The Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision (the agencies) are seeking comment on a joint notice of proposed rulemaking (NPR) related to the Financial Accounting Standards Board's (FASB) adoption of Statement of Financial Accounting Standards No. 166, Accounting for Transfers of Financial Assets, an Amendment of FASB Statement No. 140 (FAS 166) and Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46(R) (FAS 167).

Background

The agencies use generally accepted accounting principles (GAAP) as the initial basis for determining whether an exposure is treated as on- or off-balance sheet for regulatory capital purposes. On June 12, 2009, the FASB issued FAS 166 and FAS 167 (new accounting standards) which are effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009. These accounting standards will make substantive changes to how banks account for many items, including securitized assets, that are currently excluded from these organizations' balance sheets.

The agencies are issuing the proposed NPR to better align regulatory capital requirements with the actual risk of certain exposures. The agencies believe that the broader accounting consolidation requirements in the new accounting standards will result in a regulatory capital treatment that more appropriately reflects the risks to which banks are exposed. Accordingly, the agencies are proposing to continue to follow GAAP by using the new accounting standards in determining on-balance sheet exposures for regulatory capital.

Under the NPR, the agencies also propose to modify their general risk-based and advanced risk-based capital adequacy frameworks to eliminate the exclusion of certain consolidated asset-backed commercial paper programs from risk-weighted assets. The agencies also propose to provide a reservation of authority in their general risk-based and advanced risk-based capital adequacy frameworks to permit the agencies to require banking organizations to treat entities that are not consolidated under GAAP as if they were consolidated for risk-based capital purposes, commensurate with the risk relationship of the banking organization to the structure.

Banks affected by the new accounting standards generally will be subject to higher minimum regulatory capital requirements. The agencies' proposal seeks comment and supporting data on whether a phase-in of the increase in regulatory capital requirements is needed. The agencies also seek comment and supporting data on a number of other matters, including policy alternatives to address any unique challenges the new accounting standards present with regard to the allowance for loan and lease losses provisioning process including, for example, the current constraint on the amount of provisions that are eligible for inclusion in tier 2 capital.

The NPR was published in the Federal Register on September 15, 2009. Comments on the NPR will be accepted through close of business, October 15, 2009.
Further Information

You may direct questions or comments to Paul Podgorski, Risk Expert, Capital Policy Division, at (202) 874-4755; or Carl Kaminski, Senior Attorney, Legislative and Regulatory Activities Division, at (202) 874-5090.

Timothy W. Long
Senior Deputy Comptroller for Bank Supervision Policy
and Chief National Bank Examiner

Related Links
- Notice of Proposed Rulemaking 74 FR 47138
DEPARTMENT OF THE TREASURY
Office of the Comptroller of the Currency
12 CFR Part 3
[Docket ID: OCC–2009–0012]
RIN 1557–AD26

FEDERAL RESERVE SYSTEM
12 CFR Parts 208 and 225
[Regulations H and Y; Docket No. R–1368]

FEDERAL DEPOSIT INSURANCE CORPORATION
12 CFR Part 325
RIN 3064–AD48

DEPARTMENT OF THE TREASURY
Office of Thrift Supervision
12 CFR Part 567
[No. OTS–2009–0015]
RIN 1550–AC36

Risk-Based Capital Guidelines; Capital Adequacy Guidelines; Capital Maintenance: Regulatory Capital; Impact of Modifications to Generally Accepted Accounting Principles; Consolidation of Asset-Backed Commercial Paper Programs; and Other Related Issues

AGENCY: Office of the Comptroller of the Currency, Department of the Treasury; Board of Governors of the Federal Reserve System; Federal Deposit Insurance Corporation; and Office of Thrift Supervision, Department of the Treasury.

ACTION: Notice of proposed rulemaking with request for public comment.

SUMMARY: The Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (Board), Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS) (collectively, the agencies) are requesting comment on a proposal to modify their general risk-based and advanced risk-based capital adequacy frameworks to eliminate the exclusion of certain consolidated asset-backed commercial paper programs from risk-weighted assets and provide a reservation of authority in their general risk-based and advanced risk-based capital adequacy frameworks to permit the agencies to require banking organizations to treat entities that are
not consolidated under accounting standards as if they were consolidated for risk-based capital purposes, commensurate with the risk relationship of the banking organization to the structure. The agencies are issuing this proposal and request for comment to better align capital requirements with the actual risk of certain exposures and to obtain information and views from the public on the effect on regulatory capital that will result from the implementation of the Financial Accounting Standard Board’s (FASB) Statement of Financial Accounting Standards No. 166, Accounting for Transfers of Financial Assets, an Amendment of FASB Statement No. 140 and Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46(R).

DATES: Comments on this notice of proposed rulemaking must be received by October 15, 2009.

ADRESSES: Comments should be directed to:

OCC: Because paper mail in the Washington, DC area and at the agencies is subject to delay, commenters are encouraged to submit comments by the Federal eRulemaking Portal or e-mail, if possible. Please use the title “Risk-Based Capital Guidelines; Capital Adequacy Guidelines; Capital Maintenance: Regulatory Capital; Impact of Modifications to Generally Accepted Accounting Principles; Consolidation of Asset-Backed Commercial Paper Programs; and Other Related Issues” to facilitate the organization and distribution of the comments. You may submit comments by any of the following methods:

- **Federal eRulemaking Portal—“Regulations.gov”**: Go to http://www.regulations.gov. Under the “More Search Options” tab click next to the “Advanced Document Search” option where indicated, select “Comptroller of the Currency” from the agency drop-down menu, then click “Submit.” In the “Docket ID” column, select “OCC–2009–0012” to view public comments for this rulemaking action.

- **Viewing Comments Electronically**: You may inspect and photocopy comments at the OCC, 250 E. Street, SW., Washington, DC. For security reasons, the OCC requires that visitors make an appointment to inspect comments. You may do so by calling (202) 874–4700. Upon arrival, visitors must present valid government-issued photo identification and submit to security screening in order to inspect and photocopy comments.

- **Docket**: You may view or request available background documents and project summaries using the methods described above.

- **Board**: You may submit comments, identified by Docket No. R–1368, by any of the following methods:
  - **Federal eRulemaking Portal**: http://www.regulations.gov. Follow the instructions for submitting comments.

- **E-mail**: reg.s.comments@occ.treas.gov.
- **Mail**: Office of the Comptroller of the Currency, 250 E Street, SW., Mail Stop 2–3, Washington, DC 20219.

- **Fax**: (202) 874–5274.
- **Hand Delivery/Courier**: 250 E Street, SW., Mail Stop 2–3, Washington, DC 20219.

**Instructions**: You must include “OCC” as the agency name and “Docket Number OCC–2009–0012” in your comment. In general, the OCC will enter all comments received into the docket and publish them on the Regulations.gov Web site without change, including any business or personal information that you provide such as name and address information, e-mail addresses, or phone numbers. Comments received, including attachments and other supporting materials, are part of the public record and subject to public disclosure. Do not enclose any information in your comment or supporting materials that you consider confidential or inappropriate for public disclosure.

You may review comments and other related materials that pertain to this proposed rule by any of the following methods:

- **Viewing Comments Electronically**: Go to http://www.regulations.gov, under the “More Search Options” tab click next to the “Advanced Document Search” option where indicated, select “Comptroller of the Currency” from the agency drop-down menu, then click “Submit.” In the “Docket ID” column, select “OCC–2009–0012” to view public comments for this rulemaking action.

- **Viewing Comments Personally**: You may inspect and photocopy comments at the OCC, 250 E. Street, SW., Washington, DC. For security reasons, the OCC requires that visitors make an appointment to inspect comments. You may do so by calling (202) 874–4700. Upon arrival, visitors must present valid government-issued photo identification and submit to security screening in order to inspect and photocopy comments.

- **Docket**: You may view or request available background documents and project summaries using the methods described above.

- **Board**: You may submit comments, identified by Docket No. R–1368, by any of the following methods:
  - **Federal eRulemaking Portal**: http://www.regulations.gov. Follow the instructions for submitting comments.

- **E-mail**: reg.s.comments@occ.treas.gov.

- **Fax**: (202) 874–5274.
- **Hand Delivery/Courier**: 250 E Street, SW., Mail Stop 2–3, Washington, DC 20219.

- **FAX**: (202) 452–3819 or (202) 452–3102.
- **Mail**: Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551.

All public comments are available from the Board’s Web site at http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm as submitted, unless modified for technical reasons. Accordingly, your comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper form in Room MP–500 of the Board’s Martin Building (20th and C Street, NW.) between 9 a.m. and 5 p.m. on weekdays.

**FDIC**: You may submit comments by any of the following methods:

- **Federal eRulemaking Portal**: http://www.regulations.gov. Follow the instructions for submitting comments.


- **Mail**: Robert E. Feldman, Executive Secretary, Attention: Comments/Legal ESS, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.

- **Hand Delivered/Courier**: The guard station at the rear of the 550 17th Street Building (located on F Street), on business days between 7 a.m. and 5 p.m.

- **E-mail**: comments@FDIC.gov.

**Instructions**: Comments submitted must include “FDIC” and “RIN 3064–AD48.” Comments received will be posted without change to http://www.FDIC.gov/regulations/laws/federal/propose.html, including any personal information provided.

**OTS**: You may submit comments, identified by OTS–2009–0015, by any of the following methods:

- **Federal eRulemaking Portal**: “Regulations.gov”: Go to http://www.regulations.gov. Under the “More Search Options” tab click next to the “Advanced Document Search” option where indicated, select “Office of Thrift Supervision” from the agency drop-down menu, then click “Submit.” In the “Docket ID” column, select “OTS–2009–0015” to submit or view public comments and to view supporting and related materials for this proposed rulemaking. The “How to Use This Site” link on the Regulations.gov home page provides information on using Regulations.gov, including instructions for submitting or viewing public comments, viewing other supporting and related materials, and viewing the docket after the close of the comment period.

- **Fax**: (202) 452–3819 or (202) 452–3102.
- **Mail**: Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551.

All public comments are available from the Board’s Web site at http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm as submitted, unless modified for technical reasons. Accordingly, your comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper form in Room MP–500 of the Board’s Martin Building (20th and C Street, NW.) between 9 a.m. and 5 p.m. on weekdays.

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- **Mail**: Robert E. Feldman, Executive Secretary, Attention: Comments/Legal ESS, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.

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- **E-mail**: comments@FDIC.gov.

**Instructions**: Comments submitted must include “FDIC” and “RIN 3064–AD48.” Comments received will be posted without change to http://www.FDIC.gov/regulations/laws/federal/propose.html, including any personal information provided.

**OTS**: You may submit comments, identified by OTS–2009–0015, by any of the following methods:

- **Federal eRulemaking Portal**: “Regulations.gov”: Go to http://www.regulations.gov. Under the “More Search Options” tab click next to the “Advanced Document Search” option where indicated, select “Office of Thrift Supervision” from the agency drop-down menu, then click “Submit.” In the “Docket ID” column, select “OTS–2009–0015” to submit or view public comments and to view supporting and related materials for this proposed rulemaking. The “How to Use This Site” link on the Regulations.gov home page provides information on using Regulations.gov, including instructions for submitting or viewing public comments, viewing other supporting and related materials, and viewing the docket after the close of the comment period.
appointments will be available the next 10 a.m. and 4 p.m. In most cases, appointments on business days between materials you will be requesting will send a facsimile transmission to (202) e-mail to public.info@ots.treas.gov for access, call (202) 906–5922, send an appointment. To make an appointment may inspect comments at the Public comments for this notice of proposed ‘’Submit.’’ In the ‘’Docket ID’’ column, agency drop-down menu, then click ‘’Office of Thrift Supervision’’ from the Search’’ option where indicated, select http://www.regulations.gov Go to supporting materials that you consider information in your comment or the public record and subject to public supporting materials received are part of information provided. Comments, including attachments and other public disclosure. Do not enclose any information in your comment or supporting materials that you consider confidential or inappropriate for public disclosure.

Viewing Comments Electronically: Go to http://www.regulations.gov, under the ‘’More Search Options’’ tab click next to the ‘’Advanced Document Search’’ option where indicated, select ‘’Office of Thrift Supervision’’ from the agency drop-down menu, then click ‘’Submit.’’ In the ‘’Docket ID’’ column, select ‘’OTS–2009–0015’’ to view public comments for this notice of proposed rulemaking action.

Viewing Comments On-Site: You may inspect comments at the Public Reading Room, 1700 G Street, NW., by appointment. To make an appointment for access, call (202) 906–5922, send an e-mail to public.info@ots.treas.gov, or send a facsimile transmission to (202) 906–6518. (Prior notice identifying the materials you will be requesting will assist us in serving you.) We schedule appointments on business days between 10 a.m. and 4 p.m. In most cases, appointments will be available the next business day following the date we receive a request.


Board: Barbara J. Bouchard, Associate Director, (202) 452–3072, or Anna Lee Hewko, (202) 530–6260, Manager, Supervision Policy and Guidance, Division of Banking Supervision and Regulation; or April C. Snyder, Counsel, (202) 452–3099, or Benjamin W. McDonough, Senior Attorney, (202) 452–2036, Legal Division. For the hearing impaired only, Telecommunication Device for the Deaf (TDD), (202) 263–4869.


SUPPLEMENTARY INFORMATION:

I. Background

The agencies’ regulatory capital regime for banking organizations 1 incorporates both leverage and risk-based measures. The leverage measure 2 uses on-balance sheet assets as the basis for setting capital requirements that are intended to limit the degree to which a banking organization can leverage its equity capital base. The risk-based measures (the general risk-based capital rules 3 and the advanced approaches rules) 4 establish capital requirements intended to reflect the risks associated with on-balance sheet exposures as well as off-balance sheet exposures, such as guarantees, commitments, and derivative transactions. The agencies use generally accepted accounting principles (GAAP), as established by FASB, as the initial basis for determining whether an exposure is treated as on- or off-balance sheet for regulatory capital purposes.

The GAAP treatment for structured finance transactions using a special purpose entity (SPE) generally has been governed by the requirements of Statement of Financial Accounting Standards No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities (FAS 140) and FASB Interpretation No. 46R, Consolidation of Variable Interest Entities (FIN 46(R)). Under FAS 140 (as currently in effect), transfers of assets to an entity that meets the definition of a qualifying special purpose entity (QSPE) are usually recognized as sales, which permits the transferor to remove the assets from its balance sheet. 5 In addition, FIN 46(R) specifically excludes QSPEs from its scope despite the fact that many QSPEs would have otherwise been deemed variable interest entities (VIEs) subject to FIN 46(R) and possible consolidation. On June 12, 2009, FASB finalized modifications to FAS 140 and FIN 46(R) (the 2009 GAAP modifications) through Statement of Financial Accounting Standards No. 166, Accounting for Transfers of Financial Assets, an Amendment of FASB Statement No. 140 (FAS 166), and Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46(R) (FASB 2003).

2 Under FAS 167, all transfers of assets are recognized as sales if the transferor no longer has a controlling financial interest in the QSPE. Under FIN 46(R), transfers of assets are recognized as sales if the transferor no longer has residual interests.

I. The 2009 GAAP Modifications

Under FAS 167, a VIE is an entity whose equity investment at risk is insufficient to permit the entity to finance its activities without additional subordinated financial support for

10 Statement of Financial Accounting Standards No. 140 (FASB 2000) and Interpretation No. 46R (FASB 2003). All references made to FASB Statements of Financial Accounting Standards and Interpretations have been or will soon be included in the FASB Accounting Standards Codification that became effective on July 1, 2009.

11 The transfers are recognized as sales as long as they meet other criteria contained in the 2009 version of FAS 140, as amended. See FAS 140, paragraph 9.

12 See relevant provisions in FAS 166 paragraphs 5–7 and FAS 167 paragraphs 7–10.
example, an entity with nominal common equity and/or whose equity investors do not have rights or obligations with respect to the entity typical of equity investors. For example, a VIE generally exists when the administrators of an entity hold a nominal common equity interest, and debt holders hold the rest of the economic interests in the entity (which frequently are issued in various degrees of subordination). Similarly, an entity is a VIE if its equity holders, as a group, lack the right to make decisions about the entity’s activities; the obligation to absorb losses of the entity, or the right to receive the expected residual returns of the entity. Thus, for example, an entity whose debt holders, rather than its common equity holders, have all essential voting rights and the rights to receive all revenue generated by the entity’s assets, generally would be a VIE.

Determining whether a specific company is required to consolidate a VIE under FAS 167 depends on a qualitative analysis of whether that company has a “controlling financial interest” in the VIE. The analysis focuses on the company’s power over and interest in the VIE, rather than on quantitative equity ownership thresholds. A company has a controlling financial interest in a VIE if it has (1) the power to direct matters that most significantly impact the activities of the VIE, including, but not limited to, activities that impact the VIE’s economic performance (for example, servicing activities); and (2) either the obligation to absorb losses of the VIE that potentially could be significant to the VIE, or the right to receive benefits from the VIE that potentially could be significant to the VIE, or both. A company’s analysis of whether it must consolidate a VIE must incorporate the above criteria and take into account the company’s interest(s) in the VIE and the characteristics of the VIE, including the involvement of other VIE interest holders. FAS 167 also requires a company to conduct ongoing assessments using the above criteria to determine whether a VIE is subject to consolidation.11

FAS 166 amends FAS 140 by removing the QSPE concept from GAAP, strengthening the requirements for recognizing the transfer of financial assets to a third party, and requiring companies to make additional disclosures about any continuing involvement they may have in financial assets that they transfer.12 As a result, a company that transferred financial assets to an SPE that previously met the definition of a QSPE must now evaluate whether it must consolidate the assets, liabilities, and equity of the SPE pursuant to FAS 167. Furthermore, under the additional disclosure requirements in FAS 166, companies must detail in their financial statements their continuing involvement—through recourse or guarantee arrangements, servicing arrangements, or other relationships—in any financial assets that they transfer to an SPE (whether or not a company is required to consolidate the SPE following the transfer). These disclosure requirements apply as long as a transferring company is involved in financial assets that it has transferred.13

The 2009 GAAP modifications do not provide for the grandfathering of existing financial structures. Most banking organizations that will be required to consolidate and recognize on their balance sheets many previously unconsolidated VIEs due to the 2009 GAAP modifications will consolidate as of January 1, 2010.14 These newly consolidated entities will therefore be included in relevant regulatory reports of banking organizations, such as the bank Reports of Condition and Income (Call Reports), the Thrift Financial Report (TRF), and the bank holding company financial statements (FR Y—9C Report). A preliminary analysis of the 2009 GAAP modifications, as well as analysis derived from the agencies’ supervisory information, indicates that the categories of off-balance sheet exposures likely to be subject to consolidation on an originating or servicing banking organization’s balance sheet include:

- Certain asset-backed commercial paper (ABCP) conduits;
- Revolving securitizations structured as master trusts, including credit card and home equity line of credit (HELOC) securitizations;
- Certain mortgage loan securitizations not guaranteed by the U.S. government or a U.S. government-sponsored agency;
- Certain term loan securitizations in which a banking organization retains a residual interest and servicing rights, including some student loan and automobile loan securitizations; and
- Other SPEs, such as certain tender option bond trusts that were designed as QSPEs.

The 2009 GAAP modifications may also require banking organizations to recognize on their balance sheets certain loan participations and other exposures not related to asset securitization. In addition, banking organizations may need to establish loan loss reserves to cover incurred losses on the assets consolidated pursuant to the 2009 GAAP modifications. Each banking organization must determine which structures and exposures must be consolidated onto its balance sheet, and assess other appropriate adjustments to relevant financial reports, as a result of the 2009 GAAP modifications.

*Question 1:* Which types of VIEs will banking organizations have to consolidate onto their balance sheets due to the 2009 GAAP modifications, which types are not expected to be subject to consolidation, and why? Which types are likely to be restructured to avoid consolidation?

**III. Regulatory Capital and the 2009 GAAP Modifications**

The agencies’ capital standards generally use GAAP treatment of an exposure as a starting point for assessing regulatory capital requirements for that exposure. For example, if certain assets of a banking organization are transferred to a VIE through a secured financing but remain on the banking organization’s balance sheet under GAAP, the VIE’s assets are risk-weighted like other consolidated assets. However, if those assets are securitized through sale to a VIE that the banking organization does not consolidate under GAAP, generally the banking organization is required to

11 Under GAAP, an allowance for loan and lease losses (ALLL) should be recognized when events have occurred indicating that it is probable that an asset has been impaired or that a liability has been incurred as of the balance sheet date and that the amount of the loss can be reasonably estimated. Under the risk-based capital rules, the ALLL is a component of tier 2 capital and, therefore, included in the numerator of the total risk-based capital ratio. However, the amount of ALLL that may be included in tier 2 capital is limited to 1.25 percentage points of gross risk-weighted assets.
hold risk-based capital only against its contractual exposures to the VIE. The contractual exposures may take the form of off-balance sheet exposures such as asset-backed securities and residual interests, and off-balance sheet exposures such as liquidity facilities. The 2009 GAAP modifications generally would increase the amount of exposures recognized on banking organizations’ balance sheets. Accordingly, under the agencies’ current regulatory capital requirements, the 2009 GAAP modifications generally would result in higher regulatory capital requirements for those banking organizations that must consolidate VIEs.

Under the agencies’ leverage capital requirements, tier 1 capital is assessed against a measure of a banking organization’s total assets, net of the ALLL and certain other exposures. Therefore, previously unconsolidated assets that now must be recognized on a banking organization’s balance sheet due to the 2009 GAAP modifications will increase the denominator of the banking organization’s leverage ratio. Although the 2009 GAAP modifications will also affect the numerator of the risk-based and leverage capital ratios, in many cases both the risk-based and leverage capital ratios of affected banking organizations will decrease following implementation of the 2009 GAAP modifications.

The risk-based capital ratios, which reflect the components of regulatory capital and recognize variations of risk levels among different exposures through different risk-weight assignments. Although for many years the agencies have used financial information reported under GAAP as the starting point for banking organizations’ regulatory reporting requirements, the risk-based capital rules adjust GAAP balance sheet inputs where appropriate to capture an exposure’s risk or the ability of elements of capital to absorb loss.

In their consideration of the 2009 GAAP modifications and the interaction of the modifications with the regulatory capital requirements, the agencies have determined that the qualitative analysis required under FAS 167, as well as the enhanced requirements for recognizing transfers of financial assets under FAS 166, converge in many respects with the agencies’ assessment of a banking organization’s risk exposure to a structured finance transaction and other transactions affected by the 2009 GAAP modifications.

In the case of some structures that banking organizations were not required to consolidate prior to the 2009 GAAP modifications, the recent turmoil in the financial markets has demonstrated the extent to which the credit risk exposure of the sponsoring banking organization to such structures (and their related assets) has in fact been greater than the agencies estimated, and more associated with non-contractual considerations than the agencies had expected. For example, recent performance data on structures involving revolving assets show that banking organizations have often provided non-contractual (implicit) support to prevent senior securities of the structure from being downgraded, thereby mitigating reputational risk and the associated alienation of investors, and preserving access to cost-effective funding.

In light of this recent experience, the agencies believe that the broader accounting consolidation requirements implemented by the 2009 GAAP modifications will result in a regulatory capital treatment that more appropriately reflects the risks to which banking organizations are exposed. Additionally, the 2009 GAAP modifications require that a banking organization regularly update its consolidation analysis with respect to VIEs, and the enhanced requirements for recognition of asset transfers and ongoing disclosure requirements for financial assets with which the banking organization maintains some relationship. These requirements are consistent with the agencies’ view that the capital treatment of some previously unconsolidated VIEs does not reflect the actual risk to which the banking organization may be exposed.

Question 2: Are there features and characteristics of securitization transactions or other transactions with VIEs, other SPEs, or other entities that are more or less likely to elicit banking organizations’ provision of non-contractual (implicit) support under stressed or other circumstances due to reputational risk, business model, or other reasons? Commenters should describe such features and characteristics and the methods of support that may be provided. The agencies are particularly interested in comments regarding credit card securitizations, structured investment vehicles, money market funds, hedge funds, and other entities that are likely beneficiaries of non-contractual support.

The banking agencies have carefully considered the probable impact on banking organizations’ regulatory capital ratios that will result from the 2009 GAAP modifications and the possible alignments between these effects and the risk-based principles of the risk-based capital rules. The agencies have also carefully considered the potential financial impact of the 2009 GAAP modifications on banking organizations. As part of this consideration, the agencies reviewed relevant data from banking organizations’ public financial filings and regulatory reports as well as information obtained from the supervisory process, including the results of the Supervisory Capital Assessment Program (SCAP). The SCAP evaluated the capital position of the nineteen largest U.S. banking organizations, which are also the banking organizations most involved in asset securitization. As part of the SCAP, participating banking organizations’ capital adequacy was assessed using consolidation assumptions consistent with standards ultimately included in FAS 166 and FAS 167.

Having considered this information, including the SCAP results, the agencies do not, at this time, find that a compelling basis exists for modifying their regulatory capital requirements to alter the effect of the 2009 GAAP modifications on banking organizations’ minimum regulatory capital
requirements. Furthermore, as discussed above, the banking agencies believe that the capital treatment of many exposures that would be consolidated under the new accounting standards aligns with risk-based capital principles and results in more appropriate risk-based capital charges. The agencies also believe that it is most appropriate for the leverage ratio to continue to reflect the total on-balance sheet assets of a banking organization, in keeping with its role as a supplement to the risk-based capital measure that limits the maximum degree to which a banking organization can leverage its equity capital base.  

**Question 3:** What effect will the 2009 GAAP modifications have on banking organizations’ financial positions, lending, and activities? How will the modifications impact lending typically financed by securitization and lending in general? How may the modifications affect the financial markets? What proportion of the impact is related to regulatory capital requirements? Commenters should provide specific responses and supporting data.

**Question 4:** As is generally the case with respect to changes in accounting rules, the 2009 GAAP modifications would immediately affect banking organizations’ capital requirements. The agencies specifically request comment on the impact of immediate application of the 2009 GAAP modifications on the regulatory capital requirements of banking organizations that were not included in the SCAP. In light of the potential impact at this point in the economic cycle of the 2009 GAAP modifications on regulatory capital requirements, the agencies solicit comment on whether there are significant costs and burdens (or benefits) associated with immediate application of the 2009 GAAP modifications to regulatory capital requirements. If there are significant costs and burdens, or other relevant considerations, should the agencies consider a phase-in of the capital requirements that would result from the 2009 GAAP modifications? Commenters should provide specific and detailed rationales and supporting evidence and data to support their positions.

Additionally, if a phase-in of the impact of the GAAP modifications is appropriate, what type of phase-in should be considered? For example, would a phase-in over the course of a four-quarter period, as described below, for transactions entered into on or prior to December 31, 2009, reduce costs or burdens without reducing benefits? Under a four-quarter phase-in approach, the amount of a newly-consolidated VIE’s assets that would be subject to the phase-in would be limited to the aggregate value of the assets held by the entity as of the last day of the fiscal year prior to its implementation of the 2009 GAAP modifications. For most banking organizations, the aggregate value would be calculated as of December 31, 2009. During such a phase-in, banking organizations would be required to hold capital (for purposes of calculating both the leverage and risk-based capital ratios) incrementally against 25 percent of exposures subject to consolidation due to the 2009 GAAP modifications for each of the first three quarters of 2010, and against 100 percent of the exposures thereafter. For example, if, as a result of the 2009 GAAP modifications, a banking organization would have to consolidate $10 billion of assets associated with transactions entered into on or before December 31, 2009, it would be required to include $2.5 billion of these assets in its regulatory capital ratios the first quarter 2010, $5 billion the second, $7.5 billion the third, and the full $10 billion of assets in the fourth quarter and future reporting periods. During such a phase-in period, the amount of capital that an institution holds against all of its exposures to a single VIE as of December 31, 2009, would not be reduced as a result of this phase-in. For example, if a banking organization is effectively required to hold risk-based capital against all exposures in a VIE due to a provision of implicit recourse, that capital treatment would continue throughout 2010. For another example, if in the first quarter of the phase-in the amount of capital required for a banking organization’s credit enhancements to a securitization on December 31, 2009, exceeds the amount of capital required for 25 percent (the first quarter phase-in amount) of the newly consolidated underlying assets, the banking organization would be required to hold the greater amount of capital.

Regulatory capital rules establish only a minimum capital requirement. In all cases, banking organizations should hold capital commensurate with the level and nature of the risks to which they are exposed. Supervisors will review a banking organization’s securitization and other structured finance activities on an individual transaction and business-line basis, and may require a banking organization to increase its capital if they conclude that its capital position is not commensurate with its risk. 

**IV. Asset-Backed Commercial Paper Programs**

The agencies propose to eliminate existing provisions in the risk-based capital rules that permit a banking organization, if it is required to consolidate under GAAP an ABCP program that it sponsors, to exclude the consolidated ABCP program assets from risk-weighted assets and instead assess the risk-based capital requirement against any contractual exposures of the organization arising from such ABCP programs. The agencies also propose to eliminate the associated provision in the general risk-based capital rules (incorporated by reference in the advanced approaches) that excludes from tier 1 capital the majority interest in a consolidated ABCP program not included in a banking organization’s risk-weighted assets. The agencies initially implemented these provisions in the general risk-based capital rules in 2004 in response to changes in GAAP that required consolidation of certain ABCP conduits by sponsors. The provisions were driven largely by the agencies’ belief at the time that banking organizations sponsoring ABCP conduits generally faced limited risk exposures to ABCP programs, because these exposures generally were confined to the credit enhancements and liquidity facility arrangements banking organizations provide to these programs.

Additionally, the agencies believed previously that operational controls and structural provisions, as well as over-collateralization or other credit enhancements provided by the companies that sell assets into ABCP programs, could further mitigate the risk to which sponsoring banking organizations were exposed. However, in light of the increased incidence of

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23 12 CFR part 3.4(a)(1)(OCC); 12 CFR parts 208 and 225, appendix A §1 (Board); 12 CFR part 325, appendix A §1A (FDIC); 12 CFR 567.11 (OTS).
26 See 69 FR 44980 (July 28, 2004).
banking organizations providing non-contractual support to these programs, as well as the general credit risk concerns discussed above, the agencies have reconsidered the appropriateness of excluding consolidated ABCP program assets from risk-weighted assets and have determined that continuing the exclusion is no longer justified. Under the proposal, if a banking organization is required to consolidate an entity associated with an ABCP program under GAAP, it must hold regulatory capital against the assets of the entity. It would not be permitted to calculate its risk-based capital requirements with respect to the entity based on its contractual exposure to the entity.

V. Reservation of Authority

The agencies expect that there may be instances when a banking organization structures a financial transaction with an SPE to avoid consolidation under FAS 166 and FAS 167, and the resulting capital treatment is not commensurate with the actual risk relationship of the banking organization to the entity. Under this proposal, the banking organization’s primary Federal supervisor would retain the authority to require the banking organization to treat the entity as if it were consolidated onto the banking organization’s balance sheet for risk-based capital purposes.

Question 6: Does this proposal raise competitive equity concerns with respect to accounting and regulatory capital treatments in other jurisdictions or with respect to international accounting standards?

Although the agencies believe that GAAP, as modified, should remain the starting point for calculating regulatory capital ratios and that the capital requirements resulting from the 2009 GAAP modifications generally will result in a more appropriate reflection of credit risk, the agencies recognize that the principles underlying the 2009 GAAP modifications—power, benefits, and obligation to bear losses—and the resulting consolidation treatment, may not in all respects correspond to a treatment that would result from a more pure risk focus.

Question 7: Among the structures that likely will be consolidated under the 2009 GAAP modifications, for which types, if any, should the agencies consider assessing a different risk-based capital requirement than the capital treatment that will result from the implementation of the modifications? How are commenters’ views influenced by proposals for reforming the securitization markets that require securitizers to retain a percentage of the credit risk on any asset that is transferred, sold or conveyed through a securitization?

Question 8: Services of securitized residential mortgages who participate in the Treasury’s Making Home Affordable Program (MHAP) receive certain incentive payments in connection with loans modified under the program. If a structure must be consolidated solely due to loan modifications under MHAP, should these assets be included in the leverage and risk-based capital requirements?

Question 9: Which features and characteristics of transactions that may not be subject to consolidation after the 2009 GAAP modifications become effective should be subject to risk-based capital requirements as if consolidated in order to more appropriately reflect risk?

Question 10: Will securitized loans that remain on the balance sheet be subjected to the same ALLL provisioning process, including comparable loss rates, as similar loans that are not securitized? If the answer is no, please explain. If the answer is yes, how would banking organizations reflect the benefits of risk sharing if investors in securitized, on-balance sheet loans absorb realized credit losses? Commenters should provide a detailed explanation and supporting empirical analysis of why the features and characteristics of these structure types merit an alternative treatment, how the risks of the structures should be measured, and what an appropriate alternative capital treatment would be. Responses should also discuss in detail with supporting evidence how such different capital treatment may or may not give rise to capital arbitrage opportunities.

VI. Regulatory Analysis

Regulatory Flexibility Act

The Regulatory Flexibility Act, 5 U.S.C. 601 et seq. (RFA), generally requires that, in connection with a notice of proposed rulemaking, an agency prepare and make available for public comment an initial regulatory flexibility analysis that describes the impact of a proposed rule on small entities. Under regulations issued by the Small Business Administration, a small entity includes a commercial bank, bank holding company, or savings association with assets of $175 million or less (a small banking organization). As of June 30, 2009, there were approximately 2,533 small bank holding companies, 385 small savings associations, 749 small national banks, 432 small State member banks, and 3,040 small State nonmember banks.

Other than the proposed modifications to the risk-based capital rules that would no longer allow banking organizations to exclude consolidated ABCP programs from risk-weighted assets, the proposed rule does not impose any additional obligations, restrictions, burdens, or reporting, recordkeeping or compliance requirements on banks or savings associations, including small banking organizations, nor does it duplicate, overlap or conflict with other Federal rules. The agencies expect that the proposed modifications to the risk-based capital rules would not materially affect small banking organizations because they do not sponsor ABCP programs.

Paperwork Reduction Act

In accordance with the requirements of the Paperwork Reduction Act of 1995
(44 U.S.C. 3506), the agencies have reviewed the proposed rule. The Board reviewed the proposed rule under the authority delegated to the Board by the Office of Management and Budget. The agencies note that instructions related to ABCP conduits in schedule RC–R of the Consolidated Reports of Condition and Income (OMB Nos. 7100–0036, 1557–0081, and 3064–0052; FFIEC 031 and 041) and schedule HC–R of the Consolidated Financial Statements for Bank Holding Companies (OMB No. 7100–0128; FR Y–9C) would need to be revised under the proposal. The agencies, however, do not believe that there would be any additional burden associated with these instructional changes as they would be in accordance with GAAP.

OCC/OTS Executive Order 12866

Executive Order 12866 requires Federal agencies to prepare a regulatory impact analysis for agency actions that are found to be “significant regulatory actions.” Significant regulatory actions include, among other things, rulemakings that “have an annual effect on the economy of $100 million or more or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or Tribal governments or communities.” The OCC and the OTS each determined that its portion of the proposed rule is not a significant regulatory action under Executive Order 12866.

OCC/OTS Unfunded Mandates Reform Act 1995 Determination

The Unfunded Mandates Reform Act of 1995 29 (UMRA) requires that an agency prepare a budgetary impact statement before promulgating a rule that includes a Federal mandate that may result in the expenditure by State, local, and Tribal governments, in the aggregate, or by the private sector of $100 million or more (adjusted annually for inflation) in any one year. If a budgetary impact statement is required, section 205 of the UMRA also requires an agency to identify and consider a reasonable number of regulatory alternatives before promulgating a rule. The OCC and the OTS each have determined that its proposed rule will not result in expenditures by State, local, and Tribal governments, in the aggregate, or by the private sector, of $100 million or more in any one year. Accordingly, neither the OCC nor the OTS has prepared a budgetary impact statement or specifically addressed the regulatory alternatives considered.

Solicitation of Comments on Use of Plain Language

Section 722 of the GLBA required the agencies to use plain language in all proposed and final rules published after January 1, 2000. The agencies invite comment on how to make this proposed rule easier to understand. For example:

- Have the agencies organized the material to suit your needs? If not, how could they present the rule more clearly?
- Are the requirements in the rule clearly stated? If not, how could the rule be more clearly stated?
- Do the regulations contain technical language or jargon that is not clear? If so, which language requires clarification?
- Would a different format (grouping and order of sections, use of headings, paragraphing) make the regulation easier to understand? If so, what changes would achieve that?
- Is this section format adequate? If not, which of the sections should be changed and how?
- What other changes can the agencies incorporate to make the regulation easier to understand?

List of Subjects

12 CFR Part 3

Administrative practice and procedure, Banks, Banking, 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, Risk.

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, Risk, Savings associations.
interests), and loans that a bank may provide to such a variable interest entity are not subject to any capital charge under section 4 of this appendix A.

4. In appendix C to Part 3:
   A. In section 1, redesignate paragraph (c)(3) as paragraph (c)(4).
   B. Add a new paragraph (c)(3).
   C. Remove section 42(l) and redesignate section 42(m) as section 42(l).

The additions and revisions read as follows:

Appendix C to Part 3—Capital Adequacy Guidelines for Banks: Internal-Ratings-Based and Advanced Measurement Approaches

* * * * *

Section 1. * * *

(c) * * *

(3) Regulatory capital treatment of unconsolidated entities. If the OCC determines that the capital treatment for a banking organization’s exposure or other relationship to an entity not consolidated on the bank’s balance sheet is not commensurate with the actual risk relationship of the banking organization to the entity, for risk-based capital purposes, it may require the banking organization to treat the entity as if it were consolidated onto the bank’s balance sheet and require the bank to hold capital against the entity’s exposures. The OCC will look to the substance of and risk associated with the transaction as well as other relevant factors the OCC deems appropriate in determining whether to require such treatment and in determining the bank’s compliance with minimum risk-based capital requirements. In making a determination under this paragraph, the OCC will apply notice and response procedures in the same manner and to the same extent as the notice and response procedures in 12 CFR 3.12.

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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 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)

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


6. In appendix A to part 208:
   A. Amend section I by adding a new paragraph immediately prior to the last undesignated paragraph.
   B. Amend paragraph (c) of section II.A.1 by removing the last sentence.
   C. Remove paragraph (b) of section III.B.6 and redesignate paragraph (c) of section III.B.6 as paragraph (b).

The addition reads as follows:

Appendix A to Part 208—Capital Adequacy Guidelines for State Member Banks: Risk-Based Measure

I. * * *

If the Federal Reserve determines that the capital treatment for a banking organization’s exposure or other relationship to an entity not consolidated on the banking organization’s balance sheet is not commensurate with the actual risk relationship of the banking organization to the entity, for risk-based capital purposes, it may require the banking organization to treat the entity as if it were consolidated onto the banking organization’s balance sheet and require the banking organization to hold capital against the entity’s exposures.

* * * * *

7. In appendix F to part 208:
   A. Redesignate paragraph (c)(3) as (c)(4) and add a new paragraph (c)(3).
   B. Remove section 42(l) and redesignate section 42(m) as section 42(l).

The addition reads as follows:

Appendix F to Part 208—Capital Adequacy Guidelines for Banks: Internal-Ratings-Based and Advanced Measurement Approaches

* * * * *

Section 1. * * *

(c) * * *

(3) Regulatory capital treatment of unconsolidated entities. If the Federal Reserve determines that the capital treatment for a bank’s exposure or other relationship to an entity not consolidated on the bank’s balance sheet is not commensurate with the actual risk relationship of the bank to the entity, for risk-based capital purposes, it may require the bank to treat the entity as if it were consolidated onto the bank’s balance sheet and require the bank to hold capital against the entity’s exposures.

* * * * *

10. In appendix G to part 225:
   A. In section 1, redesignate paragraph (c)(3) as paragraph (c)(4) and add a new paragraph (c)(3).
   B. Remove section 42(l) and redesignate section 42(m) as section 42(l).

The added text will read as follows:

Appendix F to Part 208—Capital Adequacy Guidelines for Banks: Internal-Ratings-Based and Advanced Measurement Approaches

* * * * *

1. * * *

(c) * * *

(3) Regulatory capital treatment of unconsolidated entities. If the Federal Reserve determines that the capital treatment for a banking organization’s exposure or other relationship to an entity not consolidated on the banking organization’s balance sheet is not commensurate with the actual risk relationship of the banking organization to the entity, for risk-based capital purposes, it may require the banking organization to treat the entity as if it were consolidated onto the banking organization’s balance sheet and require the banking organization to hold capital against the entity’s exposures.

Federal Deposit Insurance Corporation

12 CFR Chapter III

Authority for 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

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

12. In Appendix A to part 325, A. Revise section I.A.1.(d); B. Amend section II.A. by adding a new paragraph 4; C. Remove section II.B.6.b. and redesignate section II.B.6.c. as section II.B.6.b.

The added text to read as follows:

Appendix A to Part 325—Statement of Policy on Risk Based Capital

* * * * *

I. * * *

A. * * * *

1. * * * *

(d) Minority interests in small business investment companies, investment funds that hold nonfinancial equity investments [as defined in section II.B.(6)(ii) of this appendix A], and subsidiaries that are engaged in non-financial activities are not included in the bank’s Tier 1 or total capital base if the bank's interest in the company or fund is held under one of the legal authorities listed in section II.B.(6)(ii) of this appendix A.

* * * * *

II. * * *

A. * * * *

4. The Director of the Division of Supervision and Consumer Protection (DSC) may, on a case-by-case basis, determine that the regulatory capital treatment for an exposure to a transaction that is not subject to consolidation on the balance sheet is not commensurate with the risk of the exposure and the relationship of the bank to the transaction. In making this determination, the DSC may require the bank to treat the transaction as if it were consolidated on the balance sheet of the bank for regulatory capital purposes and calculate the appropriate regulatory capital ratios accordingly.

* * * * *

13. In Appendix D to part 325, A. Amend section 1(c) by redesigning paragraph 4(c)(3) as paragraph 4(c)(4) and adding a new paragraph 4(c)(3);

B. Remove section 42(l) and redesignate section 42(m) as section 42(l)

The added text should read as follows:

Appendix D to Part 325—Capital Adequacy Guidelines for Banks: Internal-Ratings-Based and Advanced Measurement Approaches

* * * * *

Section 1. * * *

(c) * * *

(3) OTS may find that the capital treatment for an exposure to a transaction not subject to consolidation on the savings association’s balance sheet does not appropriately reflect the risks imposed on the savings association. Accordingly, OTS may require the savings association to treat the transaction as if it were consolidated on the savings association’s balance sheet. OTS will look to the substance of and risk associated with the transaction as well as other relevant factors in determining whether to require such treatment and in calculating regulatory capital as OTS deems appropriate.

* * * * *

(d) In making a determination under this paragraph (c) of this section, the OTS will notify the savings association of the determination and solicit a response from the savings association. After review of the response by the savings association, the OTS shall issue a final supervisory decision regarding the determination made under paragraph (c) of this section.

18. In Appendix C to part 567, Section 1, redesignate paragraph (c)(3) as paragraph (c)(4) to read as follows:

Appendix C to Part 567—Risk-Based Capital Requirements—Internal Ratings-Based and Advanced Measurement Approaches

* * * * *

(c) * * *

(3) Regulatory capital treatment of unconsolidated entities. OTS may find that the capital treatment for an exposure to a transaction not subject to consolidation on the savings association’s balance sheet does not appropriately reflect the risks imposed on the savings association. Accordingly, OTS may require the savings association to treat the transaction as if it were consolidated on the savings association’s balance sheet. OTS will look to the substance of and risk associated with the transaction as well as other relevant factors in determining whether to require such treatment and in calculating regulatory capital as OTS deems appropriate.

(4) Other supervisory authority. Nothing in this appendix limits the authority of the OTS 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.

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Appendix C to Part 567—[Amended]

19. In appendix C to part 567 remove section 42(l) and redesignate section 42(m) as section 42(l).

By order of the Board of Governors of the Federal Reserve System.

Jennifer J. Johnson,
Secretary of the Board.

Dated: Washington, DC, this 27th day of August 2009.

By order of the Board of Directors.

Robert E. Feldman,
Executive Secretary.

John C. Dugan,
Comptroller of the Currency.

By the Office of Thrift Supervision.

John E. Bowman,
Acting Director.

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