. Werthan](#)

### **OCC Proposes Rule to Remove References to Credit Ratings in Determining Whether Investment Securities Are Eligible for Investment**

On November 29, the Office of the Comptroller of the Currency (OCC) proposed a rule to remove references to credit ratings from various OCC regulations and related guidance "to assist national banks and federal savings associations in meeting due diligence requirements in assessing credit risk for portfolio investments." Comments may be submitted through December 29.

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Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) requires federal agencies to review regulations that require the use of an assessment of creditworthiness of a security or money market instrument and to substitute any references to, or requirements of, reliance on credit ratings with standards of creditworthiness that each agency determines to be appropriate. On August 13, 2010, the OCC previously published an advance notice of proposed rulemaking (ANPR) that identified the references to credit ratings in its regulations at 12 CFR parts 1, 16, and 28 and requested comment on alternative creditworthiness standards. On October 14, 2010, the Office of Thrift Supervision (the OTS) published a similar ANPR describing the references to credit ratings in the non-capital regulations applicable to savings associations, including the OTS's investment securities regulations. Notwithstanding the requirements of section 939A of the Dodd-Frank Act, a majority of commenters on the ANPRs said that the agencies should continue to use credit ratings, arguing that credit ratings are a valuable tool for national banks and Federal savings associations (herein, referred to collectively as "banks") – especially small banks – for measuring credit risk.

Under the existing OCC rules, an investment security must not be "predominantly speculative in nature." The OCC rules provide that an obligation is not predominantly speculative in nature" if it is rated investment grade or, if unrated, is the credit equivalent of investment grade. As noted, the proposed OCC rule would remove references to

credit ratings in the OCC's non-capital regulations. Under the proposed amendments to Parts 1 and 16, a security would be "investment grade" if the issuer of the security "has an adequate capacity to meet financial commitments under the security for the projected life of the asset or exposure." The "adequate capacity to meet financial commitments" standard would replace language in §§ 1.2 and 16.2 which currently reference Nationally Recognized Statistical Rating Organization credit ratings. To meet this new standard, national banks must be able to determine that "the risk of default by the obligor is low and the full and timely repayment of principal and interest is expected." While "external credit ratings and assessments remain valuable sources of information and provide national banks with a standardized credit risk indicator, banks must supplement the external ratings with due diligence processes and analyses that are appropriate for the bank's risk profile and for the size and complexity of the instrument." In addition to following the standard under the proposed rule, national banks and federal savings associations would be expected to continue to maintain appropriate ongoing reviews of their investment portfolios to verify that they meet safety and soundness requirements appropriate for the institution's risk profile and for the size and complexity of the portfolios.

According to the OCC, the proposed guidance "clarifies" steps national banks should take to demonstrate they have properly verified their investments meet the newly established credit quality standards under 12 CFR Part 1 and steps national banks and federal savings associations should take to demonstrate they met due diligence requirements when purchasing investment securities and conducting ongoing reviews of their investment portfolios. Additionally, when purchasing corporate debt securities, Federal savings associations will need to follow requirements to be established by the Federal Deposit Insurance Corporation pursuant to 12 U.S.C. 1831e(d) (as amended by section 939(a)(2) of the Dodd-Frank Act).

For more information, click [here](#).

To review the proposed guidance, click [here](#).

Katten Muchin Rosenman LLP  
Charlotte Chicago Irving London Los Angeles New York Washington, DC