

Text of Common Appendix (All Agencies)

The text of the agencies' common appendix appears below:

Appendix [] to Part [] – Capital Adequacy Guidelines for [Banks]:¹ Standardized Framework

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¹ For simplicity, and unless otherwise noted, this NPR uses the term [BANK] to include banks, savings associations, and bank holding companies. The term [agency] refers to the primary Federal supervisor of the bank applying the rule. The term [the general risk-based capital rules] refers to each agency's existing non-internal ratings based capital rules. The term [the advanced approaches risk-based capital rules] refers to each agency's existing internal ratings based capital rules. The term [the market risk rule] refers to the agencies' existing market risk capital rules.

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Part I. General Provisions

Section 1. Purpose, Applicability, Election Procedures, and Reservation of Authority

(a) Purpose. This appendix establishes:

(1) Methodologies for the calculation of risk-based capital requirements for [BANK]s that elect to use this appendix; and

(2) Operational and public disclosure requirements for such [BANK]s.

(b) Applicability. This appendix applies to a [BANK] that:

(1) Elects to use this appendix to calculate its risk-based capital requirements;

(2) Must use this appendix based on a determination by the [agency] under paragraph

(c)(3) of this section;

(3) Is a subsidiary of or controls a depository institution that uses 12 CFR part 3, appendix D; 12 CFR part 208, appendix G; 12 CFR part 325, appendix E; or 12 CFR part 567, appendix B to calculate its risk-based capital requirements; or

(4) Is a subsidiary of a bank holding company that uses 12 CFR part 225, appendix H, to calculate its risk-based capital requirements.

(c) Election procedures. (1) Opt-in procedures. (i) Except for a [BANK] that is required under section 1(b)(1) of [the advanced approaches risk-based capital rules] to use that capital framework (other than a [BANK] that is exempt under section 1(b)(3) of [the advanced approaches risk-based capital rules]), any [BANK] may elect to use this appendix to calculate its risk-based capital requirements.

(ii) Unless otherwise waived by the [agency], a [BANK] must notify the [agency] of its intent to use this appendix in writing at least 60 days before the beginning of the calendar quarter in which it first uses this appendix. This notice must contain a list of any affiliated depository institutions or bank holding companies, if applicable, that seek not to apply this appendix under section 1(c)(2)(iii) of 12 CFR part 3, appendix D; 12 CFR part 208, appendix G; 12 CFR part 225, appendix H; 12 CFR part 325, appendix E; or 12 CFR part 567, appendix B.

(2) Opt-out procedures. (i) A [BANK] that uses this appendix to calculate its risk-based capital requirements may instead elect to use the [the general risk-based capital rules] or [the advanced approaches risk-based capital rules].

(ii) Unless otherwise waived by the [agency], a [BANK] must notify the [agency] of its intent to cease the use of this appendix in writing at least 60 days before the beginning of the calendar quarter in which it plans to cease the use of this appendix. Such notice must include an explanation of the [BANK]'s rationale for ceasing the use of this appendix and a statement regarding the appendix or rules the [BANK] plans to use to calculate its risk-based capital requirements.

(iii) A [BANK] that otherwise would be required to apply this appendix under paragraph (b)(3) or (b)(4) of this section may continue to use [the general risk-based capital rules] if the

[agency] determines in writing that application of this appendix is not appropriate in light of the [BANK]'s asset size, level of complexity, risk profile, or scope of operations.

(3) Supervisory application of this appendix and exclusion. (i) The [agency] may apply this appendix to any [BANK] if the [agency] determines that application of this appendix is appropriate in light of the [BANK]'s asset size, level of complexity, risk profile, or scope of operations.

(ii) The [agency] may exclude a [BANK] that has opted-in under paragraph (c)(1) of this section from using this appendix if the [agency] determines that application of this appendix is not appropriate in light of the [BANK]'s asset size, level of complexity, risk profile, or scope of operations.

(d) Reservation of authority. (1) Additional capital in the aggregate. The [agency] may require a [BANK] to hold an amount of capital greater than otherwise required under this appendix if the [agency] determines that the [BANK]'s risk-based capital requirement under this appendix is not commensurate with the [BANK]'s credit, market, operational, or other risks.

(2) Risk-weighted asset amounts. (i) If the [agency] determines that the risk-weighted asset amount calculated under this appendix by the [BANK] for one or more exposures is not commensurate with the risks associated with those exposures, the [agency] may require the [BANK] to assign a different risk-weighted asset amount to the exposure(s) or to deduct the amount of the exposure from capital.

(ii) If the [agency] determines that the risk-weighted asset amount for operational risk produced by the [BANK] under this appendix is not commensurate with the operational risks of the [BANK], the [agency] may require the [BANK] to assign a different risk-weighted asset amount for operational risk.

(3) Other supervisory authority. Nothing in this appendix limits the authority of the [agency] under any other provision of law or regulation to take supervisory or enforcement action, including action to address unsafe or unsound practices or conditions, deficient capital levels, or violations of law.

(e) Notice and response procedures. In making a determination under paragraph (c)(2)(iii), (c)(3), or (d) of this section, the [agency] will apply notice and response procedures in the same manner as the notice and response procedures in 12 CFR 3.12 (for national banks), 12 CFR 263.202 (for bank holding companies and state member banks), 12 CFR 325.6(c) (for state nonmember banks), and 12 CFR 567.3(d) (for savings associations).

(f) Principle of conservatism. Notwithstanding the requirements of this appendix, a [BANK] may choose not to apply a provision of this appendix to one or more exposures, provided that:

(1) The [BANK] can demonstrate on an ongoing basis to the satisfaction of the [agency] that not applying the provision would, in all circumstances, unambiguously generate a risk-based capital requirement for each such exposure greater than that which would otherwise be required under this appendix;

(2) The [BANK] appropriately manages the risk of each such exposure;

(3) The [BANK] notifies the [agency] in writing prior to applying this principle to each such exposure; and

(4) The exposures to which the [BANK] applies this principle are not, in the aggregate, material to the [BANK].

Section 2. Definitions. For the purposes of this appendix, the following definitions apply:

Affiliate with respect to a company means any company that controls, is controlled by, or is under common control with, the company.

Applicable external rating. With respect to an exposure, applicable external rating means:

- (1) If the exposure has a single external rating, the external rating; and
- (2) If the exposure has multiple external ratings, the lowest external rating.

(See also external rating.)

Applicable inferred rating. With respect to an exposure, applicable inferred rating means:

- (1) If the exposure has a single inferred rating, the inferred rating; and
- (2) If the exposure has multiple inferred ratings, the lowest inferred rating.

(See also external rating, inferred rating.)

Asset-backed commercial paper (ABCP) program means a program that primarily issues commercial paper that:

- (1) Has an external rating; and
- (2) Is backed by underlying exposures held in a bankruptcy-remote securitization special purpose entity (SPE).

Asset-backed commercial paper (ABCP) program sponsor means a [BANK] that:

- (1) Establishes an ABCP program;
- (2) Approves the sellers permitted to participate in an ABCP program;
- (3) Approves the exposures to be purchased by an ABCP program; or
- (4) Administers the ABCP program by monitoring the underlying exposures,

underwriting or otherwise arranging for the placement of debt or other obligations issued by the program, compiling monthly reports, or ensuring compliance with the program

documents and with the program's credit and investment policy.

Carrying value means, with respect to an asset, the value of the asset on the balance sheet of the [BANK] determined in accordance with generally accepted accounting principles (GAAP).

Clean-up call means a contractual provision that permits an originating [BANK] or servicer to call securitization exposures before their stated maturity or call date. (See also eligible clean-up call.)

Commitment means any legally binding arrangement that obligates a [BANK] to extend credit or to purchase assets.

Commodity derivative contract means a commodity-linked swap, purchased commodity-linked option, forward commodity-linked contract, or any other instrument linked to commodities that gives rise to similar counterparty credit risks.

Company means a corporation, partnership, limited liability company, business trust, special purpose entity, depository institution, association, or similar organization.

Control. A person or company controls a company if it:

(1) Owns, controls, or holds with power to vote 25 percent or more of a class of voting securities of the company; or

(2) Consolidates the company for financial reporting purposes.

Controlled early amortization provision means an early amortization provision that meets all the following conditions:

(1) The originating [BANK] has appropriate policies and procedures to ensure that it has sufficient capital and liquidity available in the event of an early amortization;

(2) Throughout the duration of the securitization (including the early amortization period), there is the same pro rata sharing of interest, principal, expenses, losses, fees, recoveries, and other cash flows from the underlying exposures based on the originating [BANK]'s and the investors' relative shares of the underlying exposures outstanding measured on a consistent monthly basis;

(3) The amortization period is sufficient for at least 90 percent of the total underlying exposures outstanding at the beginning of the early amortization period to be repaid or recognized as in default; and

(4) The schedule for repayment of investor principal is not more rapid than would be allowed by straight-line amortization over an 18-month period.

Corporate exposure means a credit exposure to a natural person or a company (including an industrial development bond, an exposure to a government-sponsored entity (GSE), or an exposure to a securities broker or dealer) that is not:

(1) An exposure to a sovereign entity, the Bank for International Settlements, the European Central Bank, the European Commission, the International Monetary Fund, a multilateral development bank (MDB), a depository institution, a foreign bank, a credit union, or a public sector entity (PSE);

(2) A regulatory retail exposure;

(3) A residential mortgage exposure;

(4) A pre-sold construction loan;

(5) A statutory multifamily mortgage;

(6) A securitization exposure; or

(7) An equity exposure.

Credit derivative means a financial contract executed under standard industry credit derivative documentation that allows one party (the protection purchaser) to transfer the credit risk of one or more exposures (reference exposure) to another party (the protection provider). (See also eligible credit derivative.)

Credit-enhancing interest-only strip (CEIO) means an on-balance sheet asset that, in form or in substance:

(1) Represents a contractual right to receive some or all of the interest and no more than a minimal amount of principal due on the underlying exposures of a securitization; and

(2) Exposes the holder to credit risk directly or indirectly associated with the underlying exposures that exceeds a pro rata share of the holder's claim on the underlying exposures, whether through subordination provisions or other credit-enhancement techniques.

Credit-enhancing representations and warranties means representations and warranties that are made or assumed in connection with a transfer of underlying exposures (including loan servicing assets) and that obligate a [BANK] to protect another party from losses arising from the credit risk of the underlying exposures. Credit-enhancing representations and warranties include provisions to protect a party from losses resulting from the default or nonperformance of the obligors of the underlying exposures or from an insufficiency in the value of the collateral backing the underlying exposures. Credit-enhancing representations and warranties do not include:

(1) Early default clauses and similar warranties that permit the return of, or premium refund clauses that cover, loans secured by a first lien on one-to-four family residential property for a period not to exceed 120 days from the date of transfer, provided that the date of transfer is within one year of origination of the residential mortgage exposure;

(2) Premium refund clauses that cover underlying exposures guaranteed, in whole or in part, by the U.S. government, a U.S. government agency, or a GSE, provided that the clauses are for a period not to exceed 120 days from the date of transfer; or

(3) Warranties that permit the return of underlying exposures in instances of misrepresentation, fraud, or incomplete documentation.

Credit risk mitigant means collateral, a credit derivative, or a guarantee.

Depository institution means a depository institution as defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813).

Derivative contract means a financial contract whose value is derived from the values of one or more underlying assets, reference rates, or indices of asset values or reference rates.

Derivative contracts include interest rate derivative contracts, exchange rate derivative contracts, equity derivative contracts, commodity derivative contracts, credit derivative contracts, and any other instrument that poses similar counterparty credit risks. Derivative contracts also include unsettled securities, commodities, and foreign exchange transactions with a contractual settlement or delivery lag that is longer than the lesser of the market standard for the particular instrument or five business days.

Early amortization provision means a provision in the documentation governing a securitization that, when triggered, causes investors in the securitization exposures to be repaid before the original stated maturity of the securitization exposures, unless the provision:

(1) Is triggered solely by events not directly related to the performance of the underlying exposures or the originating [BANK] (such as material changes in tax laws or regulations); or

(2) Leaves investors fully exposed to future draws by obligors on the underlying exposures even after the provision is triggered. (See also controlled early amortization provision.)

Effective notional amount means, for an eligible guarantee or eligible credit derivative, the lesser of the contractual notional amount of the credit risk mitigant or the exposure amount of the hedged exposure, multiplied by the percentage coverage of the credit risk mitigant. For example, the effective notional amount of an eligible guarantee that covers, on a pro rata basis, 40 percent of any losses on a \$100 bond would be \$40.

Eligible asset-backed commercial paper (ABCP) liquidity facility means a liquidity facility supporting ABCP, in form or in substance, that is subject to an asset quality test at the time of draw that precludes funding against assets that are 90 days or more past due or in default. If the assets or exposures that an eligible ABCP liquidity facility is required to fund against are externally rated at the inception of the facility, the facility can be used to fund only those assets or exposures with an applicable external rating of at least investment grade at the time of funding. Notwithstanding the two preceding sentences, a liquidity facility is an eligible ABCP liquidity facility if the assets or exposures funded under the liquidity facility that do not meet the eligibility requirements are guaranteed by a sovereign entity with an issuer rating in one of the three highest investment grade rating categories.

Eligible clean-up call means a clean-up call that:

- (1) Is exercisable solely at the discretion of the originating [BANK] or servicer;
- (2) Is not structured to avoid allocating losses to securitization exposures held by investors or otherwise structured to provide credit enhancement to the securitization; and

(3) (i) For a traditional securitization, is only exercisable when 10 percent or less of the principal amount of the underlying exposures or securitization exposures (determined as of the inception of the securitization) is outstanding; or

(ii) For a synthetic securitization, is only exercisable when 10 percent or less of the principal amount of the reference portfolio of underlying exposures (determined as of the inception of the securitization) is outstanding.

Eligible credit derivative means a credit derivative in the form of a credit default swap, nth-to-default swap, total return swap, or any other form of credit derivative approved by the [agency], provided that:

(1) The contract meets the requirements of an eligible guarantee and has been confirmed by the protection purchaser and the protection provider;

(2) Any assignment of the contract has been confirmed by all relevant parties;

(3) If the credit derivative is a credit default swap or nth-to-default swap, the contract includes the following credit events:

(i) Failure to pay any amount due under the terms of the reference exposure, subject to any applicable minimal payment threshold that is consistent with standard market practice and with a grace period that is closely in line with the grace period of the reference exposure; and

(ii) Bankruptcy, insolvency, or inability of the obligor on the reference exposure to pay its debts, or its failure or admission in writing of its inability generally to pay its debts as they become due, and similar events;

(4) The terms and conditions dictating the manner in which the contract is to be settled are incorporated into the contract;

(5) If the contract allows for cash settlement, the contract incorporates a robust valuation process to estimate loss reliably and specifies a reasonable period for obtaining post-credit event valuations of the reference exposure;

(6) If the contract requires the protection purchaser to transfer an exposure to the protection provider at settlement, the terms of at least one of the exposures that is permitted to be transferred under the contract provide that any required consent to transfer may not be unreasonably withheld;

(7) If the credit derivative is a credit default swap or nth-to-default swap, the contract clearly identifies the parties responsible for determining whether a credit event has occurred, specifies that this determination is not the sole responsibility of the protection provider, and gives the protection purchaser the right to notify the protection provider of the occurrence of a credit event; and

(8) If the credit derivative is a total return swap and the [BANK] records net payments received on the swap as net income, the [BANK] records offsetting deterioration in the value of the hedged exposure (through reductions in fair value).

Eligible guarantee means a guarantee from an eligible guarantor that:

(1) Is written;

(2) Is either unconditional, or a contingent obligation of the United States Government or its agencies, the validity of which to the beneficiary is dependent upon some affirmative action on the part of the beneficiary of the guarantee or a third party (for example, servicing requirements);

(3) Covers all or a pro rata portion of all contractual payments of the obligor on the reference exposure;

(4) Gives the beneficiary a direct claim against the protection provider;

(5) Is not unilaterally cancelable by the protection provider for reasons other than the breach of the contract by the beneficiary;

(6) Is legally enforceable against the protection provider in a jurisdiction where the protection provider has sufficient assets against which a judgment may be attached and enforced;

(7) Requires the protection provider to make payment to the beneficiary on the occurrence of a default (as defined in the guarantee) of the obligor on the reference exposure in a timely manner without the beneficiary first having to take legal actions to pursue the obligor for payment;

(8) Does not increase the beneficiary's cost of credit protection on the guarantee in response to deterioration in the credit quality of the reference exposure; and

(9) Is not provided by an affiliate of the [BANK], unless the affiliate is an insured depository institution, foreign bank, securities broker or dealer, or insurance company that:

(i) Does not control the [BANK]; and

(ii) Is subject to consolidated supervision and regulation comparable to that imposed on U.S. depository institutions, securities brokers or dealers, or insurance companies (as the case may be).

Eligible guarantor means:

(1) A sovereign entity, the Bank for International Settlements, the International Monetary Fund, the European Central Bank, the European Commission, a Federal Home Loan Bank, the Federal Agricultural Mortgage Corporation (Farmer Mac), an MDB, a depository institution, a foreign bank, a credit union, a bank holding company (as defined in section 2 of the Bank Holding Company Act (12 U.S.C. 1841)), or a savings and loan holding company (as defined in

12 U.S.C. 1467a) provided all or substantially all of the holding company's activities are permissible for a financial holding company under 12 U.S.C. 1843(k); or

(2) Any other entity (other than a SPE) if at the time the entity issued the guarantee or credit derivative or any time thereafter, the entity has issued and outstanding an unsecured debt security without credit enhancement that has an applicable external rating based on a long-term rating.

Eligible margin loan means an extension of credit where:

(1) The extension of credit is collateralized exclusively by liquid and readily marketable debt or equity securities, gold, or conforming residential mortgage exposures;

(2) The collateral is marked-to-market daily, and the transaction is subject to daily margin maintenance requirements;

(3) The extension of credit is conducted under an agreement that provides the [BANK] the right to accelerate and terminate the extension of credit and to liquidate or set off collateral promptly upon an event of default (including upon an event of bankruptcy, insolvency, or similar proceeding) of the counterparty, provided that, in any such case, any exercise of rights under the agreement will not be stayed or avoided under applicable law in the relevant jurisdictions;² and

(4) The [BANK] has conducted sufficient legal review to conclude with a well-founded basis (and maintains sufficient written documentation of that legal review) that the agreement meets the requirements of paragraph (3) of this definition and is legal, valid, binding, and enforceable under applicable law in the relevant jurisdictions.

² This requirement is met where all transactions under the agreement are (i) executed under U.S. law and (ii) constitute "securities contracts" under section 555 of the Bankruptcy Code (11 U.S.C. 555), qualified financial contracts under section 11(e)(8) of the Federal Deposit Insurance Act (12 U.S.C. 1821(e)(8)), or netting contracts between or among financial institutions under sections 401-407 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (12 U.S.C. 4401-4407) or the Federal Reserve Board's Regulation EE (12 CFR part 231).

Eligible servicer cash advance facility means a servicer cash advance facility in which:

(1) The servicer is entitled to full reimbursement of advances, except that a servicer may be obligated to make non-reimbursable advances for a particular underlying exposure if any such advance is contractually limited to an insignificant amount of the outstanding principal balance of that exposure;

(2) The servicer's right to reimbursement is senior in right of payment to all other claims on the cash flows from the underlying exposures of the securitization; and

(3) The servicer has no legal obligation to, and does not, make advances to the securitization if the servicer concludes the advances are unlikely to be repaid.

Equity derivative contract means an equity-linked swap, purchased equity-linked option, forward equity-linked contract, or any other instrument linked to equities that gives rise to similar counterparty credit risks.

Equity exposure means:

(1) A security or instrument (whether voting or non-voting) that represents a direct or indirect ownership interest in, and is a residual claim on, the assets and income of a company, unless:

(i) The issuing company is consolidated with the [BANK] under GAAP;

(ii) The [BANK] is required to deduct the ownership interest from tier 1 or tier 2 capital under this appendix;

(iii) The ownership interest incorporates a payment or other similar obligation on the part of the issuing company (such as an obligation to make periodic payments); or

(iv) The ownership interest is a securitization exposure;

(2) A security or instrument that is mandatorily convertible into a security or instrument described in paragraph (1) of this definition;

(3) An option or warrant that is exercisable for a security or instrument described in paragraph (1) of this definition; or

(4) Any other security or instrument (other than a securitization exposure) to the extent the return on the security or instrument is based on the performance of a security or instrument described in paragraph (1) of this definition.

Exchange rate derivative contract means a cross-currency interest rate swap, forward foreign-exchange contract, currency option purchased, or any other instrument linked to exchange rates that gives rise to similar counterparty credit risks.

Exposure amount means:

(1) For the on-balance sheet component of an exposure (other than an OTC derivative contract; a repo-style transaction or an eligible margin loan for which the [BANK] determines the exposure amount under paragraph (c) or (d) of section 37; or a securitization exposure), exposure amount means:

(i) If the exposure is a security classified as available-for-sale, the [BANK]'s carrying value of the exposure, less any unrealized gains on the exposure, plus any unrealized losses on the exposure.

(ii) If the exposure is not a security classified as available-for-sale, the [BANK]'s carrying value of the exposure.

(2) For the off-balance sheet component of an exposure (other than an OTC derivative contract; a repo-style transaction or an eligible margin loan for which the [BANK] calculates the exposure amount under paragraph (c) or (d) of section 37; or a securitization exposure), exposure

amount means the notional amount of the off-balance sheet component multiplied by the appropriate credit conversion factor (CCF) in section 34.

(3) If the exposure is an OTC derivative contract, the exposure amount determined under section 35 or 37.

(4) If the exposure is an eligible margin loan or repo-style transaction for which the [BANK] calculates the exposure amount as provided in paragraph (c) or (d) of section 37, the exposure amount determined under section 37.

(5) If the exposure is a securitization exposure, the exposure amount determined under section 42.

External rating means a credit rating that is assigned by a nationally recognized statistical rating organization (NRSRO) to an exposure, provided:

(1) The credit rating fully reflects the entire amount of credit risk with regard to all payments owed to the holder of the exposure. If a holder is owed principal and interest on an exposure, the credit rating must fully reflect the credit risk associated with timely repayment of principal and interest. If a holder is owed only principal on an exposure, the credit rating must fully reflect only the credit risk associated with timely repayment of principal; and

(2) The credit rating is published in an accessible form and is or will be included in the transition matrices made publicly available by the NRSRO that summarize the historical performance of positions rated by the NRSRO. (See also applicable external rating, applicable inferred rating, inferred rating, issuer rating.)

Financial collateral means collateral:

(1) In the form of:

(i) Cash on deposit with the [BANK] (including cash held for the [BANK] by a third-party custodian or trustee);

(ii) Gold bullion;

(iii) Long-term debt securities that have an applicable external rating of one category below investment grade or higher;

(iv) Short-term debt instruments that have an applicable external rating of at least investment grade;

(v) Equity securities that are publicly traded;

(vi) Convertible bonds that are publicly traded;

(vii) Money market mutual fund shares and other mutual fund shares if a price for the shares is publicly quoted daily; or

(viii) Conforming residential mortgage exposures; and

(2) In which the [BANK] has a perfected, first priority security interest or, outside of the United States, the legal equivalent thereof (with the exception of cash on deposit and notwithstanding the prior security interest of any custodial agent).

Financial standby letter of credit means a letter of credit or similar arrangement that represents an irrevocable obligation of a [BANK] to a third-party beneficiary:

(1) To repay money borrowed by, or advanced to, or for the account of, a second party (the account party); or

(2) To make payment on behalf of the account party, in the event that the account party fails to fulfill its financial obligation to the beneficiary.

First-lien residential mortgage exposure means a residential mortgage exposure secured by a first lien or a residential mortgage exposure secured by first and junior lien(s) where no other party holds an intervening lien. (See also residential mortgage exposure.)

Foreign bank means a foreign bank as defined in section 211.2 of the Federal Reserve Board's Regulation K (12 CFR 211.2) other than a depository institution. (See also depository institution.)

GAAP means generally accepted accounting principles as used in the United States.

Gain-on-sale means an increase in the equity capital (as reported on Schedule RC of the Consolidated Statement of Condition and Income (Call Report), Schedule HC of the FR Y-9C Report, or Schedule SC of the Thrift Financial Report) of a [BANK] that results from a securitization (other than an increase in equity capital that results from the [BANK]'s receipt of cash in connection with the securitization). (See also securitization.)

Guarantee means a financial guarantee, letter of credit, insurance, or other similar financial instrument (other than a credit derivative) that allows one party (beneficiary) to transfer the credit risk of one or more specific exposures (reference exposure) to another party (protection provider). (See also eligible guarantee.)

Inferred rating. (1) Securitization exposures. A securitization exposure has an inferred rating equal to the external rating of the securitization exposure referenced in paragraph (1)(ii) of this definition if:

- (i) The securitization exposure does not have an external rating; and
- (ii) Another securitization exposure issued by the same obligor and secured by the same underlying exposures:
 - (A) Has an external rating;

(B) Is subordinated in all respects to the exposure with no external rating;

(C) Does not benefit from any credit enhancement that is not available to the exposure with no external rating;

(D) Has an effective remaining maturity that is equal to or longer than that of the exposure with no external rating; and

(E) Is the most immediately subordinated exposure to the exposure with no external rating that meets the requirements of paragraph (1)(ii)(A) through (1)(ii)(D) of this definition.

(2) Other exposures. With respect to an exposure to a sovereign entity, an exposure to a PSE, or a corporate exposure, inferred rating means an inferred rating based on an issuer rating and an inferred rating based on a specific issue as determined under section 32 of this appendix. (See also applicable external rating, applicable inferred rating, external rating, issuer rating.)

Interest rate derivative contract means a single-currency interest rate swap, basis swap, forward rate agreement, purchased interest rate option, when-issued securities, or any other instrument linked to interest rates that gives rise to similar counterparty credit risks.

Investing [BANK] means, with respect to a securitization, a [BANK] that assumes the credit risk of a securitization exposure (other than an originating [BANK] of the securitization). In a typical synthetic securitization, the investing [BANK] sells credit protection on a pool of underlying exposures to the originating [BANK].

Investment fund means a company:

(1) All or substantially all of the assets of which are financial assets; and

(2) That has no material liabilities.

Issuer rating means a credit rating that is assigned by an NRSRO to an entity, provided:

(1) The credit rating reflects the entity's capacity and willingness to satisfy all of its financial obligations; and

(2) The credit rating is published in an accessible form and is or will be included in the transition matrices made publicly available by the NRSRO that summarize the historical performance of the NRSRO's ratings. (See also applicable external rating, applicable inferred rating.)

Junior-lien residential mortgage exposure means a residential mortgage exposure that is not a first-lien residential mortgage exposure. (See also first-lien residential mortgage exposure, residential mortgage exposure.)

Main index means the Standard & Poor's 500 Index, the FTSE All-World Index, and any other index for which the [BANK] can demonstrate to the satisfaction of the [agency] that the equities represented in the index have comparable liquidity, depth of market, and size of bid-ask spreads as equities in the Standard & Poor's 500 Index and FTSE All-World Index.

Multi-lateral development bank (MDB) means the International Bank for Reconstruction and Development, the International Finance Corporation, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the European Bank for Reconstruction and Development, the European Investment Bank, the European Investment Fund, the Nordic Investment Bank, the Caribbean Development Bank, the Islamic Development Bank, the Council of Europe Development Bank, and any other multilateral lending institution or regional development bank in which the U.S. government is a shareholder or contributing member or which the [agency] determines poses comparable credit risk.

Nationally recognized statistical rating organization (NRSRO) means an entity registered with the Securities and Exchange Commission (SEC) as a nationally recognized statistical rating organization under section 15E of the Securities Exchange Act of 1934 (15 U.S.C. 78o-7).

Netting set means a group of transactions with a single counterparty that is subject to a qualifying master netting agreement.

Nth-to-default credit derivative means a credit derivative that provides credit protection only for the nth-defaulting reference exposure in a group of reference exposures.

Operational risk means the risk of loss resulting from inadequate or failed internal processes, people, and systems or from external events (including legal risk but excluding strategic and reputational risk).

Original maturity with respect to an off-balance sheet commitment means the length of time between the date a commitment is issued and:

(1) For a commitment that is not subject to extension or renewal, the stated expiration date of the commitment; or

(2) For a commitment that is subject to extension or renewal, the earliest date on which the [BANK] can, at its option, unconditionally cancel the commitment.

Originating [BANK], with respect to a securitization, means a [BANK] that:

(1) Directly or indirectly originated or securitized the underlying exposures included in the securitization; or

(2) Serves as an ABCP program sponsor to the securitization.

Over-the-counter (OTC) derivative contract means a derivative contract that is not traded on an exchange that requires the daily receipt and payment of cash-variation margin.

Performance standby letter of credit (or performance bond) means an irrevocable obligation of a [BANK] to pay a third-party beneficiary when a customer (account party) fails to perform on any contractual nonfinancial or commercial obligation. To the extent permitted by law or regulation, performance standby letters of credit include arrangements backing, among other things, subcontractors' and suppliers' performance, labor and materials contracts, and construction bids.

Pre-sold construction loan means any one-to-four family residential pre-sold construction loan for a residence meeting the requirements under section 618(a)(1) or (2) of the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 (RTCRRRI Act) and under 12 CFR part 3, appendix A, section 3(a)(3)(iv) (for national banks); 12 CFR part 208, appendix A, section III.C.3. (for state member banks); 12 CFR part 225, appendix A, section III.C.3. (for bank holding companies); 12 CFR part 325, appendix A, section II.C. (for state nonmember banks), and that is not 90 days or more past due or on nonaccrual; or 12 CFR 567.1 (definition of “qualifying residential construction loan”) (for savings associations), and that is not on nonaccrual.

Protection amount (P) means, with respect to an exposure hedged by an eligible guarantee or eligible credit derivative, the effective notional amount of the guarantee or credit derivative as reduced to reflect any currency mismatch, maturity mismatch, or lack of restructuring coverage (as provided in section 36).

Publicly traded means traded on:

- (1) Any exchange registered with the SEC as a national securities exchange under section 6 of the Securities Exchange Act of 1934 (15 U.S.C. 78f); or
- (2) Any non-U.S.-based securities exchange that:

(i) Is registered with, or approved by, a national securities regulatory authority; and

(ii) Provides a liquid, two-way market for the instrument in question, meaning that there are enough independent bona fide offers to buy and sell so that a sales price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined promptly and a trade can be settled at such a price within five business days.

Public sector entity (PSE) means a state, local authority, or other governmental subdivision below the sovereign entity level.

Qualifying master netting agreement means any written, legally enforceable bilateral netting agreement, provided that:

(1) The agreement creates a single legal obligation for all individual transactions covered by the agreement upon an event of default, including bankruptcy, insolvency, or similar proceeding, of the counterparty;

(2) The agreement provides the [BANK] the right to accelerate, terminate, and close out on a net basis all transactions under the agreement and to liquidate or set off collateral promptly upon an event of default, including upon an event of bankruptcy, insolvency, or similar proceeding, of the counterparty, provided that, in any such case, any exercise of rights under the agreement will not be stayed or avoided under applicable law in the relevant jurisdictions;

(3) The [BANK] has conducted sufficient legal review to conclude with a well-founded basis (and has maintained sufficient written documentation of that legal review) that:

(i) The agreement meets the requirements of paragraph (2) of this definition; and

(ii) In the event of a legal challenge (including one resulting from default or from bankruptcy, insolvency, or similar proceeding) the relevant court and administrative authorities

would find the agreement to be legal, valid, binding, and enforceable under the law of the relevant jurisdictions;

(4) The [BANK] establishes and maintains procedures to monitor possible changes in relevant law and to ensure that the agreement continues to satisfy the requirements of this definition; and

(5) The agreement does not contain a walkaway clause (that is, a provision that permits a non-defaulting counterparty to make a lower payment than it would make otherwise under the agreement, or no payment at all, to a defaulter or the estate of a defaulter, even if the defaulter or the estate of the defaulter is a net creditor under the agreement).

Regulatory retail exposure means an exposure that meets the following requirements:

(1) The [BANK]'s aggregate exposure to a single obligor does not exceed \$1 million;

(2) The exposure is part of a well diversified portfolio; and

(3) The exposure is not:

(i) An exposure to a sovereign entity, the Bank for International Settlements, the European Central Bank, the European Commission, the International Monetary Fund, an MDB, a depository institution, a foreign bank, a credit union, or a PSE;

(ii) An acquisition, development, and construction loan;

(iii) A residential mortgage exposure;

(iv) A pre-sold construction loan;

(v) A statutory multifamily mortgage;

(vi) A securitization exposure;

(vii) An equity exposure; or

(viii) A debt security.

Repo-style transaction means a repurchase or reverse repurchase transaction, or a securities borrowing or securities lending transaction, including a transaction in which the [BANK] acts as agent for a customer and indemnifies the customer against loss, provided that:

(1) The transaction is based solely on liquid and readily marketable securities, cash, gold, or conforming residential mortgage exposures;

(2) The transaction is marked-to-market daily and subject to daily margin maintenance requirements;

(3) (i) The transaction is a “securities contract” or “repurchase agreement” under section 555 or 559, respectively, of the Bankruptcy Code (11 U.S.C. 555 or 559), a qualified financial contract under section 11(e)(8) of the Federal Deposit Insurance Act (12 U.S.C. 1821(e)(8)), or a netting contract between or among financial institutions under sections 401-407 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (12 U.S.C. 4401-4407) or the Federal Reserve Board’s Regulation EE (12 CFR part 231); or

(ii) If the transaction does not meet the criteria in paragraph (3)(i) of this definition, then either:

(A) The transaction is executed under an agreement that provides the [BANK] the right to accelerate, terminate, and close out the transaction on a net basis and to liquidate or set off collateral promptly upon an event of default (including upon an event of bankruptcy, insolvency, or similar proceeding) of the counterparty, provided that, in any such case, any exercise of rights under the agreement will not be stayed or avoided under applicable law in the relevant jurisdictions; or

(B) The transaction is:

(I) Either overnight or unconditionally cancelable at any time by the [BANK]; and

(II) Executed under an agreement that provides the [BANK] the right to accelerate, terminate, and close out the transaction on a net basis and to liquidate or set off collateral promptly upon an event of counterparty default; and

(4) The [BANK] has conducted sufficient legal review to conclude with a well-founded basis (and maintains sufficient written documentation of that legal review) that the agreement meets the requirements of paragraph (3) of this definition and is legal, valid, binding, and enforceable under applicable law in the relevant jurisdictions.

Residential mortgage exposure means an exposure (other than a pre-sold construction loan) that is primarily secured by one-to-four family residential property. (See also first-lien residential mortgage exposure, junior-lien residential mortgage exposure.)

Securities and Exchange Commission (SEC) means the U.S. Securities and Exchange Commission.

Securitization means a traditional securitization or a synthetic securitization.

Securitization exposure means an on-balance sheet or off-balance sheet credit exposure that arises from a traditional or synthetic securitization (including credit-enhancing representations and warranties). (See also synthetic securitization, traditional securitization.)

Securitization special purpose entity (securitization SPE) means a corporation, trust, or other entity organized for the specific purpose of holding underlying exposures of a securitization, the activities of which are limited to those appropriate to accomplish this purpose, and the structure of which is intended to isolate the underlying exposures held by the entity from the credit risk of the seller of the underlying exposures to the entity.

Servicer cash advance facility means a facility under which the servicer of the underlying exposures of a securitization may advance cash to ensure an uninterrupted flow of payments to

investors in the securitization, including advances made to cover foreclosure costs or other expenses to facilitate the timely collection of the underlying exposures. (See also eligible servicer cash advance facility.)

Sovereign entity means a central government (including the U.S. government) or an agency, department, ministry, or central bank of a central government.

Sovereign of incorporation means the country where an entity is incorporated, chartered, or similarly established.

Statutory multifamily mortgage means any multifamily residential mortgage that:

(1) Meets the requirements under section 618(b)(1) of the RTCRRI Act, and under 12 CFR part 3, appendix A, section 3(a)(3)(v) (for national banks); 12 CFR part 208, appendix A, section III.C.3. (for state member banks); 12 CFR part 225, appendix A, section III.C.3. (for bank holding companies); 12 CFR part 325, appendix A, section II.C. (for state nonmember banks); or 12 CFR 567.1 (definition of “qualifying multifamily mortgage loan”) and 12 CFR 567.6(a)(1)(iii) (for savings associations); and

(2) Is not on nonaccrual.

Subsidiary means, with respect to a company, a company controlled by that company.

Synthetic securitization means a transaction in which:

(1) All or a portion of the credit risk of one or more underlying exposures is transferred to one or more third parties through the use of one or more credit derivatives or guarantees (other than a guarantee that transfers only the credit risk of an individual retail exposure);

(2) The credit risk associated with the underlying exposures has been separated into at least two tranches reflecting different levels of seniority;

(3) Performance of the securitization exposures depends upon the performance of the underlying exposures; and

(4) All or substantially all of the underlying exposures are financial exposures (such as loans, commitments, credit derivatives, guarantees, receivables, asset-backed securities, mortgage-backed securities, other debt securities, or equity securities).

Tier 1 capital has the same meaning as in [the general risk-based capital rules], except as modified in part II of this appendix.

Tier 2 capital has the same meaning as in [the general risk-based capital rules], except as modified in part II of this appendix.

Total qualifying capital means the sum of tier 1 capital and tier 2 capital, after all deductions required in this appendix.

Total risk-weighted assets means the sum of a [BANK]'s:

(1) Total risk-weighted assets for general credit risk as calculated under section 31 of this appendix;

(2) Total risk-weighted assets for unsettled transactions as calculated under paragraph (f) of section 38 of this appendix;

(3) Total risk-weighted assets for securitization exposures as calculated under paragraph (b) of section 42 of this appendix;

(4) Total risk-weighted assets for equity exposures as calculated under paragraph (a) of section 52 of this appendix; and

(5) Risk-weighted assets for operational risk as calculated under section 61 of this appendix.

Traditional securitization means a transaction in which:

(1) All or a portion of the credit risk of one or more underlying exposures is transferred to one or more third parties other than through the use of credit derivatives or guarantees.

(2) The credit risk associated with the underlying exposures has been separated into at least two tranches reflecting different levels of seniority.

(3) Performance of the securitization exposures depends upon the performance of the underlying exposures.

(4) All or substantially all of the underlying exposures are financial exposures (such as loans, commitments, credit derivatives, guarantees, receivables, asset-backed securities, mortgage-backed securities, other debt securities, or equity securities).

(5) The underlying exposures are not owned by an operating company.

(6) The underlying exposures are not owned by a small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682).

(7) (i) For banks and bank holding companies, the underlying exposures are not owned by a firm an investment in which qualifies as a community development investment under 12 U.S.C. 24(Eleventh); or

(ii) For savings associations, the underlying exposures are not owned by a firm an investment in which is designed primarily to promote community welfare, including the welfare of low- and moderate-income communities or families, such as by providing services or employment.

(8) The [agency] may determine that a transaction in which the underlying exposures are owned by an investment firm that exercises substantially unfettered control over the size and composition of its assets, liabilities, and off-balance sheet exposures is not a traditional securitization based on the transaction's leverage, risk profile, or economic substance.

(9) The [agency] may deem a transaction that meets the definition of a traditional securitization, notwithstanding paragraph (5), (6), or (7) of this definition, to be a traditional securitization based on the transaction's leverage, risk profile, or economic substance.

Unconditionally cancelable means with respect to a commitment that a [BANK] may, at any time, with or without cause, refuse to extend credit under the facility (to the extent permitted under applicable law).

Underlying exposures means one or more exposures that have been securitized in a securitization transaction.

Value-at-Risk (VaR) means the estimate of the maximum amount that the value of one or more exposures could decline due to market price or rate movements during a fixed holding period within a stated confidence interval.

Section 3. Minimum Risk-Based Capital Requirements and Overall Capital Adequacy

(a) Except as modified by paragraph (c) of this section, each [BANK] must meet a minimum ratio of:

- (1) Total qualifying capital to total risk-weighted assets of 8.0 percent; and
- (2) Tier 1 capital to total risk-weighted assets of 4.0 percent.

(b) Each [BANK] must hold capital commensurate with the level and nature of all risks to which the [BANK] is exposed.

(c) When a [BANK] subject to [the market risk rule] calculates its risk-based capital requirements under this appendix, the [BANK] must also refer to [the market risk rule] for supplemental rules to calculate risk-based capital requirements adjusted for market risk.

(d) A [BANK] must have a rigorous process for assessing its overall capital adequacy in relation to its risk profile and a comprehensive strategy for maintaining an appropriate level of capital.

Section 4. Merger and Acquisition Transitional Arrangements

(a) Mergers and acquisitions of companies that use the general risk-based capital rules. If a [BANK] that uses this appendix merges with or acquires a company that uses the general risk-based capital rules (12 CFR part 3, appendix A; 12 CFR part 208, appendix A; 12 CFR part 225, appendix A; 12 CFR part 325, appendix A; or 12 CFR part 567, subpart B), the [BANK] may use the general risk-based capital rules to calculate the risk-weighted asset amounts for, and the deductions from capital associated with, the merged or acquired company's exposures for up to 12 months after the last day of the calendar quarter during which the merger or acquisition consummates. The risk-weighted assets of the merged or acquired company calculated under the general risk-based capital rules are included in the [BANK]'s total risk-weighted assets. Deductions associated with the exposures of the merged or acquired company are deducted from the [BANK]'s tier 1 capital and tier 2 capital. If a [BANK] relies on this paragraph, the [BANK] separately must disclose publicly the amounts of risk-weighted assets and total qualifying capital calculated under this appendix for the acquiring [BANK] and under the general risk-based capital rules for the acquired company.

(b) Mergers and acquisitions of companies that use the standardized risk-based capital rules. If a [BANK] that uses this appendix merges with or acquires a company that uses different aspects of the standardized risk-based capital rules (12 CFR part 3, appendix D; 12 CFR part 208, appendix G; 12 CFR part 225, appendix H; 12 CFR part 325, appendix E; or 12 CFR part 567, appendix B), the [BANK] may continue to use the merged or acquired company's systems

to determine the risk-weighted asset amounts for, and deductions from capital associated with, the merged or acquired company's exposures for up to 12 months after the last day of the calendar quarter during which the merger or acquisition consummates. The risk-weighted assets of the merged or acquired company are included in the [BANK]'s total risk-weighted assets. Deductions associated with the exposures of the merged or acquired company are deducted from the [BANK]'s tier 1 capital and tier 2 capital. If a [BANK] relies on this paragraph, the [BANK] separately must disclose publicly the amounts of risk-weighted assets and total qualifying capital for the acquiring [BANK] and for the merged or acquired company under the standardized risk-based capital rules.

(c) Mergers and acquisitions of companies that use the advanced approaches risk-based capital rules. If a [BANK] that uses this appendix merges with or acquires a company that uses the advanced approaches risk-based capital rules (12 CFR part 3, appendix C; 12 CFR part 208, appendix F; 12 CFR part 225, appendix G; 12 CFR part 325, appendix D; or 12 CFR part 567, appendix C), the [BANK] may use the advanced approaches risk-based capital rules to determine the risk-weighted asset amounts for, and deductions from capital associated with, the merged or acquired company's exposures for up to 12 months after the last day of the calendar quarter during which the merger or acquisition consummates. During the period when the advanced approaches risk-based capital rules apply to the merged or acquired company, any ALLL associated with the merged or acquired company's exposures must be excluded from the [BANK]'s tier 2 capital. Any excess eligible credit reserves associated with the merged or acquired company's exposures may be included in the acquiring [BANK]'s tier 2 capital up to 0.6 percent of the acquired company's risk-weighted assets. (Excess eligible credit reserves must be determined according to paragraph (a)(2) of section 13 of the advanced approaches risk-

based capital rules.) If a [BANK] relies on this paragraph, the [BANK] separately must disclose publicly the amounts of risk-weighted assets and qualifying capital calculated under this appendix for the acquiring [BANK] and under the advanced approaches risk-based capital rules for the acquired company.

Part II. Qualifying Capital

Section 21. Modifications to Tier 1 and Tier 2 Capital

(a) Modifications to tier 1 and tier 2 capital. A [BANK] that uses this appendix must make the same deductions from its tier 1 capital and tier 2 capital required in [the general risk-based capital rules], except that:

(1) A [BANK] is not required to make the deductions from capital for CEIOs in 12 CFR part 3, appendix A, section 2(c)(1)(iv) (for national banks); 12 CFR part 208, appendix A, section II.B.1.e. (for state member banks); 12 CFR part 225, appendix A, section II.B.1.e. (for bank holding companies); 12 CFR part 325, appendix A, section II.B.5. (for state nonmember banks); and 12 CFR 567.5(a)(2)(iii) and 567.12(e) (for savings associations);

(2) (i) A bank or bank holding company is not required to make the deductions from capital for nonfinancial equity investments in 12 CFR part 3, appendix A, section 2(c)(1)(v) (for national banks); 12 CFR part 208, appendix A, section II.B.5. (for state member banks); 12 CFR part 225, appendix A, section II.B.5. (for bank holding companies); and 12 CFR part 325, appendix A, section II.B. (for state nonmember banks);

(ii) A savings association is not required to deduct investments in equity securities from capital under 12 CFR 567.5(c)(2)(ii). However, it must continue to deduct equity investments in real estate under that section. See 12 CFR 567.1, which defines equity investments, including equity securities and equity investments in real estate; and

(3) A [BANK] must make the additional deductions from capital required by paragraphs (b) and (c) of this section.

(b) Deductions from tier 1 capital. In accordance with paragraph (a) of section 41 and paragraph (a)(1) of section 42, a [BANK] must deduct any after-tax gain-on-sale resulting from a securitization from tier 1 capital.

(c) Deductions from tier 1 and tier 2 capital. A [BANK] must deduct the exposures specified in paragraphs (c)(1) through (c)(3) in this section 50 percent from tier 1 capital and 50 percent from tier 2 capital. If the amount deductible from tier 2 capital exceeds the [BANK]'s actual tier 2 capital, however, the [BANK] must deduct the excess amount from tier 1 capital.

(1) Credit-enhancing interest-only strips (CEIOs). In accordance with paragraphs (a)(1) and (c) of section 42, any CEIO that does not constitute after-tax gain-on-sale.

(2) Certain securitization exposures. In accordance with paragraphs (a)(3) and (c) of section 42 and sections 43 and 44, certain securitization exposures that are required to be deducted from capital.

(3) Certain unsettled transactions. In accordance with paragraph (e)(3) of section 38, the [BANK]'s exposure on certain unsettled transactions.

Part III. Risk-Weighted Assets for General Credit Risk

Section 31. Mechanics for Calculating Risk-Weighted Assets for General Credit Risk

A [BANK] must risk weight its assets and exposures as follows:

(a) A [BANK] must determine the exposure amount of each on-balance sheet asset, each OTC derivative contract, and each off-balance sheet commitment, trade and transaction-related contingency, guarantee, repurchase agreement, securities lending and borrowing transaction, financial standby letter of credit, forward agreement, or other similar transaction that is not:

- (1) An unsettled transaction subject to section 38;
- (2) A securitization exposure; or
- (3) An equity exposure (other than an equity derivative contract).

(b) A [BANK] must multiply each exposure amount identified under paragraph (a) of this section by the risk weight appropriate to the exposure based on the obligor or exposure type, eligible guarantor, or financial collateral to determine the risk-weighted asset amount for each exposure.

(c) Total risk-weighted assets for general credit risk equals the sum of the risk-weighted asset amounts calculated under paragraph (b) of this section.

Section 32. Inferred Ratings for General Credit Risk

(a) General. This section describes two kinds of inferred ratings, an inferred rating based on an issuer rating and an inferred rating based on a specific issue. This section applies to an exposure to a sovereign entity, an exposure to a PSE, and a corporate exposure, except as otherwise provided in this appendix.

(b) Inferred rating based on an issuer rating. If a senior exposure to an obligor (that is, an exposure that ranks pari passu with an obligor's general creditors in the event of bankruptcy, insolvency, or other similar proceeding) has no external rating and the obligor has one or more issuer ratings, the senior exposure has inferred rating(s) equal to the issuer rating(s) of the obligor that reflects the currency in which the exposure is denominated.

(c) Inferred rating based on a specific issue. (1) An exposure with no external rating (the unrated exposure) has inferred rating(s) based on a specific issue equal to the external rating in paragraph (c)(1)(ii), if another exposure issued by the same obligor and secured by the same collateral (if any):

- (i) Ranks pari passu with the unrated exposure (or at the [BANK]'s option, is subordinated in all respects to the unrated exposure);
- (ii) Has an external rating based on a long-term rating;
- (iii) Does not benefit from any credit enhancement that is not available to the unrated exposure;
- (iv) Has an effective remaining maturity that is equal to or longer than that of the unrated exposure; and
- (v) Is denominated in the same currency as the unrated exposure. This requirement does not apply where the unrated exposure is denominated in a foreign currency that arises from a [BANK]'s participation in a loan extended or guaranteed by an MDB against convertibility and transfer risk. If the [BANK]'s participation is only partially guaranteed against convertibility and transfer risk by an MDB, the [BANK] may only use the external rating denominated in the foreign currency for the portion of the participation that benefits from the MDB's guarantee.

(2) An unrated exposure has inferred rating(s) equal to the external rating(s) based on any long-term rating of low-quality exposure(s) that are issued by the same obligor and that are senior in all respects to the unrated exposure. For the purposes of this paragraph, a low-quality exposure is an exposure that would receive a risk weight of 150 percent (for an exposure to a sovereign entity or a corporate exposure) or 100 percent or greater (for an exposure to a PSE) under section 33.

Section 33. General Risk Weights

(a) Exposures to sovereign entities. (1) A [BANK] must assign a risk weight to an exposure to a sovereign entity using the risk weight that corresponds to its applicable external or applicable inferred rating in Table 1.

(2) Notwithstanding paragraph (a)(1) of this section, a [BANK] may assign a risk weight that is lower than the applicable risk weight in Table 1 to an exposure to a sovereign entity if:

- (i) The exposure is denominated in the sovereign entity’s currency;
- (ii) The [BANK] has at least an equivalent amount of liabilities in that currency; and
- (iii) The sovereign entity allows banks under its jurisdiction to assign the lower risk weight to the same exposures to the sovereign entity.

Table 1 – Exposures to Sovereign Entities

Applicable external or applicable inferred rating of an exposure to a sovereign entity	Example	Risk weight (in percent)
Highest investment grade rating	AAA	0
Second-highest investment grade rating	AA	0
Third-highest investment grade rating	A	20
Lowest investment grade rating	BBB	50
One category below investment grade	BB	100
Two categories below investment grade	B	100
Three categories or more below investment grade	CCC	150
No applicable rating	N/A	100

(b) Certain supranational entities and multilateral development banks. A [BANK] may assign a zero percent risk weight to an exposure to the Bank for International Settlements, the European Central Bank, the European Commission, the International Monetary Fund, or an MDB.

(c) Exposures to depository institutions, foreign banks, and credit unions. (1) Except as provided in paragraph (c)(2) of this section, a [BANK] must assign a risk weight to an exposure to a depository institution, a foreign bank, or a credit union using the risk weight that corresponds to the lowest issuer rating of the entity’s sovereign of incorporation in Table 2.

(2) A [BANK] must assign a risk weight of at least 100 percent to an exposure to a depository institution or a foreign bank that is includable in the depository institution’s or foreign

bank’s regulatory capital and that is not subject to deduction as a reciprocal holding pursuant to 12 CFR part 3, appendix A, section 2(c)(6)(ii) (national banks); 12 CFR part 208, appendix A, section II.B.3 (state member banks); 12 CFR part 225, appendix A, section II.B.3 (bank holding companies); 12 CFR part 325, appendix A, section I.B.(4) (state nonmember banks); and 12 CFR part 567.5(c)(2)(i) (savings associations).

Table 2 – Exposures to Depository Institutions, Foreign Banks, and Credit Unions

Lowest issuer rating of the sovereign of incorporation	Example	Risk weight (in percent)
Highest investment grade rating	AAA	20
Second-highest investment grade rating	AA	20
Third-highest investment grade rating	A	50
Lowest investment grade rating	BBB	100
One category below investment grade	BB	100
Two categories below investment grade	B	100
Three categories or more below investment grade	CCC	150
No issuer rating	N/A	100

(d) Exposures to public sector entities. (1) Subject to the limitation in paragraph (d)(2) of this section, a [BANK]:

(i) Must risk weight an exposure to a PSE with an applicable external or applicable inferred rating based on a long-term rating using the risk weight that corresponds to the applicable external or applicable inferred rating based on a long-term rating in Table 3.

(ii) Must assign a 50 percent risk weight to an exposure to a PSE with no applicable external rating based on a long-term rating and no applicable inferred rating based on a long-term rating.

(iii) May assign a lower risk weight than would otherwise apply under Table 3 to an exposure to a foreign PSE if:

(A) The PSE’s sovereign of incorporation allows banks under its jurisdiction to assign the lower risk weight; and

(B) The risk weight is not lower than the risk weight that corresponds to the lowest issuer rating of the PSE’s sovereign of incorporation in Table 1.

(2) A [BANK] may not assign an exposure to a PSE with no external rating a risk weight that is lower than the risk weight that corresponds to the lowest issuer rating of the PSE’s sovereign of incorporation in Table 1.

Table 3 – Exposures to Public Sector Entities: Long-term Credit Rating

Applicable external or applicable inferred rating of an exposure to a PSE	Example	Risk weight (in percent)
Highest investment grade rating	AAA	20
Second-highest investment grade rating	AA	20
Third-highest investment grade rating	A	50
Lowest investment grade rating	BBB	50
One category below investment grade	BB	100
Two categories below investment grade	B	100
Three categories or more below investment grade	CCC	150
No applicable rating	N/A	50

(e) Corporate exposures. A [BANK] must use one of the following approaches to assign risk weights to corporate exposures:

(1) 100 percent risk weight approach. A [BANK] that chooses this approach must assign a 100 percent risk weight to all corporate exposures.

(2) Ratings approach. (i) Subject to the limitations in paragraph (e)(2)(ii) of this section, a [BANK] that chooses this approach:

(A) Must assign a risk weight to a corporate exposure with an applicable external or applicable inferred rating based on a long-term rating using the risk weight that corresponds to the applicable external or applicable inferred rating based on a long-term rating in Table 4.

(B) Must assign a risk weight to a corporate exposure with an applicable external rating based on a short-term rating using the risk weight that corresponds to the applicable external rating based on a short-term rating in Table 5.

(C) Must assign a 100 percent risk weight to all corporate exposures with no external rating and no inferred rating.

(ii) Limitations. (A) A [BANK] may not assign a corporate exposure with no external rating a risk weight that is lower than the risk weight that corresponds to the lowest issuer rating of the obligor’s sovereign of incorporation in Table 1.

(B) If an obligor has any exposure with an external rating based on a short-term rating that corresponds to a risk weight of 150 percent under Table 5, a [BANK] must assign a 150 percent risk weight to a corporate exposure to that obligor with no external rating and that ranks pari passu with or is subordinated to the externally rated exposure.

Table 4 – Corporate Exposures: Long-Term Credit Rating

Applicable external or applicable inferred rating of the corporate exposure	Example	Risk weight (in percent)
Highest investment grade rating	AAA	20
Second-highest investment grade rating	AA	20
Third-highest investment grade rating	A	50
Lowest investment grade rating	BBB	100
One category below investment grade	BB	100
Two categories below investment grade	B	150
Three categories or more below investment grade	CCC	150
No applicable rating	N/A	100

Table 5 – Corporate Exposures: Short-Term Credit Rating

Applicable external rating of the corporate exposure	Example	Risk weight (in percent)
Highest investment grade rating	A-1/P-1	20
Second-highest investment grade rating	A-2/P-2	50
Third-highest investment grade rating	A-3/P-3	100
Below investment grade	B, C and non-prime	150
No applicable external rating	N/A	100

(f) Regulatory retail exposures. A [BANK] must assign a 75 percent risk weight to a regulatory retail exposure.

(g) Residential mortgage exposures. (1) First-lien residential mortgage exposures. (i) A [BANK] must assign the applicable risk weight in Table 6, using the loan-to-value ratio (LTV ratio) as described in paragraph (g)(3) of this section, to a first-lien residential mortgage exposure that is secured by property that is owner-occupied or rented, is prudently underwritten, is not 90 days or more past due, and is not on nonaccrual. A first-lien residential mortgage exposure that has been restructured may receive a risk weight lower than 100 percent only if the [BANK] updates the LTV ratio at the time of restructuring as provided under paragraph (g)(3) of this section.

(ii) If a first-lien residential mortgage exposure does not satisfy these requirements, the [BANK] must assign a 100 percent risk weight to the exposure if the LTV ratio is 90 percent or less, and must assign a 150 percent risk weight if the LTV ratio is greater than 90 percent.

Table 6 – Risk Weights for First-Lien Residential Mortgage Exposures

Loan-to-value ratio (in percent)	Risk weight (in percent)
Less than or equal to 60	20
Greater than 60 and less than or equal to 80	35
Greater than 80 and less than or equal to 85	50
Greater than 85 and less than or equal to 90	75
Greater than 90 and less than or equal to 95	100
Greater than 95	150

(2) Junior-lien residential mortgage exposures. (i) A [BANK] must assign the applicable risk weight in Table 7, using the LTV ratio described in paragraph (g)(3) of this section, to a junior-lien residential mortgage exposure that is not 90 days or more past due or on nonaccrual.

(ii) If a junior-lien residential mortgage exposure is 90 days or more past due or on nonaccrual, a [BANK] must assign a 150 percent risk weight to the exposure.

Table 7 – Risk Weights for Junior-Lien Residential Mortgage Exposures

Loan-to-value ratio (in percent)	Risk weight (in percent)
Less than or equal to 60	75
Greater than 60 and less than or equal to 90	100
Greater than 90	150

(3) LTV ratio calculation. To determine the appropriate risk weight for a residential mortgage exposure under this paragraph (g), a [BANK] must calculate the LTV ratio (that is, the loan amount of the exposure divided by the value of the property) as described in this paragraph. A [BANK] must calculate a separate LTV ratio for the funded and unfunded portions of a residential mortgage exposure and must assign a risk weight to the exposure amount of each portion according to its respective LTV ratio.

(i) Loan amount for calculating the LTV ratio of the funded portion of a residential mortgage exposure.

(A) First-lien residential mortgage exposure. The loan amount of the funded portion of a first-lien residential mortgage exposure is the principal amount of the exposure.

(B) Junior-lien residential mortgage exposure. The loan amount of the funded portion of a junior-lien residential mortgage exposure is the principal amount of the exposure plus the principal amounts of all senior exposures secured by the same residential property on the date of origination of the junior-lien residential mortgage exposure plus the unfunded portion of the maximum contractual amount of any senior exposure(s) secured by the same residential property.

(ii) Loan amount for calculating the LTV ratio of the unfunded portion of a residential mortgage exposure. The loan amount of the unfunded portion of a residential mortgage exposure is:

(A) The amount calculated under paragraph (g)(3)(i) of this section; plus

(B) The unfunded portion of the maximum contractual amount of the exposure.

(iii) PMI. A [BANK] may reduce the loan amount in the LTV ratio up to the amount covered by loan-level private mortgage insurance (PMI). The loan-level PMI must protect the [BANK] in the event of borrower default up to a predetermined amount of the residential mortgage exposure, and may not have a pool-level cap that would effectively reduce coverage below the predetermined amount of the exposure. Loan-level PMI must be provided by a regulated mortgage insurance company that is not an affiliate of the [BANK], and that:

(A) Has issued long-term senior debt (without credit enhancement) that has an external rating that is in at least the third-highest investment grade rating category; or

(B) Has a claims-paying rating that is in at least the third-highest investment grade rating category.

(iv) Value. (A) The value of the property is the lesser of the actual acquisition cost (for a purchase transaction) or the estimate of the property's value at the origination of the loan or, at the [BANK]'s option, at the time of restructuring.

(B) A [BANK] must base all estimates of a property's value on an appraisal or evaluation of the property that satisfies subpart C of 12 CFR part 34 (national banks); subpart E of 12 CFR part 208 (state member banks); 12 CFR part 323 (state nonmember banks); and 12 CFR part 564 (savings associations).

(h) Pre-sold residential construction loans. A [BANK] must assign a 50 percent risk weight to a pre-sold construction loan unless the purchase contract is cancelled. A [BANK] must assign a 100 percent risk weight to such loan if the purchase contract is cancelled.

(i) Statutory multifamily mortgages. A [BANK] must assign a 50 percent risk weight to a statutory multifamily mortgage.

(j) Past due exposures. Except for a residential mortgage exposure, if an exposure is 90 days or more past due or on nonaccrual:

(1) A [BANK] must assign a 150 percent risk weight to the portion of the exposure that does not have a guarantee or that is unsecured.

(2) A [BANK] may assign a risk weight to the collateralized portion of the exposure based on the risk weight of the collateral under this section if the collateral meets the requirements of paragraph (b)(1) of section 37 of this appendix.

(3) A [BANK] may assign a risk weight to the guaranteed portion of the exposure based on the risk weight that would apply under section 36 of this appendix if the guarantee or credit derivative meets the requirements of that section.

(k) Other assets. (1) A [BANK] may assign a zero percent risk weight to cash owned and held in all offices of the [BANK] or in transit; to gold bullion held in the [BANK]'s own vaults or held in another depository institution's vaults on an allocated basis, to the extent the gold bullion assets are offset by gold bullion liabilities; and to derivative contracts that are publicly traded on an exchange that requires the daily receipt and payment of cash-variation margin.

(2) A [BANK] may assign a 20 percent risk weight to cash items in the process of collection.

(3) A [BANK] must apply a 100 percent risk weight to all assets not specifically assigned a different risk weight under this appendix (other than exposures that are deducted from tier 1 or tier 2 capital).

Section 34. Off-Balance Sheet Exposures

(a) General. (1) A [BANK] must calculate the exposure amount of an off-balance sheet exposure using the credit conversion factors (CCFs) in paragraph (b) of this section.

(2) Where a [BANK] commits to provide a commitment, the [BANK] may apply the lower of the two applicable CCFs.

(3) Where a [BANK] provides a commitment structured as a syndication or participation, the [BANK] is only required to calculate the exposure amount for its pro rata share of the commitment.

(b) Credit conversion factors. (1) Zero percent CCF. A [BANK] must apply a zero percent CCF to the unused portion of commitments that are unconditionally cancelable.

(2) 20 percent CCF. A [BANK] must apply a 20 percent CCF to the following off-balance-sheet exposures:

(i) Commitments with an original maturity of one year or less that are not unconditionally

cancelable.

(ii) Self-liquidating, trade-related contingent items that arise from the movement of goods, with an original maturity of one year or less.

(3) 50 percent CCF. A [BANK] must apply a 50 percent CCF to the following off-balance-sheet exposures:

(i) Commitments with an original maturity of more than one year that are not unconditionally cancelable by the [BANK].

(ii) Transaction-related contingent items, including performance bonds, bid bonds, warranties, and performance standby letters of credit.

(4) 100 percent CCF. A [BANK] must apply a 100 percent CCF to the following off-balance-sheet items and other similar transactions:

(i) Guarantees;

(ii) Repurchase agreements (the off-balance sheet component of which equals the sum of the current market values of all positions the [BANK] has sold subject to repurchase);

(iii) Off-balance sheet securities lending transactions (the off-balance sheet component of which equals the sum of the current market values of all positions the [BANK] has lent under the transaction);

(iv) Off-balance sheet securities borrowing transactions (the off-balance sheet component of which equals the sum of the current market values of all non-cash positions the [BANK] has posted as collateral under the transaction);

(v) Financial standby letters of credit; and

(vi) Forward agreements. Forward agreements are legally binding contractual obligations to purchase assets with certain drawdown at a specified future date. Such obligations do not include commitments to make residential mortgage loans or forward foreign exchange contracts.

Section 35. OTC Derivative Contracts

A [BANK] must calculate the exposure amount of an OTC derivative contract under this section.

(a) A [BANK] must determine the exposure amount for an OTC derivative contract that is not subject to a qualifying master netting agreement using the single OTC derivative contract calculation in paragraph (c) of this section.

(b) A [BANK] must determine the exposure amount for multiple OTC derivative contracts that are subject to a qualifying master netting agreement using the multiple OTC derivative contracts calculation in paragraph (d) of this section.

(c) Single OTC derivative contract. Except as modified by paragraph (e) of this section, the exposure amount for a single OTC derivative contract that is not subject to a qualifying master netting agreement is equal to the sum of the [BANK]'s current credit exposure and potential future credit exposure (PFE) on the derivative contract.

(1) Current credit exposure. The current credit exposure for a single OTC derivative contract is the greater of the mark-to-market value of the derivative contract or zero.

(2) PFE. The PFE for a single OTC derivative contract, including an OTC derivative contract with a negative mark-to-market value, is calculated by multiplying the notional principal amount of the derivative contract by the appropriate conversion factor in Table 8. For purposes of calculating either the PFE under this paragraph or the gross PFE under paragraph (d) of this section for exchange rate contracts and other similar contracts in which the notional principal

amount is equivalent to the cash flows, notional principal amount is the net receipts to each party falling due on each value date in each currency. For any OTC derivative contract that does not fall within one of the specified categories in Table 8, the PFE must be calculated using the appropriate “other” conversion factor. A [BANK] must use an OTC derivative contract’s effective notional principal amount (that is, its apparent or stated notional principal amount multiplied by any multiplier in the OTC derivative contract) rather than its apparent or stated notional principal amount in calculating PFE. PFE of the protection provider of a credit derivative is capped at the net present value of the amount of unpaid premiums.

Table 8 – Conversion Factor Matrix for OTC Derivative Contracts¹

Remaining maturity ²	Interest rate	Foreign exchange rate and gold	Credit (investment-grade reference obligor) ³	Credit (non-investment-grade reference obligor)	Equity	Precious metals (except gold)	Other
One year or less	0.00	0.01	0.05	0.10	0.06	0.07	0.10
Greater than one year and less than or equal to five years	0.005	0.05	0.05	0.10	0.08	0.07	0.12
Greater than five years	0.015	0.075	0.05	0.10	0.10	0.08	0.15

¹For an OTC derivative contract with multiple exchanges of principal, the conversion factor is multiplied by the number of remaining payments in the derivative contract.

²For an OTC derivative contract that is structured such that on specified dates any outstanding exposure is settled and the terms are reset so that the market value of the contract is zero, the remaining maturity equals the time until the next reset date. For an interest rate derivative contract with a remaining maturity of greater than one year that meets these criteria, the minimum conversion factor is 0.005.

³A [BANK] must use the column labeled “Credit (investment-grade reference obligor)” for a credit derivative whose reference obligor has an outstanding unsecured debt security that has an applicable external rating based on a long-term rating of at least investment grade without credit enhancement. A [BANK] must use the column labeled “Credit (non-investment grade reference obligor)” for all other credit derivatives.

(d) Multiple OTC derivative contracts subject to a qualifying master netting agreement.

Except as modified by paragraph (e) of this section, the exposure amount for multiple OTC derivative contracts subject to a qualifying master netting agreement is equal to the sum of the net current credit exposure and the adjusted sum of the PFE for all OTC derivative contracts subject to the qualifying master netting agreement.

(1) Net current credit exposure. The net current credit exposure is the greater of the net sum of all positive and negative mark-to-market values of the individual OTC derivative contracts subject to the qualifying master netting agreement or zero.

(2) Adjusted sum of the PFE. The adjusted sum of the PFE, A_{net} , is calculated as $A_{net} = (0.4 \times A_{gross}) + (0.6 \times NGR \times A_{gross})$, where:

(i) A_{gross} = the gross PFE (that is, the sum of the PFE amounts (as determined under paragraph (c)(2) of this section) for each individual OTC derivative contract subject to the qualifying master netting agreement); and

(ii) NGR = the net to gross ratio (that is, the ratio of the net current credit exposure to the gross current credit exposure). In calculating the NGR , the gross current credit exposure equals the sum of the positive current credit exposures (as determined under paragraph (c)(1) of this section) of all individual OTC derivative contracts subject to the qualifying master netting agreement.

(e) Collateralized OTC derivative contracts. A [BANK] may recognize the credit risk mitigation benefits of financial collateral that secures an OTC derivative contract or multiple OTC derivatives subject to a qualifying master netting agreement (netting set) by using the simple approach in paragraph (b) of section 37 of this appendix. Alternatively, a [BANK] may recognize the credit risk mitigation benefits of financial collateral that secures such a contract or

netting set if the financial collateral is marked-to-market on a daily basis and subject to a daily margin maintenance requirement by applying a risk weight to the exposure as if it is uncollateralized and adjusting the exposure amount calculated under paragraph (c) or (d) of this section using the collateral haircut approach in paragraph (c) of section 37 of this appendix. The [BANK] must substitute the exposure amount calculated under paragraph (c) or (d) of this section for $\sum E$ in the equation in paragraph (c)(3) of section 37 and must use a 10-business-day minimum holding period ($T_M=10$).

(f) Counterparty credit risk for credit derivatives. (1) A [BANK] that purchases a credit derivative that is recognized under section 36 as a credit risk mitigant for an exposure that is not a covered position under [the market risk rule] is not required to compute a separate counterparty credit risk capital requirement under section 31 provided that the [BANK] does so consistently for all such credit derivatives and either includes all or excludes all such credit derivatives that are subject to a qualifying master netting agreement from any measure used to determine counterparty credit risk exposure to all relevant counterparties for risk-based capital purposes.

(2) A [BANK] that is the protection provider in a credit derivative must treat the credit derivative as an exposure to the reference obligor and is not required to compute a counterparty credit risk capital requirement for the credit derivative under section 31 provided that it does so consistently for all such credit derivatives and either includes all or excludes all such credit derivatives that are subject to a qualifying master netting agreement from any measure used to determine counterparty credit risk exposure to all relevant counterparties for risk-based capital purposes (unless the [BANK] is treating the credit derivative as a covered position under [the market risk rule], in which case the [BANK] must compute a supplemental counterparty credit risk capital requirement under this section).

(g) Counterparty credit risk for equity derivatives. (1) A [BANK] must treat an equity derivative contract as an equity exposure and compute a risk-weighted asset amount for the equity derivative contract under part V of this appendix (unless the [BANK] is treating the contract as a covered position under [the market risk rule]).

(2) In addition, the [BANK] must also calculate a risk-based capital requirement for the counterparty credit risk of an equity derivative contract under this part if the [BANK] is treating the contract as a covered position under [the market risk rule].

(3) If the [BANK] risk weights the contract under the Simple Risk-Weight Approach (SRWA) in section 52 of this appendix, a [BANK] may choose not to hold risk-based capital against the counterparty credit risk of the equity derivative contract, as long as it does so for all such contracts. Where the equity derivative contracts are subject to a qualified master netting agreement, a [BANK] using the SRWA must either include all or exclude all of the contracts from any measure used to determine counterparty credit risk exposure.

Section 36. Guarantees and Credit Derivatives: Substitution Treatment

(a) Scope. (1) General. A [BANK] may recognize the credit risk mitigation benefits of an eligible guarantee or eligible credit derivative by substituting the risk weight associated with a protection provider for the risk weight assigned to an exposure, as provided under this section.

(2) This section applies to exposures for which:

- (i) Credit risk is fully covered by an eligible guarantee or eligible credit derivative; or
- (ii) Credit risk is covered on a pro rata basis (that is, on a basis in which the [BANK] and the protection provider share losses proportionately) by an eligible guarantee or eligible credit derivative.

(3) Exposures on which there is a tranching of credit risk (reflecting at least two different levels of seniority) generally are securitization exposures subject to the securitization framework in part IV of this appendix.

(4) If multiple eligible guarantees or eligible credit derivatives cover a single exposure described in paragraph (a)(2) of this section, a [BANK] may treat the hedged exposure as multiple separate exposures each covered by a single eligible guarantee or eligible credit derivative and may calculate a separate risk-weighted asset amount for each separate exposure as described in paragraph (c) of this section.

(5) If a single eligible guarantee or eligible credit derivative covers multiple hedged exposures described in paragraph (a)(2) of this section, a [BANK] must treat each hedged exposure as covered by a separate eligible guarantee or eligible credit derivative and must calculate a separate risk-weighted asset amount for each exposure as described in paragraph (c) of this section.

(6) If a [BANK] calculates the risk-weighted asset amount under section 31 for an exposure whose applicable external or applicable inferred rating reflects the benefits of a credit risk mitigant provided to the exposure, the [BANK] may not use the credit risk mitigation rules in this section to further reduce the risk-weighted asset amount for the exposure to reflect that credit risk mitigant.

(b) Rules of recognition. (1) A [BANK] may only recognize the credit risk mitigation benefits of eligible guarantees and eligible credit derivatives.

(2) A [BANK] may only recognize the credit risk mitigation benefits of an eligible credit derivative to hedge an exposure that is different from the credit derivative's reference exposure

used for determining the derivative's cash settlement value, deliverable obligation, or occurrence of a credit event if:

(i) The reference exposure ranks pari passu with or is subordinated to the hedged exposure; and

(ii) The reference exposure and the hedged exposure are to the same legal entity, and legally enforceable cross-default or cross-acceleration clauses are in place to assure payments under the credit derivative are triggered when the obligor fails to pay under the terms of the hedged exposure.

(c) Substitution approach. (1) Full coverage. If an eligible guarantee or eligible credit derivative meets the conditions in paragraphs (a) and (b) of this section and the protection amount (P) of the guarantee or credit derivative is greater than or equal to the exposure amount of the hedged exposure, a [BANK] may recognize the guarantee or credit derivative in determining the risk-weighted asset amount for the hedged exposure by substituting the risk weight applicable to the guarantee or credit derivative under section 33 for the risk weight assigned to the exposure. If the [BANK] determines that full substitution under this paragraph leads to an inappropriate degree of risk mitigation, the [BANK] may substitute a higher risk weight than that applicable to the guarantee or credit derivative.

(2) Partial coverage. If an eligible guarantee or eligible credit derivative meets the conditions in paragraphs (a) and (b) of this section and the protection amount (P) of the guarantee or credit derivative is less than the exposure amount of the hedged exposure, the [BANK] must treat the hedged exposure as two separate exposures (protected and unprotected) in order to recognize the credit risk mitigation benefit of the guarantee or credit derivative.

(i) The [BANK] may calculate the risk-weighted asset amount for the protected exposure under section 31 of this appendix, where the applicable risk weight is the risk weight applicable to the guarantee or credit derivative. If the [BANK] determines that full substitution under this paragraph leads to an inappropriate degree of risk mitigation, the [BANK] may use a higher risk weight than that applicable to the guarantee or credit derivative.

(ii) The [BANK] must calculate the risk-weighted asset amount for the unprotected exposure under section 31 of this appendix, where the applicable risk weight is that of the hedged exposure.

(iii) The treatment in this paragraph (c)(2) is applicable when the credit risk of an exposure is covered on a partial pro rata basis and may be applicable when an adjustment is made to the effective notional amount of the guarantee or credit derivative under paragraph (d), (e), or (f) of this section.

(d) Maturity mismatch adjustment. (1) A [BANK] that recognizes an eligible guarantee or eligible credit derivative in determining the risk-weighted asset amount for a hedged exposure must adjust the effective notional amount of the credit risk mitigant to reflect any maturity mismatch between the hedged exposure and the credit risk mitigant.

(2) A maturity mismatch occurs when the residual maturity of a credit risk mitigant is less than that of the hedged exposure(s).

(3) The residual maturity of a hedged exposure is the longest possible remaining time before the obligor is scheduled to fulfil its obligation on the exposure. If a credit risk mitigant has embedded options that may reduce its term, the [BANK] (protection purchaser) must use the shortest possible residual maturity for the credit risk mitigant. If a call is at the discretion of the protection provider, the residual maturity of the credit risk mitigant is at the first call date. If the

call is at the discretion of the [BANK] (protection purchaser), but the terms of the arrangement at origination of the credit risk mitigant contain a positive incentive for the [BANK] to call the transaction before contractual maturity, the remaining time to the first call date is the residual maturity of the credit risk mitigant. For example, where there is a step-up in cost in conjunction with a call feature or where the effective cost of protection increases over time even if credit quality remains the same or improves, the residual maturity of the credit risk mitigant will be the remaining time to the first call.

(4) A credit risk mitigant with a maturity mismatch may be recognized only if its original maturity is greater than or equal to one year and its residual maturity is greater than three months.

(5) When a maturity mismatch exists, the [BANK] must apply the following adjustment to reduce the effective notional amount of the credit risk mitigant: $P_m = E \times (t-0.25)/(T-0.25)$, where:

(i) P_m = effective notional amount of the credit risk mitigant, adjusted for maturity mismatch;

(ii) E = effective notional amount of the credit risk mitigant;

(iii) t = the lesser of T or the residual maturity of the credit risk mitigant, expressed in years; and

(iv) T = the lesser of five or the residual maturity of the hedged exposure, expressed in years.

(e) Adjustment for credit derivatives without restructuring as a credit event. If a [BANK] recognizes an eligible credit derivative that does not include as a credit event a restructuring of the hedged exposure involving forgiveness or postponement of principal, interest, or fees that

results in a credit loss event (that is, a charge-off, specific provision, or other similar debit to the profit and loss account), the [BANK] must apply the following adjustment to reduce the effective notional amount of the credit derivative: $Pr = Pm \times 0.60$, where:

(1) Pr = effective notional amount of the credit risk mitigant, adjusted for lack of restructuring event (and maturity mismatch, if applicable); and

(2) Pm = effective notional amount of the credit risk mitigant (adjusted for maturity mismatch, if applicable).

(f) Currency mismatch adjustment. (1) If a [BANK] recognizes an eligible guarantee or eligible credit derivative that is denominated in a currency different from that in which the hedged exposure is denominated, the [BANK] must apply the following formula to the effective notional amount of the guarantee or credit derivative: $Pc = Pr \times (1 - H_{FX})$, where:

(i) Pc = effective notional amount of the credit risk mitigant, adjusted for currency mismatch (and maturity mismatch and lack of restructuring event, if applicable);

(ii) Pr = effective notional amount of the credit risk mitigant (adjusted for maturity mismatch and lack of restructuring event, if applicable); and

(iii) H_{FX} = haircut appropriate for the currency mismatch between the credit risk mitigant and the hedged exposure.

(2) A [BANK] must set H_{FX} equal to eight percent unless it qualifies for the use of and uses its own internal estimates of foreign exchange volatility based on a 10-business-day holding period and daily marking-to-market and remargining. A [BANK] qualifies for the use of its own internal estimates of foreign exchange volatility if it qualifies for:

(i) The own-estimates haircuts in paragraph (c)(5) of section 37; or

(ii) The simple VaR methodology in paragraph (d) of section 37.

(3) A [BANK] must adjust H_{FX} calculated in paragraph (f)(2) of this section upward if the [BANK] revalues the guarantee or credit derivative less frequently than once every 10 business days using the following square root of time formula:

$$H_M = H_N \sqrt{\frac{T_M}{T_N}}, \text{ where}$$

- (i) T_M equals the greater of 10 or the number of days between revaluation;
- (ii) T_N equals the holding period used by the [BANK] to derive H_N ; and
- (iii) H_N equals the haircut based on the holding period T_N .

Section 37. Collateralized Transactions

(a) General. (1) This section provides three approaches that a [BANK] may use to recognize the risk-mitigating effects of financial collateral:

- (i) The simple approach. A [BANK] may use the simple approach for any exposure.
- (ii) The collateral haircut approach. A [BANK] may use the collateral haircut approach for repo-style transactions, eligible margin loans, collateralized OTC derivative contracts, and single-product netting sets of such transactions.
- (iii) The simple VaR methodology. A [BANK] may use the simple VaR methodology for single-product netting sets of repo-style transactions and eligible margin loans.

(2) A [BANK] may use any approach described in this section that is valid for a particular type of exposure or transaction; however, it must use the same approach for similar exposures or transactions.

(3) If a [BANK] calculates its risk-weighted asset amount under section 31 for an exposure whose applicable external or applicable inferred rating reflects the benefits of financial collateral to the exposure, the [BANK] may not use the credit risk mitigation rules in this section

to further reduce the risk-weighted asset amount for the exposure to reflect that financial collateral.

(b) The simple approach. (1) General requirements. (i) A [BANK] may recognize the credit risk mitigation benefits of financial collateral that secures any exposure or any collateral that secures a repo-style transaction that is included in the [BANK]'s VaR-based measure under [the market risk rule].

(ii) To qualify for the simple approach the collateral must meet the following requirements:

(A) The collateral must be subject to a collateral agreement for at least the life of the exposure;

(B) The collateral must be revalued at least every six months; and

(C) The collateral (other than gold) and the exposure must be denominated in the same currency.

(2) Risk weight substitution. (i) A [BANK] may risk weight the portion of an exposure that is secured by the market value of collateral (that meets the requirements of paragraph (b)(1) of this section) based on the risk weight assigned to the collateral under this appendix. For repurchase agreements, reverse repurchase agreements, and securities lending and borrowing transactions, the collateral is the instruments, gold, and cash the [BANK] has borrowed, purchased subject to resale, or taken as collateral from the counterparty under the transaction. Except as provided in paragraph (b)(3) of this section, the risk weight assigned to the collateralized portion of the exposure may not be less than 20 percent.

(ii) A [BANK] must risk weight the unsecured portion of the exposure based on the risk weight assigned to the exposure under this appendix.

(3) Exceptions to the 20 percent risk-weight floor and other requirements.

Notwithstanding paragraph (b)(2)(i) of this section:

(i) A [BANK] may assign a zero percent risk weight to an exposure to an OTC derivative contract that is marked-to-market on a daily basis and subject to a daily margin maintenance requirement, to the extent the contract is collateralized by cash on deposit.

(ii) A [BANK] may assign a 10 percent risk weight to an exposure to an OTC derivative contract that is marked-to-market on a daily basis and subject to a daily margin maintenance requirement, to the extent that the contract is collateralized by a sovereign security or a PSE security that qualifies for a zero percent risk weight under section 33 of this appendix.

(iii) A [BANK] may assign a zero percent risk weight to the collateralized portion of an exposure where:

(A) The financial collateral is cash on deposit; or

(B) The financial collateral is a sovereign security or a PSE security, the security qualifies for a zero percent risk weight under section 33, and the [BANK] has discounted the market value of the collateral by 20 percent.

(iv) If a [BANK] recognizes collateral in the form of a conforming residential mortgage, the [BANK] must risk weight the portion of the exposure that is secured by the conforming residential mortgage at 50 percent.

(c) Collateral haircut approach. (1) General. A [BANK] may recognize the credit risk mitigation benefits of financial collateral that secures an eligible margin loan, repo-style transaction, collateralized OTC derivative contract, or single-product netting set of such transactions, and of any collateral that secures a repo-style transaction that is included in the

[BANK]'s VaR-based measure under [the market risk rule] by using the collateral haircut approach in this paragraph (c).

(2) Approaches for the calculation of collateral haircuts. There are two ways to calculate collateral haircuts: the standard supervisory haircuts approach and the own internal estimates for haircuts approach. For exposures other than repo-style transactions included in the [BANK]'s VaR-based measure under the [the market risk rule], a [BANK] must use the standard supervisory haircut approach with a minimum 10-business-day holding period if it chooses to recognize in the exposure amount the benefits of collateral in the form of a conforming residential mortgage.

(3) Exposure amount equation. Under either collateral haircut approach, a [BANK] must determine the exposure amount for an eligible margin loan, repo-style transaction, collateralized OTC derivative contract, or a single-product netting set of such transactions by setting the exposure amount equal to $\max \{0, [(\sum E - \sum C) + \sum(E_s \times H_s) + \sum(E_{fx} \times H_{fx})]\}$, where:

(i)(A) For eligible margin loans and repo-style transactions, $\sum E$ equals the value of the exposure (the sum of the current market values of all instruments, gold, and cash the [BANK] has lent, sold subject to repurchase, or posted as collateral to the counterparty under the transaction (or netting set)); and

(B) For collateralized OTC derivative contracts and netting sets thereof, $\sum E$ equals the exposure amount of the OTC derivative contract (or netting set) calculated under paragraph (c) or (d) of section 35;

(ii) $\sum C$ equals the value of the collateral (the sum of the current market values of all instruments, gold and cash the [BANK] has borrowed, purchased subject to resale, or taken as collateral from the counterparty under the transaction (or netting set));

(iii) Es equals the absolute value of the net position in a given instrument or in gold (where the net position in a given instrument or in gold equals the sum of the current market values of the instrument or gold the [BANK] has lent, sold subject to repurchase, or posted as collateral to the counterparty minus the sum of the current market values of that same instrument or gold the [BANK] has borrowed, purchased subject to resale, or taken as collateral from the counterparty);

(iv) Hs equals the market price volatility haircut appropriate to the instrument or gold referenced in Es;

(v) Efx equals the absolute value of the net position of instruments and cash in a currency that is different from the settlement currency (where the net position in a given currency equals the sum of the current market values of any instruments or cash in the currency the [BANK] has lent, sold subject to repurchase, or posted as collateral to the counterparty minus the sum of the current market values of any instruments or cash in the currency the [BANK] has borrowed, purchased subject to resale, or taken as collateral from the counterparty); and

(vi) Hfx equals the haircut appropriate to the mismatch between the currency referenced in Efx and the settlement currency.

(4) Standard supervisory haircuts. Under the standard supervisory haircuts approach:

(i) A [BANK] must use the haircuts for market price volatility (Hs) in Table 9, as adjusted in certain circumstances as provided under in paragraph (c)(4)(iii) and (iv) of this section:

Table 9 – Standard Supervisory Market Price Volatility Haircuts¹

Applicable external rating grade category for debt securities	Residual maturity for debt securities	Sovereign entities ²	Other issuers
Two highest investment-grade rating categories for long-term ratings/highest investment-grade rating category for short-term ratings	≤ 1 year	0.005	0.01
	>1 year, ≤ 5 years	0.02	0.04
	> 5 years	0.04	0.08
Two lowest investment-grade rating categories for both short- and long-term ratings	≤ 1 year	0.01	0.02
	>1 year, ≤ 5 years	0.03	0.06
	> 5 years	0.06	0.12
One rating category below investment grade	All	0.15	0.25
Main index equities (including convertible bonds) and gold		0.15	
Other publicly traded equities (including convertible bonds), conforming residential mortgages, and nonfinancial collateral		0.25	
Mutual funds		Highest haircut applicable to any security in which the fund can invest	
Cash on deposit with the [BANK] (including a certificate of deposit issued by the [BANK])		0	

¹The market price volatility haircuts in Table 9 are based on a 10-business-day holding period.

²This column includes the haircuts for MDBs and foreign PSEs that receive a zero percent risk weight under section 33.

(ii) For currency mismatches, a [BANK] must use a haircut for foreign exchange rate volatility (Hfx) of 8.0 percent, as adjusted in certain circumstances as provided under paragraph (c)(4)(iii) and (iv) of this section.

(iii) For repo-style transactions, a [BANK] may multiply the standard supervisory haircuts provided in paragraphs (c)(4)(i) and (ii) of this section by the square root of $\frac{1}{2}$ (which equals 0.707107).

(iv) A [BANK] must adjust the standard supervisory haircuts provided in paragraphs (c)(4)(i) and (ii) of this section upward on the basis of a holding period longer than 10 business days (for eligible margin loans and OTC derivative contracts) or five business days (for repo-style transactions) where and as appropriate to take into account the illiquidity of an instrument.

(5) Own internal estimates for haircuts. With the prior written approval of the [agency], a [BANK] may calculate haircuts (H_s and H_{fx}) using its own internal estimates of the volatilities of market prices and foreign exchange rates.

(i) To receive [agency] approval to use its own internal estimates, a [BANK] must satisfy the following minimum quantitative standards:

(A) A [BANK] must use a 99th percentile one-tailed confidence interval.

(B) The minimum holding period for a repo-style transaction is five business days and for an eligible margin loan or OTC derivative contract is 10 business days. When a [BANK] calculates an own-estimates haircut on a T_N -day holding period, which is different from the minimum holding period for the transaction type, the applicable haircut (H_M) is calculated using the following square root of time formula:

$$H_M = H_N \sqrt{\frac{T_M}{T_N}}, \text{ where:}$$

(I) T_M equals 5 for repo-style transactions and 10 for eligible margin loans and OTC derivative contracts;

(II) T_N equals the holding period used by the [BANK] to derive H_N ; and

(III) H_N equals the haircut based on the holding period T_N .

(C) A [BANK] must adjust holding periods upward where and as appropriate to take into account the illiquidity of an instrument.

(D) The historical observation period must be at least one year.

(E) A [BANK] must update its data sets and recompute haircuts no less frequently than quarterly and must also reassess data sets and haircuts whenever market prices change materially.

(ii) With respect to debt securities that have an applicable external rating of investment grade, a [BANK] may calculate haircuts for categories of securities. For a category of securities, the [BANK] must calculate the haircut on the basis of internal volatility estimates for securities in that category that are representative of the securities in that category that the [BANK] has lent, sold subject to repurchase, posted as collateral, borrowed, purchased subject to resale, or taken as collateral. In determining relevant categories, the [BANK] must at a minimum take into account:

(A) The type of issuer of the security;

(B) The applicable external rating of the security;

(C) The maturity of the security; and

(D) The interest rate sensitivity of the security.

(iii) With respect to debt securities that have an applicable external rating of below investment grade and equity securities, a [BANK] must calculate a separate haircut for each individual security.

(iv) Where an exposure or collateral (whether in the form of cash or securities) is denominated in a currency that differs from the settlement currency, the [BANK] must calculate a separate currency mismatch haircut for its net position in each mismatched currency based on

estimated volatilities of foreign exchange rates between the mismatched currency and the settlement currency.

(v) A [BANK]'s own estimates of market price and foreign exchange rate volatilities may not take into account the correlations among securities and foreign exchange rates on either the exposure or collateral side of a transaction (or netting set) or the correlations among securities and foreign exchange rates between the exposure and collateral sides of the transaction (or netting set).

(d) Simple VaR methodology. (1) With the prior written approval of the [agency], a [BANK] may estimate the exposure amount for a single-product netting set of repo-style transactions or eligible margin loans using a VaR model that meets the requirements in paragraph (d)(3) of this section. However, a [BANK] may not use the VaR model described below to recognize in the exposure amount the benefits of collateral in the form of a conforming residential mortgage (other than for repo-style transactions included in the [BANK]'s VaR-based measure under [the market risk rule]).

(2) The [BANK] must set the exposure amount equal to $\max \{0, [(\sum E - \sum C) + PFE]\}$, where:

(i) $\sum E$ equals the value of the exposure (the sum of the current market values of all instruments, gold, and cash the [BANK] has lent, sold subject to repurchase, or posted as collateral to the counterparty under the netting set);

(ii) $\sum C$ equals the value of the collateral (the sum of the current market values of all instruments, gold, and cash the [BANK] has borrowed, purchased subject to resale, or taken as collateral from the counterparty under the netting set); and

(iii) PFE equals the [BANK]'s empirically based best estimate of the 99th percentile, one-tailed confidence interval for an increase in the value of $(\sum E - \sum C)$ over a five-business-day holding period for repo-style transactions or over a 10-business-day holding period for eligible margin loans using a minimum one-year historical observation period of price data representing the instruments that the [BANK] has lent, sold subject to repurchase, posted as collateral, borrowed, purchased subject to resale, or taken as collateral.

(3) The [BANK] must validate its VaR model, including by establishing and maintaining a rigorous and regular backtesting regime. For the purposes of this section, backtesting means a comparison of a [BANK]'s internal estimates with actual outcomes during a sample period not used in model development.

Section 38. Unsettled Transactions

(a) Definitions. For purposes of this section:

(1) Delivery-versus-payment (DvP) transaction means a securities or commodities transaction in which the buyer is obligated to make payment only if the seller has made delivery of the securities or commodities and the seller is obligated to deliver the securities or commodities only if the buyer has made payment.

(2) Payment-versus-payment (PvP) transaction means a foreign exchange transaction in which each counterparty is obligated to make a final transfer of one or more currencies only if the other counterparty has made a final transfer of one or more currencies.

(3) Qualifying central counterparty means a counterparty (for example, a clearing house) that:

(i) Facilitates trades between counterparties in one or more financial markets by either guaranteeing trades or novating contracts;

(ii) Requires all participants in its arrangements to be fully collateralized on a daily basis;
and

(iii) The [BANK] demonstrates to the satisfaction of the [agency] is in sound financial condition and is subject to effective oversight by a national supervisory authority.

(4) Normal settlement period. A transaction has a normal settlement period if the contractual settlement period for the transaction is equal to or less than the market standard for the instrument underlying the transaction and equal to or less than five business days.

(5) Positive current exposure. The positive current exposure of a [BANK] for a transaction is the difference between the transaction value at the agreed settlement price and the current market price of the transaction, if the difference results in a credit exposure of the [BANK] to the counterparty.

(b) Scope. This section applies to all transactions involving securities, foreign exchange instruments, and commodities that have a risk of delayed settlement or delivery. This section does not apply to:

(1) Transactions accepted by a qualifying central counterparty that are subject to daily marking-to-market and daily receipt and payment of variation margin;

(2) Repo-style transactions, including unsettled repo-style transactions;

(3) One-way cash payments on OTC derivative contracts; or

(4) Transactions with a contractual settlement period that is longer than the normal settlement period (which are treated as OTC derivative contracts as provided in section 35).

(c) System-wide failures. In the case of a system-wide failure of a settlement or clearing system, the [agency] may waive risk-based capital requirements for unsettled and failed transactions until the situation is rectified.

(d) Delivery-versus-payment (DvP) and payment-versus-payment (PvP) transactions. A [BANK] must hold risk-based capital against any DvP or PvP transaction with a normal settlement period if the [BANK]'s counterparty has not made delivery or payment within five business days after the settlement date. The [BANK] must determine its risk-weighted asset amount for such a transaction by multiplying the positive current exposure of the transaction for the [BANK] by the appropriate risk weight in Table 10.

Table 10 – Risk Weights for Unsettled DvP and PvP Transactions

Number of business days after contractual settlement date	Risk weight to be applied to positive current exposure (in percent)
From 5 to 15	100.0
From 16 to 30	625.0
From 31 to 45	937.5
46 or more	1,250.0

(e) Non-DvP/non-PvP (non-delivery-versus-payment/non-payment-versus-payment) transactions. (1) A [BANK] must hold risk-based capital against any non-DvP/non-PvP transaction with a normal settlement period if the [BANK] has delivered cash, securities, commodities, or currencies to its counterparty but has not received its corresponding deliverables by the end of the same business day. The [BANK] must continue to hold risk-based capital against the transaction until the [BANK] has received its corresponding deliverables.

(2) From the business day after the [BANK] has made its delivery until five business days after the counterparty delivery is due, the [BANK] must calculate the risk-weighted asset amount for the transaction by treating the current market value of the deliverables owed to the [BANK] as an exposure to the counterparty and using the applicable counterparty risk weight in section 33.

(3) If the [BANK] has not received its deliverables by the fifth business day after counterparty delivery was due, the [BANK] must deduct the current market value of the deliverables owed to the [BANK] 50 percent from tier 1 capital and 50 percent from tier 2 capital.

(f) Total risk-weighted assets for unsettled transactions. Total risk-weighted assets for unsettled transactions is the sum of the risk-weighted asset amounts of all DvP, PvP, and non-DvP/non-PvP transactions.

Part IV. Risk-Weighted Assets for Securitization Exposures

Section 41. Operational Requirements for Securitization Exposures

(a) Operational criteria for traditional securitizations. A [BANK] that transfers exposures it has originated or purchased to a securitization SPE or other third party in connection with a traditional securitization may exclude the exposures from the calculation of its risk-weighted assets only if each condition in this paragraph (a) is satisfied. A [BANK] that meets these conditions must hold risk-based capital against any securitization exposures it retains in connection with the securitization. A [BANK] that fails to meet these conditions must instead hold risk-based capital against the transferred exposures as if they had not been securitized and must deduct from tier 1 capital any after-tax gain-on-sale resulting from the transaction. The conditions are:

- (1) The transfer is considered a sale under GAAP;
- (2) The [BANK] has transferred to one or more third parties credit risk associated with the underlying exposures; and
- (3) Any clean-up calls relating to the securitization are eligible clean-up calls.

(b) Operational criteria for synthetic securitizations. For synthetic securitizations, a [BANK] may recognize for risk-based capital purposes the use of a credit risk mitigant to hedge underlying exposures only if each condition in this paragraph (b) is satisfied. A [BANK] that fails to meet these conditions must instead hold risk-based capital against the underlying exposures as if they had not been synthetically securitized. The conditions are:

(1) The credit risk mitigant is financial collateral, an eligible credit derivative, or an eligible guarantee;

(2) The [BANK] transfers credit risk associated with the underlying exposures to one or more third parties, and the terms and conditions in the credit risk mitigants employed do not include provisions that:

(i) Allow for the termination of the credit protection due to deterioration in the credit quality of the underlying exposures;

(ii) Require the [BANK] to alter or replace the underlying exposures to improve the credit quality of the pool of underlying exposures;

(iii) Increase the [BANK]'s cost of credit protection in response to deterioration in the credit quality of the underlying exposures;

(iv) Increase the yield payable to parties other than the [BANK] in response to a deterioration in the credit quality of the underlying exposures; or

(v) Provide for increases in a retained first loss position or credit enhancement provided by the [BANK] after the inception of the securitization;

(3) The [BANK] obtains a well-reasoned opinion from legal counsel that confirms the enforceability of the credit risk mitigant in all relevant jurisdictions; and

(4) Any clean-up calls relating to the securitization are eligible clean-up calls.

Section 42. Risk-Weighted Assets for Securitization Exposures

(a) Hierarchy of approaches. Except as provided elsewhere in this section or in section 41:

(1) A [BANK] must deduct from tier 1 capital any after-tax gain-on-sale resulting from a securitization and must deduct from total capital in accordance with paragraph (c) of this section the portion of any CEIO that does not constitute after-tax gain-on-sale.

(2) If a securitization exposure does not require deduction under paragraph (a)(1) of this section and qualifies for the Ratings-Based Approach (RBA) in section 43 of this appendix, a [BANK] must apply the RBA to the exposure.

(3) If a securitization exposure does not require deduction under paragraph (a)(1) of this section and does not qualify for the RBA, a [BANK] must apply the treatments in section 44.

(4) If a securitization exposure is an OTC derivative contract (other than a credit derivative) that has a first priority claim on the cash flows from the underlying exposures (notwithstanding amounts due under interest rate or currency derivative contracts, fees due, or other similar payments), with approval of the [agency], a [BANK] may choose to set the risk-weighted asset amount of the exposure equal to the amount of the exposure as determined in paragraph (d) of this section rather than apply the hierarchy of approaches described in paragraphs (a)(1) through (3) of this section.

(b) Total risk-weighted assets for securitization exposures. A [BANK]'s total risk-weighted assets for securitization exposures equals the sum of the risk-weighted asset amount for securitization exposures that the [BANK] risk weights under section 43, 44, or 45 of this appendix plus any risk-weighted asset amount calculated under section 46 of this appendix, as modified by paragraphs (e) through (k) of this section.

(c) Deductions. (1) If a [BANK] must deduct a securitization exposure from total capital, the [BANK] must take the deduction 50 percent from tier 1 capital and 50 percent from tier 2 capital. If the amount deductible from tier 2 capital exceeds the [BANK]'s tier 2 capital, the [BANK] must deduct the excess from tier 1 capital.

(2) A [BANK] may calculate any deduction from tier 1 capital and tier 2 capital for a securitization exposure net of any deferred tax liabilities associated with the securitization exposure.

(d) Exposure amount of a securitization exposure. (1) On-balance sheet securitization exposures. The exposure amount of an on-balance sheet securitization exposure that is not a repo-style transaction, eligible margin loan, or OTC derivative contract (other than a credit derivative) is:

(i) The [BANK]'s carrying value minus any unrealized gains and plus any unrealized losses on the exposure, if the exposure is a security classified as available-for-sale; or

(ii) The [BANK]'s carrying value, if the exposure is not a security classified as available-for-sale.

(2) Off-balance sheet securitization exposures. (i) The exposure amount of an off-balance sheet securitization exposure that is not a repo-style transaction or an OTC derivative contract (other than a credit derivative) is the notional amount of the exposure. For an off-balance sheet securitization exposure to an ABCP program, such as a liquidity facility, the notional amount may be reduced to the maximum potential amount that the [BANK] could be required to fund given the ABCP program's current underlying assets (calculated without regard to the current credit quality of those assets).

(ii) A [BANK] must determine the exposure amount of an eligible ABCP liquidity facility by multiplying the notional amount of the exposure by the appropriate CCF:

(A) 20 percent, for an eligible ABCP liquidity facility with an original maturity of one year or less that does not qualify for the RBA.

(B) 50 percent, for an eligible ABCP liquidity facility with an original maturity of over one year that does not qualify for the RBA.

(C) 100 percent, for an eligible ABCP liquidity facility that qualifies for the RBA.

(3) Repo-style transactions, eligible margin loans, and OTC derivative contracts. The exposure amount of a securitization exposure that is a repo-style transaction, eligible margin loan, or OTC derivative contract (other than a credit derivative) is the exposure amount of the transaction as calculated under section 35 or 37 of this appendix.

(e) Overlapping exposures. If a [BANK] has multiple securitization exposures that provide duplicative coverage to the underlying exposures of a securitization (such as when a [BANK] provides a program-wide credit enhancement and multiple pool-specific liquidity facilities to an ABCP program), the [BANK] is not required to hold duplicative risk-based capital against the overlapping position. Instead, the [BANK] may apply to the overlapping position the applicable risk-based capital treatment that results in the highest risk-based capital requirement.

(f) Implicit support. If a [BANK] provides support to a securitization in excess of the [BANK]'s contractual obligation to provide credit support to the securitization (implicit support):

(1) The [BANK] must hold regulatory capital against all of the underlying exposures associated with the securitization as if the exposures had not been securitized and must deduct from tier 1 capital any after-tax gain-on-sale resulting from the securitization; and

(2) The [BANK] must disclose publicly:

(i) That it has provided implicit support to the securitization; and

(ii) The regulatory capital impact to the [BANK] of providing such implicit support.

(g) Undrawn portion of an eligible servicer cash advance facility. Regardless of any other provision of this part, a [BANK] is not required to hold risk-based capital against the undrawn portion of an eligible servicer cash advance facility.

(h) Interest-only mortgage-backed securities. Regardless of any other provisions of this part, the risk weight for a non-credit-enhancing interest-only mortgage-backed security may not be less than 100 percent.

(i) Small-business loans and leases on personal property transferred with recourse. (1) Regardless of any other provisions of this appendix, a [BANK] that has transferred small-business loans and leases on personal property (small-business obligations) with recourse must include in risk-weighted assets only the contractual amount of retained recourse if all the following conditions are met:

(i) The transaction is a sale under GAAP.

(ii) The [BANK] establishes and maintains, pursuant to GAAP, a non-capital reserve sufficient to meet the [BANK]'s reasonably estimated liability under the recourse arrangement.

(iii) The loans and leases are to businesses that meet the criteria for a small-business concern established by the Small Business Administration under section 3(a) of the Small Business Act (15 U.S.C. 632).

(iv) The [BANK] is well capitalized, as defined in the [agency]'s prompt corrective action regulation -- 12 CFR part 6 (for national banks); 12 CFR part 208, subpart D (for state member banks or bank holding companies); 12 CFR part 325, subpart B (for state nonmember banks); and 12 CFR part 565 (for savings associations). For purposes of determining whether a [BANK] is well capitalized for purposes of this paragraph, the [BANK]'s capital ratios must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in this paragraph (i)(1).

(2) The total outstanding amount of recourse retained by a [BANK] on transfers of small-business obligations receiving the capital treatment specified in paragraph (i)(1) of this section cannot exceed 15 percent of the [BANK]'s total qualifying capital.

(3) If a [BANK] ceases to be well capitalized or exceeds the 15 percent capital limitation, the capital treatment specified in paragraph (i)(1) of this section will continue to apply to any transfers of small-business obligations with recourse that occurred during the time that the [BANK] was well capitalized and did not exceed the capital limit.

(4) The risk-based capital ratios of the [BANK] must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section as provided in 12 CFR part 3, appendix A (for national banks); 12 CFR part 208, appendix A (for state member banks); 12 CFR part 225, appendix A (for bank holding companies); 12 CFR part 325, appendix A (for state nonmember banks); and 12 CFR 567.6(b)(5)(v) (for savings associations).

(j) Consolidated ABCP programs. (1) A [BANK] that qualifies as a primary beneficiary and must consolidate an ABCP program as a variable interest entity under GAAP may exclude the consolidated ABCP program assets from risk-weighted assets if the [BANK] is the sponsor

of the ABCP program. If a [BANK] excludes such consolidated ABCP program assets from risk-weighted assets, the [BANK] must hold risk-based capital against any securitization exposures of the [BANK] to the ABCP program in accordance with this part.

(2) If a [BANK] either is not permitted, or elects not, to exclude consolidated ABCP program assets from its risk-weighted assets, the [BANK] must hold risk-based capital against the consolidated ABCP program assets in accordance with this appendix but is not required to hold risk-based capital against any securitization exposures of the [BANK] to the ABCP program.

(k) Nth-to-default credit derivatives. (1) First-to-default credit derivatives. (i) Protection purchaser. A [BANK] that obtains credit protection on a group of underlying exposures through a first-to-default credit derivative must determine its risk-based capital requirement for the underlying exposures as if the [BANK] synthetically securitized the underlying exposure with the lowest risk-based capital requirement and had obtained no credit risk mitigant on the other underlying exposures.

(ii) Protection provider. A [BANK] that provides credit protection on a group of underlying exposures through a first-to-default credit derivative must determine its risk-weighted asset amount for the derivative by applying the RBA or, if the derivative does not qualify for the RBA, by setting its risk-weighted asset amount for the derivative equal to the product of:

(A) The protection amount of the derivative; and

(B) The sum of the risk weights of the individual underlying exposures, up to a maximum of 1,250 percent.

(2) Second-or-subsequent-to-default credit derivatives. (i) Protection purchaser. (A) A [BANK] that obtains credit protection on a group of underlying exposures through an nth-to-

default credit derivative (other than a first-to-default credit derivative) may recognize the credit risk mitigation benefits of the derivative only if:

(I) The [BANK] also has obtained credit protection on the same underlying exposures in the form of first-through-(n-1)-to-default credit derivatives; or

(II) If n-1 of the underlying exposures have already defaulted.

(B) If a [BANK] satisfies the requirements of paragraph (k)(2)(i)(A) of this section, the [BANK] must determine its risk-based capital requirement for the underlying exposures as if the [BANK] had only synthetically securitized the underlying exposure with the nth lowest risk-based capital requirement and had obtained no credit risk mitigant on the other underlying exposures.

(ii) Protection provider. A [BANK] that provides credit protection on a group of underlying exposures through an nth-to-default credit derivative (other than a first-to-default credit derivative) must determine its risk-weighted asset amount for the derivative by applying the RBA in section 43 of this appendix (if the derivative qualifies for the RBA) or, if the derivative does not qualify for the RBA, by setting its risk-weighted asset amount for the derivative equal to the product of:

(A) The protection amount of the derivative; and

(B) The sum of the risk weights of the individual underlying exposures (excluding the n-1 underlying exposures with the lowest risk-based capital requirement), up to a maximum of 1,250 percent.

Section 43. Ratings-Based Approach (RBA)

(a) Eligibility requirements for use of the RBA. (1) Originating [BANK]. An originating [BANK] must use the RBA to calculate its risk-based capital requirement for a securitization

exposure if the exposure has two or more external or inferred ratings (and may not use the RBA if the exposure has fewer than two external or inferred ratings).

(2) Investing [BANK]. An investing [BANK] must use the RBA to calculate the risk-based capital requirement for a securitization exposure if the exposure has one or more external or inferred ratings (and may not use the RBA if the exposure has no external rating or inferred rating).

(b) Ratings-based approach. (1) A [BANK] must determine its risk-based capital requirement for a securitization exposure not required to be deducted under Table 11 or 12 by multiplying the exposure amount (as determined in paragraph (d) of section 42) by the risk weight that corresponds to the applicable external or applicable inferred rating provided in Table 11 or 12. If the applicable table requires deduction, the exposure amount must be deducted from total capital in accordance with paragraph (c) of section 42.

(2) A [BANK] must apply the risk weights in Table 11 when the securitization exposure's applicable external or applicable inferred rating represents a long-term credit rating, and must apply the risk weights in Table 12 when the securitization exposure's applicable external or applicable inferred rating represents a short-term credit rating.

Table 11 – Long-term Credit Rating Risk Weights under the RBA

Applicable external or applicable inferred rating of a securitization exposure	Example	Risk Weight (in percent)
Highest investment grade rating	AAA	20
Second-highest investment grade rating	AA	20
Third-highest investment grade rating	A	50
Lowest investment grade rating	BBB	100
One category below investment grade	BB	350
Two categories below investment grade	B	Deduction
Three categories or more below investment grade	CCC	Deduction

Table 12 – Short-term Credit Rating Risk Weights under the RBA

Applicable external or applicable inferred rating of a securitization exposure	Example	Risk Weight (in percent)
Highest investment grade rating	A-1/P-1	20
Second-highest investment grade rating	A-2/P-2	50
Third-highest investment grade rating	A-3/P-3	100
All other ratings	N/A	Deduction

Section 44. Securitization Exposures That Do Not Qualify for the RBA

A [BANK] must deduct from total capital all securitization exposures that do not qualify for the RBA in section 43 of this appendix with the following exceptions, provided that the [BANK] knows the composition of the underlying exposures at all times:

(a) An eligible ABCP liquidity facility. A [BANK] may determine the risk-weighted asset amount of an eligible ABCP liquidity facility by multiplying the exposure amount by the highest risk weight applicable to any of the individual underlying exposures covered by the facility.

(b) A first priority securitization exposure. A [BANK] may determine the risk-weighted asset amount of a first priority securitization exposure by multiplying the exposure amount by the weighted-average risk weight of the underlying exposures. For purposes of this section, a first priority securitization exposure is a securitization exposure that has a first priority claim on the cash flows from the underlying exposures and that is not an eligible ABCP liquidity facility. When determining whether a securitization exposure has a first priority claim on the cash flows from the underlying exposures, a [BANK] is not required to consider amounts due under interest rate or currency derivative contracts, fees due, or other similar payments.

(c) A securitization exposure in a second loss position or better in an ABCP program. (1)

A [BANK] may determine the risk-weighted asset amount of a securitization exposure that is in a second loss position or better in an ABCP program that meets the requirements of paragraph (c)(2) of this section by multiplying the exposure amount by the higher of the following risk weights:

(i) 100 percent; or

(ii) The highest risk weight applicable to any of the individual underlying exposures of the ABCP program.

(2) Requirements. (i) The exposure is not a first priority securitization exposure or an eligible ABCP liquidity facility;

(ii) The exposure must be economically in a second loss position or better, and the first loss position must provide significant credit protection to the second loss position;

(iii) The credit risk of the exposure must be the equivalent of investment grade or better; and

(iv) The [BANK] holding the exposure must not retain or provide the first loss position.

Section 45. Recognition of Credit Risk Mitigants for Securitization Exposures

(a) General. (1) An originating [BANK] that has obtained a credit risk mitigant to hedge its securitization exposure to a synthetic or traditional securitization that satisfies the operational criteria in section 41 of this appendix may recognize the credit risk mitigant under section 36 or 37 of this appendix, but only as provided in this section.

(2) An investing [BANK] that has obtained a credit risk mitigant to hedge a securitization exposure may recognize the credit risk mitigant under section 36 or 37 of this appendix, but only as provided in this section.

(3) A [BANK] that has used section 43 or section 44 to calculate its risk-based capital requirement for a securitization exposure based on external or inferred ratings that reflect the benefits of a credit risk mitigant provided to the associated securitization or that supports some or all of the underlying exposures may not use the credit risk mitigation rules in this section to further reduce its risk-based capital requirement for the exposure to reflect that credit risk mitigant.

(b) Eligible guarantors for securitization exposures. A [BANK] may only recognize an eligible guarantee or eligible credit derivative from an eligible guarantor that:

(1) Is described in paragraph (1) of the definition of eligible guarantor; or

(2) Has issued and outstanding an unsecured debt security without credit enhancement that has an applicable external rating based on a long-term rating in one of the three highest investment grade rating categories.

(c) Mismatches. A [BANK] must make applicable adjustments to the protection amount of an eligible guarantee or credit derivative as required in paragraphs (d), (e), and (f) of section 36 of this appendix for any hedged securitization exposure. In the context of a synthetic securitization, when an eligible guarantee or eligible credit derivative covers multiple hedged exposures that have different residual maturities, the [BANK] must use the longest residual maturity of any of the hedged exposures as the residual maturity of all the hedged exposures.

Section 46. Risk-Weighted Assets for Securitizations with Early Amortization Provisions

(a) General. (1) An originating [BANK] must hold risk-based capital against the sum of the originating [BANK]'s interest and the investors' interest in a securitization that:

(i) Includes one or more underlying exposures in which the borrower is permitted to vary the drawn amount within an agreed limit under a line of credit; and

(ii) Contains an early amortization provision.

(2) The total capital requirement for a [BANK]'s exposures to a single securitization with an early amortization provision is subject to a maximum capital requirement equal to the greater of:

(i) The capital requirement for retained securitization exposures, or

(ii) The capital requirement for the underlying exposures that would apply if the [BANK] directly held the underlying exposures.

(3) For securitizations described in paragraph (a)(1) of this section, an originating [BANK] must calculate the risk-based capital requirement for the originating [BANK]'s interest under sections 42-45, and the risk-weighted asset amount for the investors' interest under paragraph (c) of this section.

(b) Definitions. For purposes of this section:

(1) Investors' interest means, with respect to a securitization, the exposure amount of the underlying exposures multiplied by the ratio of:

(i) The total amount of securitization exposures issued by the securitization SPE; divided by

(ii) The outstanding principal amount of the underlying exposures.

(2) Excess spread for a period means:

(i) Gross finance charge collections and other income received by a securitization SPE (including market interchange fees) over a period minus interest paid to the holders of the securitization exposures, servicing fees, charge-offs, and other senior trust or similar expenses of the SPE over the period; divided by

(ii) The principal balance of the underlying exposures at the end of the period.

(c) Risk-weighted asset amount for investors' interest. The originating [BANK]'s risk-weighted asset amount for the investors' interest in the securitization is equal to the product of the following four quantities:

- (1) The investors' interest;
- (2) The appropriate conversion factor in paragraph (d) of this section;
- (3) The weighted-average risk weight that would apply under this appendix to the underlying exposures if the underlying exposures had not been securitized; and
- (4) The proportion of the underlying exposures in which the borrower is permitted to vary the drawn amount within an agreed limit under a line of credit.

(d) Conversion factors. (1) (i) Except as provided in paragraph (d)(2) of this section, to calculate the appropriate conversion factor, a [BANK] must use Table 13 for a securitization that contains a controlled early amortization provision and must use Table 14 for a securitization that contains a non-controlled early amortization provision. In circumstances where a securitization contains a mix of retail and nonretail exposures or a mix of committed and uncommitted exposures, a [BANK] may take a pro rata approach to determining the conversion factor for the securitization's early amortization provision. If a pro rata approach is not feasible, a [BANK] must treat the mixed securitization as a securitization of nonretail exposures if a single underlying exposure is a nonretail exposure and must treat the mixed securitization as a securitization of committed exposures if a single underlying exposure is a committed exposure.

(ii) To find the appropriate conversion factor in the tables, a [BANK] must divide the three-month average annualized excess spread of the securitization by the excess spread trapping point in the securitization structure. In securitizations that do not require excess spread to be

trapped, or that specify trapping points based primarily on performance measures other than the three-month average annualized excess spread, the excess spread trapping point is 4.5 percent.

Table 13 – Controlled Early Amortization Provisions

	3-month average annualized excess spread	Uncommitted CF (in percent)	Committed CF (in percent)
Retail Credit Lines	Greater than or equal to 133.33% of trapping point	0	90
	Less than 133.33% to 100% of trapping point	1	
	Less than 100% to 75% of trapping point	2	
	Less than 75% to 50% of trapping point	10	
	Less than 50% to 25% of trapping point	20	
	Less than 25% of trapping point	40	
Non-retail credit lines		90	90

Table 14 – Non-controlled Early Amortization Provisions

	3-month average annualized excess spread	Uncommitted CF (in percent)	Committed CF (in percent)
Retail Credit Lines	Greater than or equal to 133.33% of trapping point	0	100
	Less than 133.33% to 100% of trapping point	5	
	Less than 100% to 75% of trapping point	15	
	Less than 75% to 50% of trapping point	50	
	Less than 50% of trapping point	100	
Non-retail credit lines		100	100

(2) For a securitization for which all or substantially all of the underlying exposures are secured by liens on one-to-four family residential property, a [BANK] may calculate the appropriate conversion factor discussed in paragraph (c)(2) of this section using paragraph (d)(1) of this section or may use a conversion factor of 10 percent. If the [BANK] chooses to use a conversion factor of 10 percent, it must use that conversion factor for all securitizations for which all or substantially all of the underlying exposures are secured by liens on one-to-four family residential property.

Part V. Risk-Weighted Assets for Equity Exposures

Section 51. Introduction and Exposure Measurement

(a) General. To calculate its risk-weighted asset amounts for equity exposures that are not equity exposures to investment funds, a [BANK] must use the Simple Risk-Weight Approach (SRWA) in section 52. A [BANK] must use the look-through approaches in section 53 to calculate its risk-weighted asset amounts for equity exposures to investment funds.

(b) Adjusted carrying value. For purposes of this part, the adjusted carrying value of an equity exposure is:

(1) For the on-balance sheet component of an equity exposure, the [BANK]'s carrying value of the exposure reduced by any unrealized gains on the exposure that are reflected in such carrying value but excluded from the [BANK]'s tier 1 and tier 2 capital; and

(2) For the off-balance sheet component of an equity exposure that is not an equity commitment, the effective notional principal amount of the exposure, the size of which is equivalent to a hypothetical on-balance sheet position in the underlying equity instrument that would evidence the same change in fair value (measured in dollars) for a given small change in the price of the underlying equity instrument, minus the adjusted carrying value of the on-balance sheet component of the exposure as calculated in paragraph (b)(1) of this section.

(3) For a commitment to acquire an equity exposure (an equity commitment), the effective notional principal amount of the exposure multiplied by the following conversion factors (CFs):

(i) Conditional equity commitments with an original maturity of one year or less receive a CF of 20 percent.

(ii) Conditional equity commitments with an original maturity of over one year receive a

CF of 50 percent.

(iii) Unconditional equity commitments receive a CF of 100 percent.

Section 52. Simple Risk-Weight Approach (SRWA)

(a) General. Under the SRWA, a [BANK]'s total risk-weighted assets for equity exposures equals the sum of the risk-weighted asset amounts for each of the [BANK]'s individual equity exposures (other than equity exposures to an investment fund) as determined in this section and the risk-weighted asset amounts for each of the [BANK]'s individual equity exposures to an investment fund as determined in section 53.

(b) SRWA computation for individual equity exposures. A [BANK] must determine the risk-weighted asset amount for an individual equity exposure (other than an equity exposure to an investment fund) by multiplying the adjusted carrying value of the equity exposure or the effective portion and ineffective portion of a hedge pair (as defined in paragraph (c) of this section) by the lowest applicable risk weight in this paragraph (b).

(1) Zero percent risk weight equity exposures. An equity exposure to a sovereign entity, the Bank for International Settlements, the European Central Bank, the European Commission, the International Monetary Fund, an MDB, a PSE, and any other entity whose credit exposures receive a zero percent risk weight under section 33 may be assigned a zero percent risk weight.

(2) 20 percent risk weight equity exposures. An equity exposure to a Federal Home Loan Bank or Federal Agricultural Mortgage Corporation (Farmer Mac) is assigned a 20 percent risk weight.

(3) 100 percent risk weight equity exposures. The following equity exposures are assigned a 100 percent risk weight:

(i) Community development equity exposures.

(A) For banks and bank holding companies, an equity exposure that qualifies as a community development investment under 12 U.S.C. 24(Eleventh), excluding equity exposures to an unconsolidated small business investment company and equity exposures held through a consolidated small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682).

(B) For savings associations, an equity exposure that is designed primarily to promote community welfare, including the welfare of low- and moderate-income communities or families, such as by providing services or employment, and excluding equity exposures to an unconsolidated small business investment company and equity exposures held through a small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682).

(ii) Effective portion of hedge pairs. The effective portion of a hedge pair.

(iii) Non-significant equity exposures. Equity exposures, excluding exposures to an investment firm that would meet the definition of a traditional securitization were it not for the [agency]'s application of paragraph (8) of that definition and has greater than immaterial leverage, to the extent that the aggregate adjusted carrying value of the exposures does not exceed 10 percent of the [BANK]'s tier 1 capital plus tier 2 capital.

(A) To compute the aggregate adjusted carrying value of a [BANK]'s equity exposures for purposes of this paragraph (b)(3)(iii), the [BANK] may exclude equity exposures described in paragraphs (b)(1), (b)(2), (b)(3)(i), and (b)(3)(ii) of this section, the equity exposure in a hedge pair with the smaller adjusted carrying value, and a proportion of each equity exposure to an investment fund equal to the proportion of the assets of the investment fund that are not equity exposures or that meet the criterion of paragraph (b)(3)(i) of this section. If a [BANK] does not

know the actual holdings of the investment fund, the [BANK] may calculate the proportion of the assets of the fund that are not equity exposures based on the terms of the prospectus, partnership agreement, or similar contract that defines the fund's permissible investments. If the sum of the investment limits for all exposure classes within the fund exceeds 100 percent, the [BANK] must assume for purposes of this paragraph (b)(3)(iii) that the investment fund invests to the maximum extent possible in equity exposures.

(B) When determining which of a [BANK]'s equity exposures qualify for a 100 percent risk weight under this paragraph, a [BANK] first must include equity exposures to unconsolidated small business investment companies or held through consolidated small business investment companies described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682), then must include publicly traded equity exposures (including those held indirectly through investment funds), and then must include non-publicly traded equity exposures (including those held indirectly through investment funds).

(4) 300 percent risk weight equity exposures. A publicly traded equity exposure (other than an equity exposure described in paragraph (b)(6) of this section and including the ineffective portion of a hedge pair) is assigned a 300 percent risk weight.

(5) 400 percent risk weight equity exposures. An equity exposure (other than an equity exposure described in paragraph (b)(6) of this section) that is not publicly traded is assigned a 400 percent risk weight.

(6) 600 percent risk weight equity exposures. An equity exposure to an investment firm that:

(i) Would meet the definition of a traditional securitization were it not for the [agency]'s application of paragraph (8) of that definition, and

(ii) Has greater than immaterial leverage is assigned a 600 percent risk weight.

(c) Hedge transactions. (1) Hedge pair. A hedge pair is two equity exposures that form an effective hedge so long as each equity exposure is publicly traded or has a return that is primarily based on a publicly traded equity exposure.

(2) Effective hedge. Two equity exposures form an effective hedge if the exposures either have the same remaining maturity or each has a remaining maturity of at least three months; the hedge relationship is formally documented in a prospective manner (that is, before the [BANK] acquires at least one of the equity exposures); the documentation specifies the measure of effectiveness (E) the [BANK] will use for the hedge relationship throughout the life of the transaction; and the hedge relationship has an E greater than or equal to 0.8. A [BANK] must measure E at least quarterly and must use one of three alternative measures of E:

(i) Under the dollar-offset method of measuring effectiveness, the [BANK] must determine the ratio of value change (RVC). The RVC is the ratio of the cumulative sum of the periodic changes in value of one equity exposure to the cumulative sum of the periodic changes in the value of the other equity exposure. If RVC is positive, the hedge is not effective and E equals 0. If RVC is negative and greater than or equal to -1 (that is, between zero and -1), then E equals the absolute value of RVC. If RVC is negative and less than -1, then E equals 2 plus RVC.

(ii) Under the variability-reduction method of measuring effectiveness:

$$E = 1 - \frac{\sum_{t=1}^T (X_t - X_{t-1})^2}{\sum_{t=1}^T (A_t - A_{t-1})^2}, \text{ where}$$

(A) $X_t = A_t - B_t$;

(B) A_t = the value at time t of one exposure in a hedge pair; and

(C) B_t = the value at time t of the other exposure in a hedge pair.

(iii) Under the regression method of measuring effectiveness, E equals the coefficient of determination of a regression in which the change in value of one exposure in a hedge pair is the dependent variable and the change in value of the other exposure in a hedge pair is the independent variable. However, if the estimated regression coefficient is positive, then the value of E is zero.

(3) The effective portion of a hedge pair is E multiplied by the greater of the adjusted carrying values of the equity exposures forming a hedge pair.

(4) The ineffective portion of a hedge pair is (1-E) multiplied by the greater of the adjusted carrying values of the equity exposures forming a hedge pair.

Section 53. Equity Exposures to Investment Funds

(a) Available approaches. (1) Unless the exposure meets the requirements for a community development equity exposure in paragraph (b)(3)(i) of section 52, a [BANK] must determine the risk-weighted asset amount of an equity exposure to an investment fund under the Full Look-Through Approach in paragraph (b) of this section, the Simple Modified Look-Through Approach in paragraph (c) of this section, the Alternative Modified Look-Through Approach in paragraph (d) of this section, or, if the investment fund qualifies for the Money Market Fund Approach, the Money Market Fund Approach in paragraph (e) of this section.

(2) The risk-weighted asset amount of an equity exposure to an investment fund that meets the requirements for a community development equity exposure in paragraph (b)(3)(i) of section 52 is its adjusted carrying value.

(3) If an equity exposure to an investment fund is part of a hedge pair and the [BANK] does not use the Full Look-Through Approach, the [BANK] may use the ineffective portion of the hedge pair as determined under paragraph (c) of section 52 as the adjusted carrying value for the equity exposure to the investment fund. The risk-weighted asset amount of the effective portion of the hedge pair is equal to its adjusted carrying value.

(b) Full Look-Through Approach. A [BANK] that is able to calculate a risk-weighted asset amount for its proportional ownership share of each exposure held by the investment fund (as calculated under this appendix as if the proportional ownership share of each exposure were held directly by the [BANK]) may set the risk-weighted asset amount of the [BANK]'s exposure to the fund equal to the product of:

(1) The aggregate risk-weighted asset amounts of the exposures held by the fund as if they were held directly by the [BANK]; and

(2) The [BANK]'s proportional ownership share of the fund.

(c) Simple Modified Look-Through Approach. Under this approach, the risk-weighted asset amount for a [BANK]'s equity exposure to an investment fund equals the adjusted carrying value of the equity exposure multiplied by the highest risk weight that applies to any exposure the fund is permitted to hold under its prospectus, partnership agreement, or similar contract that defines the fund's permissible investments (excluding derivative contracts that are used for hedging rather than speculative purposes and that do not constitute a material portion of the fund's exposures).

(d) Alternative Modified Look-Through Approach. Under this approach, a [BANK] may assign the adjusted carrying value of an equity exposure to an investment fund on a pro rata basis to different risk weight categories under this appendix based on the investment limits in the

fund's prospectus, partnership agreement, or similar contract that defines the fund's permissible investments. The risk-weighted asset amount for the [BANK]'s equity exposure to the investment fund equals the sum of each portion of the adjusted carrying value assigned to an exposure class multiplied by the applicable risk weight under this appendix. If the sum of the investment limits for exposure classes within the fund exceeds 100 percent, the [BANK] must assume that the fund invests to the maximum extent permitted under its investment limits in the exposure class with the highest applicable risk weight under this appendix and continues to make investments in order of the exposure class with the next highest applicable risk weight under this appendix until the maximum total investment level is reached. If more than one exposure class applies to an exposure, the [BANK] must use the highest applicable risk weight. A [BANK] may exclude derivative contracts held by the fund that are used for hedging rather than for speculative purposes and do not constitute a material portion of the fund's exposures.

(e) Money Market Fund Approach. The risk-weighted asset amount for a [BANK]'s equity exposure to an investment fund that is a money market fund subject to 17 CFR 270.2a-7 and that has an applicable external rating in the highest investment-grade rating category equals the adjusted carrying value of the equity exposure multiplied by seven percent.

Part VI. Risk-Weighted Assets for Operational Risk

Section 61. Basic Indicator Approach

(a) Risk-weighted assets for operational risk. Risk-weighted assets for operational risk equals 15 percent of a [BANK]'s average positive annual gross income multiplied by 12.5.

(b) Average positive annual gross income. A [BANK]'s average positive annual gross income equals the sum of the [BANK]'s positive annual gross income, as described below, over the three most recent calendar years divided by the number of those years in which its annual

gross income is positive. A [BANK] must exclude from this calculation amounts from any year in which the annual gross income is negative or zero.

(c) Annual gross income equals:

(1) For a [BANK], its net interest income plus its total noninterest income minus its underwriting income from insurance and reinsurance activities as reported on the [BANK]'s Call Report.

(2) For a bank holding company, its net interest income plus its total noninterest income minus its underwriting income from insurance and reinsurance activities as reported on the bank holding company's Y9-C Report.

(3) For a savings association, its net interest income (expense) before provision for losses on interest-bearing assets, plus total noninterest income, minus the portion of its other fees and charges that represents income derived from insurance and reinsurance underwriting activities, minus (plus) its income (loss) from the sale of assets held for sale and available-for-sale securities to include only the profit or loss from the disposition of available-for-sale securities pursuant to FASB Statement No. 115, minus (plus) its income (loss) from the sale of securities held-to-maturity, all as reported on the savings association's year-end Thrift Financial Report.

Part VII. Disclosure

Section 71. Disclosure Requirements

(a) Each [BANK] must publicly disclose each quarter its total and tier 1 risk-based capital ratios and their components (that is, tier 1 capital, tier 2 capital, total qualifying capital, and total risk-weighted assets).³

³ Other public disclosure requirements continue to apply - for example, Federal securities law and regulatory reporting requirements.

(b) A [BANK] must comply with paragraph (c) of this section unless it is a consolidated subsidiary of a bank holding company or depository institution that is subject to these disclosure requirements.

(c) (1) Each [BANK] that is not a subsidiary of a non-U.S. banking organization that is subject to comparable public disclosure requirements in its home jurisdiction must provide timely public disclosures each calendar quarter of the information in tables 15.1 – 15.10 below. If a significant change occurs, such that the most recent reported amounts are no longer reflective of the [BANK]'s capital adequacy and risk profile, then a brief discussion of this change and its likely impact must be provided as soon as practicable thereafter. Qualitative disclosures that typically do not change each quarter (for example, a general summary of the [BANK]'s risk management objectives and policies, reporting system, and definitions) may be disclosed annually, provided any significant changes to these are disclosed in the interim. Management is encouraged to provide all of the disclosures required by this appendix in one place on the [BANK]'s public website.⁴ The [BANK] must make these disclosures publicly available for each of the last three years (that is, twelve quarters) or such shorter period [beginning on the effective date of a [BANK]'s election to use this appendix].

(2) Each [BANK] is required to have a formal disclosure policy approved by the board of directors that addresses its approach for determining the disclosures it makes. The policy must address the associated internal controls and disclosure controls and procedures. The board of directors and senior management are responsible for establishing and maintaining an effective internal control structure over financial reporting, including the disclosures required by this

⁴ Alternatively, a [BANK] may provide the disclosures in more than one place, as some of them may be included in public financial reports (for example, in Management's Discussion and Analysis included in SEC filings) or other regulatory reports. The [BANK] must publicly provide a summary table that specifically indicates where all the disclosures may be found (for example, regulatory report schedules, page numbers in annual reports).

appendix, and must ensure that appropriate review of the disclosures takes place. One or more senior officers of the [BANK] must attest that the disclosures meet the requirements of this appendix.

(3) If a [BANK] believes that disclosure of specific commercial or financial information would prejudice seriously its position by making public information that is either proprietary or confidential in nature, the [BANK] need not disclose those specific items, but must disclose more general information about the subject matter of the requirement, together with the fact that, and the reason why, the specific items of information have not been disclosed.

Table 15.1 – Scope of Application

Qualitative Disclosures	(a)	The name of the top corporate entity in the group to which the appendix applies.
	(b)	An outline of differences in the basis of consolidation for accounting and regulatory purposes, with a brief description of the entities ⁵ within the group (a) that are fully consolidated; (b) that are deconsolidated and deducted; (c) for which the regulatory capital requirement is deducted; and (d) that are neither consolidated nor deducted (for example, where the investment is risk weighted).
	(c)	Any restrictions, or other major impediments, on transfer of funds or regulatory capital within the group.
Quantitative Disclosures	(d)	The aggregate amount of surplus capital of insurance subsidiaries included in the regulatory capital of the consolidated group.
	(e)	The aggregate amount by which actual regulatory capital is less than the minimum regulatory capital requirement in all subsidiaries with regulatory capital requirements and the name(s) of the subsidiaries with such deficiencies.

⁵ Entities include securities, insurance and other financial subsidiaries, commercial subsidiaries (where permitted), significant minority equity investments in insurance, financial and commercial entities.

Table 15.2 – Capital Structure

Qualitative Disclosures	(a)	Summary information on the terms and conditions of the main features of all capital instruments, especially in the case of innovative, complex or hybrid capital instruments.
Quantitative Disclosures	(b)	The amount of tier 1 capital, with separate disclosure of: <ul style="list-style-type: none"> • common stock/surplus; • retained earnings; • minority interests in the equity of subsidiaries; • restricted core capital elements as defined in [the general risk-based capital rules] • amounts deducted from tier 1 capital, including goodwill and certain intangibles.
	(c)	The total amount of tier 2 capital, with a separate disclosure of amounts deducted from tier 2 capital.
	(d)	Other deductions from capital.
	(e)	Total eligible capital.

Table 15.3 – Capital Adequacy

Qualitative disclosures	(a)	A summary discussion of the [BANK]’s approach to assessing the adequacy of its capital to support current and future activities.
Quantitative disclosures	(b)	Risk-weighted assets for: <ul style="list-style-type: none"> • Exposures to sovereign entities; • Exposures to certain supranational entities and MDBs; • Exposures to depository institutions, foreign banks, and credit unions; • Exposures to PSEs; • Corporate exposures; • Regulatory retail exposures; • Residential mortgage exposures; • Statutory multifamily mortgages and pre-sold construction loans; • Past due loans; • Other assets; • Securitization exposures; and • Equity exposures.

	(c)	Risk-weighted assets for market risk as calculated under [the market risk rule]: ⁶ <ul style="list-style-type: none"> • Standardized specific risk charge; and • Internal models approach for specific risk.
	(d)	Risk-weighted assets for operational risk.
	(e)	Total and tier 1 risk-based capital ratios: <ul style="list-style-type: none"> • For the top consolidated group; and • For each [BANK] subsidiary.
	(f)	Total risk-weighted assets.

General qualitative disclosure requirement

For each separate risk area described in tables 15.4 through 15.10, the [BANK] must describe its risk management objectives and policies.

Table 15.4⁷ – Credit Risk: General Disclosures

Qualitative Disclosures	(a)	The general qualitative disclosure requirement with respect to credit risk (excluding counterparty credit risk disclosed in accordance with Table 16.5), including: <ul style="list-style-type: none"> • Definitions of past due and impaired (for accounting purposes); • Description of approaches followed for allowances, including statistical methods used where applicable; • Discussion of the [BANK]’s credit risk management policy.
Quantitative Disclosures	(b)	Total gross credit risk exposures and average credit risk exposures, after accounting offsets in accordance with GAAP, ⁸ and without taking into account the effects of credit risk mitigation techniques (for example, collateral and netting), over the period broken down by major types of credit exposure. For example, [BANK]s could apply a breakdown similar to that used for accounting purposes. Such a breakdown might, for instance, be (a) loans, off-balance sheet commitments, and other non-derivative off-balance sheet exposures, (b) debt securities, and (c) OTC derivatives
	(c)	Geographic ⁹ distribution of exposures, broken down in significant areas by major types of credit exposure.
	(d)	Industry or counterparty type distribution of exposures, broken down by major types of credit exposure.

⁶ Risk-weighted assets determined under [the market risk rule] are to be disclosed only for the approaches used.

⁷ Table 15.4 does not include equity exposures.

⁸ For example, FASB Interpretations 39 and 41.

⁹ Geographical areas may comprise individual countries, groups of countries, or regions within countries. A [BANK] might choose to define the geographical areas based on the way the [BANK]’s portfolio is geographically managed. The criteria used to allocate the loans to geographical areas must be specified.

(e)	Remaining contractual maturity breakdown (for example, one year or less) of the whole portfolio, broken down by major types of credit exposure.
(f)	By major industry or counterparty type: <ul style="list-style-type: none"> • Amount of impaired loans; • Amount of past due loans;¹⁰ • Allowances; and • Charge-offs during the period.
(g)	Amount of impaired loans and, if available, the amount of past due loans broken down by significant geographic areas including, if practical, the amounts of allowances related to each geographical area. ¹¹
(h)	Reconciliation of changes in the allowance for loan and lease losses. ¹²

¹⁰ A [BANK] is encouraged also to provide an analysis of the aging of past-due loans.

¹¹ The portion of general allowance that is not allocated to a geographical area should be disclosed separately.

¹² The reconciliation should include the following: a description of the allowance; the opening balance of the allowance; charge-offs taken against the allowance during the period; amounts provided (or reversed) for estimated probable loan losses during the period; any other adjustments (for example, exchange rate differences, business combinations, acquisitions and disposals of subsidiaries), including transfers between allowances; and the closing balance of the allowance. Charge-offs and recoveries that have been recorded directly to the income statement should be disclosed separately.

Table 15.5 – General Disclosure for Counterparty Credit Risk-Related Exposures

<p>Qualitative Disclosures</p>	<p>(a)</p>	<p>The general qualitative disclosure requirement with respect to OTC derivatives, eligible margin loans, and repo-style transactions, including:</p> <ul style="list-style-type: none"> • Discussion of methodology used to assign economic capital and credit limits for counterparty credit exposures; • Discussion of policies for securing collateral, valuing and managing collateral, and establishing credit reserves; • Discussion of the primary types of collateral taken; • Discussion of policies with respect to wrong-way risk exposures; and • Discussion of the impact of the amount of collateral the [BANK] would have to provide given a credit rating downgrade.
<p>Quantitative Disclosures</p>	<p>(b)</p>	<p>Gross positive fair value of contracts, netting benefits, netted current credit exposure, collateral held (including type, for example, cash, government securities), and net unsecured credit exposure.¹³ Also report the notional value of credit derivative hedges purchased for counterparty credit risk protection and the distribution of current credit exposure by types of credit exposure.¹⁴</p>
	<p>(c)</p>	<p>Notional amount of purchased and sold credit derivatives, segregated between use for the [BANK]’s own credit portfolio, as well as in its intermediation activities, including the distribution of the credit derivative products used, broken down further by protection bought and sold within each product group</p>

¹³ Net unsecured credit exposure is the credit exposure after considering both the benefits from legally enforceable netting agreements and collateral arrangements without taking into account haircuts for price volatility, liquidity, etc.

¹⁴ This may include interest rate derivative contracts, foreign exchange derivative contracts, equity derivative contracts, credit derivatives, commodity or other derivative contracts, repo-style transactions, and eligible margin loans.

Table 15.6 – Credit Risk Mitigation ^{15, 16, 17}

<p>Qualitative Disclosures</p>	<p>(a)</p>	<p>The general qualitative disclosure requirement with respect to credit risk mitigation including:</p> <ul style="list-style-type: none"> • policies and processes for, and an indication of the extent to which the [BANK] uses, on- and off-balance sheet netting; • policies and processes for collateral valuation and management; • a description of the main types of collateral taken by the [BANK]; • the main types of guarantors/credit derivative counterparties and their creditworthiness; and • information about (market or credit) risk concentrations within the mitigation taken.
<p>Quantitative Disclosures</p>	<p>(b)</p>	<p>For each separately disclosed portfolio, the total exposure (after, where applicable, on- or off-balance sheet netting) that is covered by guarantees/credit derivatives and the risk-weighted asset amount associated with that exposure.</p>

¹⁵ At a minimum, a [BANK] must give the disclosures in Table 15.6 in relation to credit risk mitigation that has been recognized for the purposes of reducing capital requirements under this appendix. Where relevant, [BANK]s are encouraged to give further information about mitigants that have not been recognized for that purpose.

¹⁶ Credit derivatives that are treated, for the purposes of this appendix, as synthetic securitization exposures should be excluded from the credit risk mitigation disclosures and included within those relating to securitization.

¹⁷ Counterparty credit risk-related exposures disclosed pursuant to Table 15.5 should be excluded from the credit risk mitigation disclosures in Table 15.6.

Table 15.7 – Securitization

Qualitative disclosures	(a)	The general qualitative disclosure requirement with respect to securitization (including synthetic securitizations), including a discussion of: <ul style="list-style-type: none"> • the [BANK]’s objectives relating to securitization activity, including the extent to which these activities transfer credit risk of the underlying exposures away from the [BANK] to other entities; • the roles played by the [BANK] in the securitization process¹⁸ and an indication of the extent of the [BANK]’s involvement in each of them.
	(b)	Summary of the [BANK]’s accounting policies for securitization activities, including: <ul style="list-style-type: none"> • whether the transactions are treated as sales or financings; • recognition of gain-on-sale; • key assumptions for valuing retained interests, including any significant changes since the last reporting period and the impact of such changes; and • treatment of synthetic securitizations.
	(c)	Names of NRSROs used for securitizations and the types of securitization exposure for which each organization is used.
Quantitative disclosures	(d)	The total outstanding exposures securitized by the [BANK] in securitizations that meet the operation criteria in Section 41 (broken down into traditional/synthetic), by underlying exposure type. ^{19,20,21}
	(e)	For exposures securitized by the [BANK] in securitizations that meet the operational criteria in Section 41: <ul style="list-style-type: none"> • amount of securitized assets that are impaired/past due; and • losses recognized by the [BANK] during the current period²² broken down by exposure type.

¹⁸ For example: originator, investor, servicer, provider of credit enhancement, sponsor of asset-backed commercial paper facility, liquidity provider, swap provider.

¹⁹ Underlying exposure types may include, for example, mortgage loans secured by liens on one-to-four family residential property, home equity lines, credit card receivables, and auto loans.

²⁰ Securitization transactions in which the originating [BANK] does not retain any securitization exposure should be shown separately but need only be reported for the year of inception.

²¹ Where relevant, a [BANK] is encouraged to differentiate between exposures resulting from activities in which they act only as sponsors, and exposures that result from all other [BANK] securitization activities.

²² For example, charge-offs/allowances (if the assets remain on the [BANK]’s balance sheet) or write-downs of I/O strips and other residual interests.

	(f)	Aggregate amount of securitization exposures broken down by underlying exposure type.
	(g)	Aggregate amount of securitization exposures and the associated capital charges for these exposures by risk-weight category. Exposures that have been deducted from capital should be disclosed separately by type of underlying asset.
	(h)	For securitizations subject to the early amortization treatment, the following items by underlying asset type for securitized facilities: <ul style="list-style-type: none"> • the aggregate drawn exposures attributed to the seller’s and investors’ interests; and • the aggregate capital charges incurred by the [BANK] against the investor’s shares of drawn balances and undrawn lines.
	(i)	Summary of current year's securitization activity, including the amount of exposures securitized (by exposure type), and recognized gain- or loss-on-sale by asset type.

Table 15.8 – Operational Risk

Qualitative disclosures	(a)	The general qualitative disclosure requirement for operational risk.
	(b)	A description of the use of insurance for the purpose of mitigating operational risk.

Table 15.9 – Equities Not Subject to Market Risk Rule

<p>Qualitative Disclosures</p>	<p>(a)</p>	<p>The general qualitative disclosure requirement with respect to equity risk, including:</p> <ul style="list-style-type: none"> • differentiation between holdings on which capital gains are expected and those taken under other objectives including for relationship and strategic reasons; and • discussion of important policies covering the valuation of and accounting for equity holdings in the banking book. This includes the accounting techniques and valuation methodologies used, including key assumptions and practices affecting valuation as well as significant changes in these practices.
<p>Quantitative Disclosures</p>	<p>(b)</p>	<p>Value disclosed in the balance sheet of investments, as well as the fair value of those investments; for quoted securities, a comparison to publicly-quoted share values where the share price is materially different from fair value.</p>
	<p>(c)</p>	<p>The types and nature of investments, including the amount that is:</p> <ul style="list-style-type: none"> • Publicly traded; and • Non-publicly traded.
	<p>(d)</p>	<p>The cumulative realized gains (losses) arising from sales and liquidations in the reporting period.</p>
	<p>(e)</p>	<ul style="list-style-type: none"> • Total unrealized gains (losses)²³ • Total latent revaluation gains (losses)²⁴ • Any amounts of the above included in tier 1 and/or tier 2 capital.
	<p>(f)</p>	<p>Capital requirements broken down by appropriate equity groupings, consistent with the [BANK]’s methodology, as well as the aggregate amounts and the type of equity investments subject to any supervisory transition regarding regulatory capital requirements.</p>

²³ Unrealized gains (losses) recognized in the balance sheet but not through earnings.

²⁴ Unrealized gains (losses) not recognized either in the balance sheet or through earnings.

Table 15.10 – Interest Rate Risk for Non-trading Activities

Qualitative disclosures	(a)	The general qualitative disclosure requirement, including the nature of interest rate risk for non-trading activities and key assumptions, including assumptions regarding loan prepayments and behavior of non-maturity deposits, and frequency of measurement of interest rate risk for non-trading activities.
Quantitative disclosures	(b)	The increase (decline) in earnings or economic value (or relevant measure used by management) for upward and downward rate shocks according to management’s method for measuring interest rate risk for non-trading activities, broken down by currency (as appropriate).

END OF COMMON RULE.

[END OF COMMON TEXT]

List of Subjects

12 CFR Part 3

Administrative practices and procedure, Capital, National banks, Reporting and recordkeeping requirements, Risk.

12 CFR Part 208

Confidential business information, Crime, Currency, Federal Reserve System, Mortgages, Reporting and recordkeeping requirements, Securities.

12 CFR Part 225

Administrative practice and procedure, Banks, banking, Federal Reserve System, Holding companies, Reporting and recordkeeping requirements, Securities.

12 CFR Part 325

Administrative practice and procedure, Banks, banking, Capital Adequacy, Reporting and recordkeeping requirements, Savings associations, State nonmember banks.

12 CFR Part 567

Capital, Reporting and recordkeeping requirements, Savings associations.

Proposed Adoption of Common Appendix

The proposed adoption of the common rules by the agencies, as modified by agency-specific text, is set forth below:

DEPARTMENT OF THE TREASURY

Office of the Comptroller of the Currency

12 CFR Chapter I

Authority and Issuance

For the reasons stated in the common preamble, the Office of the Comptroller of the Currency amends Part 3 of chapter I of Title 12, Code of Federal Regulations as follows:

PART 3—MINIMUM CAPITAL RATIOS; ISSUANCE OF DIRECTIVES

1. The authority citation for part 3 continues to read as follows:

Authority: 12 U.S.C. 93a, 161, 1818, 1828(n), 1828 note, 1831n note, 1835, 3907, and 3909.

2. New Appendix D to part 3 is added as set forth at the end of the common preamble.
3. Appendix D to part 3 is amended as set forth below:
 - a. Remove “[agency]” and add “OCC” in its place wherever it appears.
 - b. Remove “[BANK]” and add “bank” in its place wherever it appears, and remove “[Banks]” and add “Banks” in its place wherever it appears.
 - c. Remove “[Appendix __ to Part __]” and add “Appendix D to Part 3” in its place wherever it appears.
 - d. Remove “[the general risk-based capital rules]” and add “12 CFR part 3, appendix A” in its place wherever it appears.
 - e. Remove “[the market risk rule]” and add “12 CFR part 3, appendix B” in its place wherever it appears.
 - f. Remove “[the advanced approaches risk-based capital rules]” and add “12 CFR part 3, appendix C” in its place wherever it appears.

g. In section 1, revise paragraph (e) to read as follows:

Section 1. Purpose, Applicability, Election Procedures, and Reservation of Authority

* * * * *

(e) Notice and response procedures. In making a determination under paragraphs (c)(3) or (d) of this section, the OCC will apply notice and response procedures in the same manner as the notice and response procedures in 12 CFR 3.12.

* * * * *

h. In section 2, revise the definitions of gain-on-sale, pre-sold construction loan, statutory multifamily mortgage, and paragraph (7) of the definition of traditional securitization to read as follows:

Section 2. Definitions

* * * * *

Gain-on-sale means an increase in the equity capital (as reported on Schedule RC of the Consolidated Statement of Condition and Income (Call Report)) of a bank that results from a securitization (other than an increase in equity capital that results from the bank's receipt of cash in connection with the securitization). (See also securitization.)

* * * * *

Pre-sold construction loan means any one-to-four family residential pre-sold construction loan for a residence meeting the requirements under section 618(a)(1) or (2) of the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 (RTCRRRI Act) and under 12 CFR part 3, appendix A, section 3(a)(3)(iv).

* * * * *

Statutory multifamily mortgage means any multifamily residential mortgage meeting the requirements under section 618(b)(1) of the RTCRRI Act, and under 12 CFR part 3, appendix A, section 3(a)(3)(v).

* * * * *

Traditional securitization * * *

(7) The underlying exposures are not owned by a firm an investment in which qualifies as a community development investment under 12 U.S.C. 24(Eleventh);

* * * * *

i. In section 21, revise paragraph (a)(1) and (a)(2) to read as follows:

Section 21. Modifications to Tier 1 and Tier 2 Capital

(a) * * *

(1) A bank is not required to make the deductions from capital for CEIOs in 12 CFR part 3, appendix A, section 2(c)(1)(iv).

(2) A bank is not required to make the deductions from capital for nonfinancial equity investments in 12 CFR part 3, appendix A, section 2(c)(1)(v).

* * * * *

j. In section 33, revise paragraphs (c)(2) and (g)(3)(iv)(B) to read as follows:

Section 33. General Risk Weights

* * * * *

(c) * * *

(2) A bank must assign a risk weight of at least 100 percent to an exposure to a depository institution or a foreign bank that is includable in the depository institution's or foreign

bank's regulatory capital and that is not subject to deduction as a reciprocal holding pursuant to 12 CFR part 3, appendix A, section 2(c)(6)(ii). * * *

(g) * * *

(3) * * *

(iv) * * *

(B) A bank must base all estimates of a property's value on an appraisal or evaluation of the property that satisfies subpart C of 12 CFR part 34.

* * * * *

k. Revise the first sentence of paragraph (i)(1)(iv) and paragraph (i)(4) of section 42 to read as follows:

Section 42. Risk-Weighted Assets for Securitization Exposures

* * * * *

(i) * * *

(1) * * *

(iv) The bank is well capitalized, as defined in the OCC's prompt corrective action regulation at 12 CFR part 6. For purposes of determining whether a bank is well capitalized for purposes of this paragraph, the bank's capital ratios must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section.

* * * * *

(4) The risk-based capital ratios of the bank must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section as provided in 12 CFR part 3, appendix A.

* * * * *

l. In section 52, revise paragraph (b)(3)(i) to read as follows:

Section 52. Simple Risk-Weight Approach (SRWA)

* * * * *

(b) * * *

(3) * * *

(i) Community development exposures. An equity exposure that qualifies as a community development investment under 12 U.S.C. 24(Eleventh), excluding equity exposures to an unconsolidated small business investment company and equity exposures held through a consolidated small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682).

* * * * *

m. In section 61, revise paragraph (c) to read as follows:

Section 61. Basic Indicator Approach

* * * * *

(c) Annual gross income. A bank's annual gross income equals its net interest income plus its total noninterest income minus its underwriting income from insurance and reinsurance activities as reported on the bank's Call Report.

* * * * *

n. In section 71, revise paragraph (b) to read as follows:

Section 71. Disclosure Requirements

* * * * *

(b) A bank must comply with paragraph (c) of section 71 of appendix H to the Federal Reserve Board's Regulation Y (12 CFR part 225, appendix H), including Tables 15.1 – 15.10, unless it is a consolidated subsidiary of a bank holding company or depository institution that is subject to these requirements.

* * * * *

- o. In section 71, remove paragraph (c) and Tables 15.1 – 15.10.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

12 CFR Chapter II

Authority and Issuance

For the reasons stated in the common preamble, the Board of Governors of the Federal Reserve System amends parts 208 and 225 of chapter II of title 12 of the Code of Federal Regulations as follows:

PART 208—MEMBERSHIP OF STATE BANKING INSTITUTIONS IN THE FEDERAL RESERVE SYSTEM (REGULATION H)

1. The authority citation for part 208 continues to read as follows:

Authority: 12 U.S.C. 24, 36, 92a, 93a, 248(a), 248(c), 321-338a, 371d, 461, 481-486, 601, 611, 1814, 1816, 1818, 1820(d)(9), 1823(j), 1828(o), 1831, 1831o, 1831p-1, 1831r-1, 1835a, 1882, 2901-2907, 3105, 3310, 3331-3351, and 3906-3909; 15 U.S.C. 78b, 78l(b), 78l(g), 78l(i), 78o-4(c)(5), 78q, 78q-1, and 78w, 6801, and 6805; 31 U.S.C. 5318; 42 U.S.C. 4012a, 4104a, 4104b, 4106, and 4128.

2. New Appendix G to part 208 is added as set forth at the end of the common preamble.

3. Appendix G to part 208 is amended as set forth below:

- a. Remove “[agency]” and add “Federal Reserve” in its place wherever it appears.
- b. Remove “[BANK]” and add “bank” in its place wherever it appears, and remove “[Banks]” and add “Banks” in its place wherever it appears.
- c. Remove “[Appendix __ to Part __]” and add “Appendix G to Part 208” in its place wherever it appears.
- d. Remove “[the general risk-based capital rules]” and add “12 CFR part 208, appendix A” in its place wherever it appears.

e. Remove “[the market risk rule]” and add “12 CFR part 208, appendix E” in its place wherever it appears.

f. Remove “[the advanced approaches risk-based capital rules]” and add “12 CFR part 208, appendix F” in its place wherever it appears.

g. In section 1, revise paragraph (e) to read as follows:

Section 1. Purpose, Applicability, Election Procedures, and Reservation of Authority

* * * * *

(e) Notice and response procedures. In making a determination under paragraphs (c)(3) or (d) of this section, the Federal Reserve will apply notice and response procedures in the same manner as the notice and response procedures in 12 CFR 263.202.

* * * * *

h. In section 2, revise the definitions of gain-on-sale, pre-sold construction loan, statutory multifamily mortgage, and paragraph (7) of the definition of traditional securitization to read as follows:

Section 2. Definitions

* * * * *

Gain-on-sale means an increase in the equity capital (as reported on Schedule RC of the Consolidated Statement of Condition and Income (Call Report)) of a bank that results from a securitization (other than an increase in equity capital that results from the bank’s receipt of cash in connection with the securitization). (See also securitization.)

* * * * *

Pre-sold construction loan means any one-to-four family residential pre-sold construction loan for a residence meeting the requirements under section 618(a)(1) or (2) of the Resolution

Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 (RTCRRRI Act) and under 12 CFR part 208, appendix A, section III.C.3.

* * * * *

Statutory multifamily mortgage means any multifamily residential mortgage meeting the requirements under section 618(b)(1) of the RTCRRRI Act and under 12 CFR part 208, appendix A, section III.C.3.

* * * * *

Traditional securitization * * *

(7) The underlying exposures are not owned by a firm an investment in which qualifies as a community development investment under 12 U.S.C. 24(Eleventh);

* * * * *

i. In section 21, revise paragraphs (a)(1) and (2) to read as follows:

Section 21. Modifications to Tier 1 and Tier 2 Capital

(a) * * *

(1) A bank is not required to make the deductions from capital for CEIOs in 12 CFR part 208, appendix A, section II.B.1.e.

(2) A bank is not required to make the deductions from capital for nonfinancial equity investments in 12 CFR part 208, appendix A, section II.B.5.

* * * * *

j. In section 33, revise paragraphs (c)(2) and (g)(3)(iv)(B) to read as follows:

Section 33. General Risk Weights

* * * * *

(c) * * *

(2) A bank must assign a risk weight of at least 100 percent to an exposure to a depository institution or a foreign bank that is includable in the depository institution's or foreign bank's regulatory capital and that is not subject to deduction as a reciprocal holding pursuant to 12 CFR part 208, appendix A, section II.B.3. * * *

(g) * * *

(3) * * *

(iv) * * *

(B) A bank must base all estimates of a property's value on an appraisal or evaluation of the property that satisfies subpart E of 12 CFR part 208.

* * * * *

k. Revise the first sentence of paragraph (i)(1)(iv) and paragraph (i)(4) of section 42 to read as follows:

Section 42. Risk-Weighted Assets for Securitization Exposures

* * * * *

(i) * * *

(1) * * *

(iv) The bank is well capitalized, as defined in the Federal Reserve's prompt corrective action regulation at 12 CFR part 208, Subpart D. For purposes of determining whether a bank is well capitalized for purposes of this paragraph, the bank's capital ratios must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section. * * *

* * * * *

(4) The risk-based capital ratios of the bank must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section as provided in 12 CFR part 208, appendix A.

* * * * *

l. In section 52, revise paragraph (b)(3)(i) to read as follows:

Section 52. Simple Risk-Weight Approach (SRWA)

* * * * *

(b) * * *

(3) * * *

(i) Community development exposures. An equity exposure that qualifies as a community development investment under 12 U.S.C. 24(Eleventh), excluding equity exposures to an unconsolidated small business investment company and equity exposures held through a consolidated small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682).

* * * * *

m. In section 61, revise paragraph (c) to read as follows:

Section 61. Basic Indicator Approach

* * * * *

(c) Annual gross income. A bank's annual gross income equals its net interest income plus its total noninterest income minus its underwriting income from insurance and reinsurance activities as reported on the bank's Call Report.

* * * * *

n. In section 71, revise paragraph (b) to read as follows:

Section 71. Disclosure Requirements

* * * * *

(b) A bank must comply with paragraph (c) of section 71 of appendix H to the Federal Reserve Board's Regulation Y (12 CFR part 225, appendix H), including Tables 15.1 – 15.10, unless it is a consolidated subsidiary of a bank holding company or depository institution that is subject to these requirements.

* * * * *

o. In section 71, remove paragraph (c) and remove Tables 15.1 – 15.10.

**PART 225—BANK HOLDING COMPANIES AND CHANGE IN BANK CONTROL
(REGULATION Y)**

1. The authority citation for part 225 continues to read as follows:

Authority: 12 U.S.C. 1817(j)(13), 1818, 1828(o), 1831i, 1831p-1, 1843(c)(8), 1844(b), 1972(1), 3106, 3108, 3310, 3331-3351, 3907, and 3909; 15 U.S.C. 6801 and 6805.

2. New Appendix H to part 225 is added as set forth at the end of the common preamble.

3. Appendix H to part 225 is amended as set forth below:

a. Remove “[agency]” and add “Federal Reserve” in its place wherever it appears.

b. Remove “[BANK]” and add in its place “bank holding company” wherever it appears, and remove “[Banks]” and add “Bank Holding Companies” in its place wherever it appears.

c. Remove “[Appendix __ to Part __]” and add “Appendix H to Part 225” in its place wherever it appears.

d. Remove “[the general risk-based capital rules]” and add “12 CFR part 225, appendix A” in its place wherever it appears.

e. Remove “[the market risk rule]” and add “12 CFR part 225, appendix E” in its place wherever it appears.

f. Remove “[the advanced approaches risk-based capital rules]” and add “12 CFR part 208, appendix G” in its place wherever it appears.

g. In section 1, revise paragraphs (b) and (e) to read as follows:

Section 1. Purpose, Applicability, Election Procedures, and Reservation of Authority

* * * * *

(b) Applicability. This appendix applies to a bank holding company that elects to use this appendix to calculate its risk-based capital requirements and that is not a consolidated subsidiary

of another bank holding company that uses this appendix to calculate its risk-based capital requirements.

* * * * *

(e) Notice and response procedures. In making a determination under paragraphs (c)(3) or (d) of this section, the Federal Reserve will apply notice and response procedures in the same manner as the notice and response procedures in 12 CFR 263.202.

* * * * *

h. In section 2, revise the definitions of gain-on-sale, pre-sold construction loan, statutory multifamily mortgage, and paragraph (7) of the definition of traditional securitization to read as follows:

Section 2. Definitions

* * * * *

Gain-on-sale means an increase in the equity capital (as reported on Schedule HC of the FR Y-9C Report) of a bank holding company that results from a securitization (other than an increase in equity capital that results from the bank holding company's receipt of cash in connection with the securitization). (See also securitization.)

* * * * *

Pre-sold construction loan means any one-to-four family residential pre-sold construction loan for a residence meeting the requirements under section 618(a)(1) or (2) of the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 (RTCRRRI Act) and under 12 CFR part 225, appendix A, section III.C.3.

* * * * *

Statutory multifamily mortgage means any multifamily residential mortgage meeting the requirements under section 618(b)(1) of the RTCRRI Act and under 12 CFR part 225, appendix A, section III.C.3.

* * * * *

Traditional securitization * * *

(7) The underlying exposures are not owned by a firm an investment in which qualifies as a community development investment under 12 U.S.C. 24(Eleventh);

* * * * *

i. In section 21, revise paragraphs (a)(1) and (2) and add a new paragraph (c)(4) to read as follows:

Section 21. Modifications to Tier 1 and Tier 2 Capital

(a) * * *

(1) A bank holding company is not required to make the deductions from capital for CEIOs in 12 CFR part 225, appendix A, section II.B.1.e.

(2) A bank holding company is not required to make the deductions from capital for nonfinancial equity investments in 12 CFR part 225, appendix A, section II.B.5. * * *

(c) * * *

(4) A bank holding company must also deduct an amount equal to the minimum regulatory capital requirement established by the regulator of any insurance underwriting subsidiary of the holding company. For U.S.-based insurance underwriting subsidiaries, this amount generally would be 200 percent of the subsidiary's Authorized Control Level as established by the appropriate state regulator of the insurance company.

j. In section 33, revise paragraph (c)(2) to read as follows:

Section 33. General Risk Weights

* * * * *

(c) * * *

(2) A bank holding company must assign a risk weight of at least 100 percent to an exposure to a depository institution or a foreign bank that is includable in the depository institution's or foreign bank's regulatory capital and that is not subject to deduction as a reciprocal holding pursuant to 12 CFR part 225, appendix A, section II.B.3. * * *

* * * * *

k. In paragraph (k)(1) of section 33, remove "A [BANK] may assign a zero percent risk weight to cash owned and held in all offices of the [BANK] or in transit; to gold bullion held in the [BANK]'s own vaults, or held in another depository institution's vaults on an allocated basis, to the extent the gold bullion assets are offset by gold bullion liabilities;" and add in its place "A bank holding company may assign a zero percent risk weight to cash owned and held in all offices of subsidiary depository institutions or in transit; to gold bullion held in either a subsidiary depository institution's own vaults, or held in another depository institution's vaults on an allocated basis, to the extent the gold bullion assets are offset by gold bullion liabilities;"

* * * * *

l. Revise the first sentence of paragraph (i)(1)(iv) and revise paragraph (i)(4) of section 42 to read as follows:

Section 42. Risk-Weighted Assets for Securitization Exposures

* * * * *

(i) * * *

(1) * * *

(iv) The bank holding company is well capitalized, as defined in the Federal Reserve's prompt corrective action regulation at 12 CFR part 208, Subpart D. For purposes of determining whether a bank holding company is well capitalized for purposes of this paragraph, the bank holding company's capital ratios must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section.

* * * * *

(4) The risk-based capital ratios of the bank holding company must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section as provided in 12 CFR part 225, appendix A.

* * * * *

m. In section 52, revise paragraph (b)(3)(i) to read as follows:

Section 52. Simple Risk-Weight Approach (SRWA)

* * * * *

(b) * * *

(3) * * *

(i) Community development exposures. An equity exposure that qualifies as a community development investment under 12 U.S.C. 24(Eleventh), excluding equity exposures to an unconsolidated small business investment company and equity exposures held through a consolidated small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682).

* * * * *

n. In section 61, revise paragraph (c) to read as follows:

Section 61. Basic Indicator Approach

* * * * *

(c) Annual gross income. A bank holding company's annual gross income equals its net interest income plus its total noninterest income minus its underwriting income from insurance and reinsurance activities as reported on the bank holding company's Y-9C Report.

* * * * *

FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Chapter III

Authority and Issuance

For the reasons stated in the common preamble, the Federal Deposit Insurance Corporation amends Part 325 of chapter III of Title 12, Code of Federal Regulations as follows:

PART 325—CAPITAL MAINTENANCE

1. The authority citation for part 325 continues to read as follows:

Authority: 12 U.S.C. 1815(a), 1815(b), 1816, 1818(a), 1818(b), 1818(t), 1819(Tenth), 1828(c), 1828(d), 1828(i), 1828(n), 1828(o), 1835, 3907, 3909, 4808; Pub. L. 102-233, 105 Stat. 1761, 1789, 1790 (12 U.S.C. 1831n, note); Pub. L. 102-242, 105 Stat. 2236, 2355, 2386 (12 U.S.C. 1828 note).

2. New Appendix E to part 325 is added as set forth at the end of the common preamble.

3. Appendix E to part 325 is amended as set forth below:

- a. Remove “[agency]” and add “FDIC” in its place wherever it appears.
- b. Remove “[BANK]” and add “bank” in its place wherever it appears, and remove “[Banks]” and add “Banks” in its place wherever it appears.
- c. Remove “[Appendix __ to Part __]” and add “Appendix E to Part 325” in its place wherever it appears.
- d. Remove “[the general risk-based capital rules]” and add “12 CFR part 325, appendix A” in its place wherever it appears.
- e. Remove “[the market risk rule]” and add “12 CFR part 325, appendix C” in its place wherever it appears.

f. Remove “[the advanced approaches risk-based capital rules]” and add “12 CFR part 325, appendix D” in its place wherever it appears.

g. In section 1, revise paragraph (e) to read as follows:

Section 1. Purpose, Applicability, Election Procedures, and Reservation of Authority

* * * * *

(e) Notice and response procedures. In making a determination under paragraphs (c)(3) or (d) of this section, the FDIC will apply notice and response procedures in the same manner as the notice and response procedures in 12 CFR 325.6(c).

* * * * *

h. In section 2, revise the definitions of gain-on-sale, pre-sold construction loan, statutory multifamily mortgage, and paragraph (7) of the definition of traditional securitization to read as follows:

Section 2. Definitions

* * * * *

Gain-on-sale means an increase in the equity capital (as reported on Schedule RC of the Consolidated Statement of Condition and Income (Call Report)) of a bank that results from a securitization (other than an increase in equity capital that results from the bank’s receipt of cash in connection with the securitization). (See also securitization.)

* * * * *

Pre-sold construction loan means any one-to-four family residential pre-sold construction loan for a residence meeting the requirements under section 618(a)(1) or (2) of the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 (RTCRRRI Act) and

under 12 CFR part 325, appendix A, section II.C, and that is not 90 days or more past due or on nonaccrual.

* * * * *

Statutory multifamily mortgage means any multifamily residential mortgage meeting the requirements under section 618(b)(1) of the RTCRRI Act and under 12 CFR part 325, appendix A, section II.C.

* * * * *

Traditional securitization * * *

(7) The underlying exposures are not owned by a firm an investment in which qualifies as a community development investment under 12 U.S.C. 24(Eleventh);

* * * * *

i. In section 21, revise paragraph (a)(1) and (a)(2) to read as follows:

Section 21. Modifications to Tier 1 and Tier 2 Capital

(a) * * *

(1) A bank is not required to make the deductions from capital for CEIOs in 12 CFR part 325, appendix A, section II.B.5.

(2) A bank is not required to make the deductions from capital for nonfinancial equity investments in 12 CFR part 325, appendix A, section II.B.

* * * * *

j. In section 33, revise paragraphs (c)(2) and (g)(3)(iv)(B) to read as follows:

Section 33. General Risk Weights

* * * * *

(c) * * *

(2) A bank must assign a risk weight of at least 100 percent to an exposure to a depository institution or a foreign bank that is includable in the depository institution's or foreign bank's regulatory capital and that is not subject to deduction as a reciprocal holding pursuant to 12 CFR part 325, appendix A, section I.B.(4).* * *

(g) * * *

(3) * * *

(iv) * * *

(B) A bank must base all estimates of a property's value on an appraisal or evaluation of the property that satisfies 12 CFR part 323.

* * * * *

k. Revise the first sentence of paragraph (i)(1)(iv) and paragraph (i)(4) of section 42 to read as follows:

Section 42. Risk-Weighted Assets for Securitization Exposures

* * * * *

(i) * * *

(1) * * *

(iv) The bank is well capitalized, as defined in the FDIC's prompt corrective action regulation at 12 CFR part 325, subpart B. For purposes of determining whether a bank is well capitalized for purposes of this paragraph, the bank's capital ratios must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section.

* * * * *

(4) The risk-based capital ratios of the bank must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section as provided in 12 CFR part 325, appendix A.

* * * * *

l. In section 52, revise paragraph (b)(3)(i) to read as follows:

Section 52. Simple Risk-Weight Approach (SRWA)

* * * * *

(b) * * *

(3) * * *

(i) Community development exposures. An equity exposure that qualifies as a community development investment under 12 U.S.C. 24(Eleventh), excluding equity exposures to an unconsolidated small business investment company and equity exposures held through a consolidated small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682).

* * * * *

m. In section 61, revise paragraph (c) to read as follows:

Section 61. Basic Indicator Approach

* * * * *

(c) Annual gross income. A bank's annual gross income equals its net interest income plus its total noninterest income minus its underwriting income from insurance and reinsurance activities as reported on the bank's Call Report.

* * * * *

n. In section 71, revise paragraph (b) to read as follows:

Section 71. Disclosure Requirements

* * * * *

(b) A bank must comply with paragraph (c) of section 71 of appendix H to the Federal Reserve Board's Regulation Y (12 CFR part 225, appendix H), including Tables 15.1 – 15.10, unless it is a consolidated subsidiary of a bank holding company or depository institution that is subject to these requirements.

* * * * *

o. In section 71, remove paragraph (c) and Tables 15.1 – 15.10.

DEPARTMENT OF THE TREASURY

Office of Thrift Supervision

12 CFR Chapter V

Authority and Issuance

For the reasons stated in the common preamble, the Office of Thrift Supervision amends Part 567 of chapter V of Title 12, Code of Federal Regulations as follows:

PART 567 – CAPITAL

1. The authority citation for part 567 continues to read as follows:

Authority: 12 U.S.C. 1462, 1462a, 1463, 1464, 1467a, 1828(note).

2. In section 567.0, revise paragraph (a), redesignate paragraph (b) as paragraph (c), add new paragraph (b), and revise redesignated paragraph (c) by adding a new heading and by amending paragraph (c)(2)(ii) to read as follows:

§ 567.0 Scope.

(a) General. This part prescribes the minimum regulatory capital requirements for savings associations. Subpart B of this part applies to all savings associations, except as described in paragraphs (b) and (c) of this section.

(b) Savings associations using the standardized approach rule. (1) A savings association that uses Appendix B of this part must utilize the methodologies in that appendix to calculate their risk based capital requirement and make the required disclosures described in that appendix.

(2) Subpart B of this part does not apply to the computation of risk-based capital requirements by a savings association that uses Appendix B of this part. However, these savings associations:

(i) Must compute the components of capital under § 567.5 subject to the modifications in section 21 of Appendix B of this part.

(ii) Must meet the leverage ratio requirement described at §§ 567.2(a)(2) and 567.8.

Notwithstanding paragraph (b)(2)(i) of this section, the savings association must compute core (tier 1) capital under section 567.5.

(iii) Must meet the tangible capital requirement described at §§ 567.2(a)(3) and 567.9.

(iv) Are subject to §§ 567.3 (individual minimum capital requirement), 567.4 (capital directives); and 567.10 (consequences of failure to meet capital requirements).

(v) Are subject to the reservations of authority at § 567.11, which supplement the reservations of authority at section 1 of Appendix B of this part.

(c) Savings associations using the advanced approaches rule.

* * * * *

(2) * * *

(ii) Must meet the leverage ratio requirement described at §§ 567.2(a)(2) and 567.8.

Notwithstanding paragraph (c)(2)(i) of this section, the savings association must compute core (tier 1) capital under section 567.5.

* * * * *

2. Appendix B is added to part 567 as set forth at the end of the common preamble.

3. Amend Appendix B of part 567 as follows:

a. Revise the heading of Appendix B to read as follows:

Risk-Based Capital Requirements – Standardized Framework

b. Remove [agency] and add “OTS” in its place wherever it appears.

c. Remove “[BANK]” and add “savings association” in its place wherever it appears, and remove “[Banks]” and add “Savings Associations” in its place wherever it appears.

d. Remove “[Appendix __ to Part __]” and add “Appendix B to Part 567” in its place wherever it appears.

e. Remove “[the general risk-based capital rules]” and add “subpart B of part 567” in its place wherever it appears.

f. Remove “[the market risk rule]” and add “any applicable market risk rule” in its place wherever it appears.

g. Remove “[the advanced approaches risk-based capital rules]” and add “Appendix C to Part 567” in its place wherever it appears.

h. In section 1, revise paragraph (e) to read as follows:

Section 1. Purpose, Applicability, Election Procedures, and Reservation of Authority

* * * * *

(e) Notice and response procedures. In making a determination under paragraphs (c)(3) or (d) of this section, the [agency] will apply notice and response procedures in the same manner as the notice and response procedures in 12 CFR 567.3(d).

* * * * *

i. In section 2, revise the definitions of gain-on-sale, pre-sold construction loan, statutory multifamily loan, and paragraph (7) of the definition of traditional securitization to read as follows:

Section 2. Definitions

* * * * *

Gain-on-sale means an increase in the equity capital (as reported on Schedule SC of the Thrift Financial Report) of a savings association that results from a securitization (other than an increase in equity capital that results from the savings association's receipt of cash in connection with the securitization). (See also securitization.)

* * * * *

Pre-sold construction loan means any one-to-four family residential pre-sold construction loan for a residence meeting the requirements under section 618(a)(1) or (2) of the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991 (RTCRRRI Act) and 12 CFR 567.1 (definition of "qualifying residential construction loan"), and that is not on nonaccrual.

* * * * *

Statutory multifamily mortgage means any multifamily residential mortgage that:

(1) Meets the requirements under section 618(b)(1) of the RTCRRRI Act and under 12 CFR 567.1 (definition of "qualifying multifamily mortgage loan") and 12 CFR 567.6(a)(1)(iii); and

(2) Is not on nonaccrual.

* * * * *

Traditional securitization * * *

(7) The underlying exposures are not owned by a firm an investment in which is designed primarily to promote community welfare, including the welfare of low- and moderate-income communities or families, such as by providing services or jobs.

* * * * *

j. Revise paragraphs (a)(1) and (2) of section 21 to read as follows:

Section 21. Modifications to Tier 1 and Tier 2 Capital

* * * * *

(a) * * *

(1) A savings association is not required to make the deductions from capital for CEIOs in 12 CFR 567.5(a)(2)(iii) and 567.12(e);

(2) A savings association is not required to deduct equity securities from capital under 12 CFR 567.5(c)(2)(ii). However, it must continue to deduct equity investments in real estate under that section. See 12 CFR 567.1, which defines equity investments, including equity securities and equity investments in real estate.

* * * * *

k. Revise paragraphs (c)(2) and (g)(3)(iv)(B) of section 33 to read as follows:

Section 33. General Risk Weights

* * * * *

(c) * * *

(2) A savings association must assign a risk weight of at least 100 percent to an exposure to a depository institution or a foreign bank that is includable in the depository institution's or foreign bank's regulatory capital and that is not subject to deduction as a reciprocal holding pursuant to 12 CFR part 567.5(c)(2)(i). * * *

(g) * * *

(3) * * *

(iv) * * *

(B) A savings association must base all estimates of a property's value on an appraisal or evaluation of the property that satisfies 12 CFR part 564.

* * * * *

1. Revise the first sentence of paragraph (i)(1)(iv) and paragraph (i)(4) of section 42 to read as follows:

Section 42. Risk-Weighted Assets for Securitization Exposures

* * * * *

(i) * * *

(1) * * *

(iv) The savings association is well capitalized, as defined in the OTS 's prompt corrective action regulation at 12 CFR part 565.

* * * * *

(4) The risk-based capital ratios of the savings association must be calculated without regard to the capital treatment for transfers of small-business obligations with recourse specified in paragraph (i)(1) of this section as provided in 12 CFR 567.6(b)(5)(v).

* * * * *

m. Revise paragraph (b)(3)(i) of section 52 to read as follows:

Section 52 Simple Risk-Weight Approach (SRWA)

* * * * *

(b) * * *

(3) * * *

(i) Community development equity exposures. An equity exposure that is designed primarily to promote community welfare, including the welfare of low- and moderate-income communities or families, such as by providing services or jobs, excluding equity exposures to an unconsolidated small business investment company and equity exposures held through a

consolidated small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682).

* * * * *

n. Revise paragraph (c) in section 61 to read as follows:

Section 61 Basic Indicator Approach

* * * * *

(c) Annual gross income. Annual gross income equals a savings association's net interest income (expense) before provision for losses on interest-bearing assets, plus total noninterest income, minus the portion of its other fees and charges that represents income derived from insurance and reinsurance underwriting activities, minus (plus) its net income (loss) from the sale of assets held for sale and available-for-sale securities to include only the profit or loss from the disposition of available-for-sale securities pursuant to FASB Statement No. 115, minus (plus) its net income (loss) from the sale of securities held-to-maturity, all as reported on the savings association's year-end Thrift Financial Report.

* * * * *

o. In section 71, revise paragraph (b) to read as follows:

Section 71. Disclosure Requirements

* * * * *

(b) A savings association must comply with paragraph (c) of this section, unless it is a consolidated subsidiary of a bank holding company or depository institution that is subject to these requirements.

* * * * *

Dated: _____, 2008

John C. Dugan,
Comptroller of the Currency

By order of the Board of Governors of the Federal Reserve System, _____, 2008

Jennifer J. Johnson
Secretary of the Board

Dated at Washington, D.C., this ____ day of _____ 2008.
By order of the Board of Directors.
Federal Deposit Insurance Corporation.

Robert E. Feldman,
Executive Secretary

Dated: _____, 2008

BY THE OFFICE OF THRIFT SUPERVISION

John M. Reich
Director

[FR Doc. 08-_____ Filed _____]

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