

**FEDERAL RESERVE SYSTEM**  
**12 CFR Parts 208 and 225**  
**[Regulations H and Y; Docket No. R-1117]**

**Risk-Based Capital Guidelines; Supplementary Capital Elements (Tier 2 Capital); Deferred Tax Assets**

**AGENCY:** Board of Governors of the Federal Reserve System.

**ACTION:** Proposed rule with request for comment.

**SUMMARY:** The Board of Governors of the Federal Reserve System (Board) is proposing to amend its risk-based capital guidelines to clarify that deferred tax assets in excess of the allowable amount (disallowed deferred tax assets) are included in the items that are deducted from tier 1 capital for the purpose of determining the maximum allowable amount of tier 2 capital that a banking organization may include in qualifying total capital and the maximum allowable amount of term subordinated debt and intermediate-term preferred stock that may be treated as supplementary capital. The proposed rule would reduce the maximum allowable amount of tier 2 capital for institutions that have disallowed deferred tax assets, as well as the amount of term subordinated debt and intermediate-term preferred stock that those institutions could include in supplementary capital. This clarification will make the Federal Reserve's capital guidelines consistent with those of the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS).

**DATES:** Comments must be received by December 27, 2001.

**ADDRESSES:** Comments should refer to Docket No. R-1117 and should be mailed to Ms. Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551, or mailed electronically to [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov). Comments addressed to Ms. Johnson may also be delivered to

the Board's mail facility in the West Courtyard between 8:45 a.m. and 5:15 p.m., located on 21st Street between Constitution Avenue and C Street, N.W. Members of the public may inspect comments in Room MP-500 of the Martin Building between 9:00 a.m. and 5:00 p.m. on weekdays pursuant to § 261.12, except as provided in § 261.14, of the Board's Rules Regarding Availability of Information, 12 CFR 261.12 and 261.14.

**FOR FURTHER INFORMATION CONTACT:** Barbara Bouchard, Associate Director (202/452-3072), or David Adkins, Supervisory Financial Analyst (202/452-5259), Division of Banking Supervision and Regulation. For users of Telecommunications Device for the Deaf (“TDD”) only, contact 202/263-4869.

**SUPPLEMENTARY INFORMATION:** Under the Board’s risk-based capital guidelines, banking organizations must deduct disallowed deferred tax assets from tier 1 capital, along with goodwill and certain other intangible assets.<sup>1</sup> As a general rule, the maximum amount of tier 2 capital that may be included in an organization’s qualifying total capital is limited to 100 percent of tier 1 capital. In addition, the aggregate amount of term subordinated debt (excluding mandatory convertible debt) and intermediate-term preferred stock that may be treated as supplementary capital is limited to 50 percent of tier 1 capital. However, for purposes of these two limitations, the Board’s current guidelines define tier 1 capital as net of goodwill and certain other intangible assets but not of disallowed deferred tax assets. This treatment is inconsistent with that of the OCC, the FDIC, and the OTS (the other federal banking agencies), whose capital guidelines specifically require disallowed deferred tax assets to be

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<sup>1</sup> The amount of deferred tax assets that may be included in a banking organization’s capital may not exceed the lesser of (i) the amount of deferred tax assets that the banking organization is expected to realize within one year, or (ii) 10 percent of tier 1 capital. Amounts in excess of this threshold represent disallowed deferred tax assets and must be deducted from a banking organization’s core capital elements in determining tier 1 capital.

deducted from tier 1 capital in determining these limitations. The Board is proposing to amend its risk-based capital guidelines so that, in addition to goodwill and certain other intangible assets, disallowed deferred tax assets will also be netted out of tier 1 capital for the purpose of determining these two limitations. These changes are being proposed in order to make the Federal Reserve's risk-based capital guidelines consistent with current market practice, and, in keeping with the mandate of section 303(a)(1) of the Riegle Community Development and Regulatory Improvement Act of 1994, to make the Federal Reserve's risk-based capital rules consistent with those of the other federal banking agencies.

#### **Regulatory Flexibility Act Analysis**

Pursuant to section 605(b) of the Regulatory Flexibility Act, the Board has determined that this rule would not have a significant impact on a substantial number of small entities in accord with the spirit and purposes of the Regulatory Flexibility Act (5 U.S.C. 601 et seq.). An analysis of recent Call Report data indicates that less than four percent of banks with assets of \$100 million or less carry disallowed deferred tax assets on their balance sheets. In addition, many of these banks may already be making the proper deduction of these disallowed deferred tax assets from tier 1 capital. Accordingly, a regulatory flexibility analysis is not required.

#### **Paperwork Reduction Act**

The Board has determined that this proposed rule does not involve a collection of information pursuant to the provisions of the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 et seq.).

#### **Solicitation of Comments Regarding the Use of "Plain Language"**

Section 722 of the Gramm-Leach-Bliley Act of 1999 requires the Board to use "plain language" in all proposed and final rules published after January 1, 2000. The Board invites comments about how to make the rule easier to understand, including answers to the following questions:

(1) Is the material organized in an effective manner? If not, how could the material be better organized?

(2) Are the terms of the proposed rule clearly stated? If not, how could the terms be more clearly stated?

(3) Does the proposed rule contain technical language or jargon that is unclear? If not, which language requires clarification?

(4) Would a different format (with respect to the grouping and order of sections and use of headings) make the proposed rule easier to understand? If so, what changes to the format would make the proposed rule easier to understand?

(5) Would increasing the number of sections (and making each section shorter) clarify the proposed rule? If so, which portions of the proposed rule should be changed in this respect?

(6) What additional changes would make the proposed rule easier to understand?

### **List of Subjects**

#### 12 CFR Part 208

Accounting, Agriculture, Banks, banking, 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.

**Authority and Issuance**

For the reasons set forth in the preamble, part 208 and part 225 of chapter II of title 12 of the Code of Federal Regulations are proposed to be amended as set forth below:

**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. In appendix A to part 208, section II.A.2. is amended by revising the first undesignated paragraph following paragraph (v) and section II.A.2.(d) is amended by revising paragraph (i) to read as follows:

**APPENDIX A TO PART 208 -- CAPITAL ADEQUACY GUIDELINES FOR STATE MEMBER BANKS: RISK-BASED MEASURE**

II. \* \* \*

A. \* \* \*

2. \* \* \*

(v) \* \* \*

The maximum amount of Tier 2 capital that may be included in a bank's qualifying total capital is limited to 100 percent of Tier 1 capital (net of goodwill, other intangible assets required to be deducted in accordance with section II.B.1.b. of this appendix, and deferred tax assets required to be deducted in accordance with section II.B.4. of this appendix).

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(d) Subordinated debt and intermediate term preferred stock. (i) The aggregate amount of term subordinated debt (excluding mandatory convertible debt) and intermediate-term preferred stock that may be treated as supplementary capital is limited to 50 percent of Tier 1 capital (net of goodwill, other intangible assets required to be deducted in accordance with section II.B.1.b. of this appendix, and deferred tax assets required to be deducted in accordance with section II.B.4. of this appendix).

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## **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. In appendix A to part 225, section II.A.2. is amended by revising the first undesignated paragraph following paragraph (v) and section II.A.2.(d) is amended by revising paragraph (i) to read as follows:

APPENDIX A TO PART 225 -- CAPITAL ADEQUACY GUIDELINES FOR BANK HOLDING COMPANIES: RISK-BASED MEASURE

II. \* \* \*

A. \* \* \*

2. \* \* \*

(v) \* \* \*

The maximum amount of Tier 2 capital that may be included in an organization's qualifying total capital is limited to 100 percent of Tier 1 capital (net of goodwill, other intangible assets required to be deducted in accordance with section II.B.1.b. of this appendix, and deferred tax assets required to be deducted in accordance with section II.B.4. of this appendix).

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(d) Subordinated debt and intermediate term preferred stock. (i) The aggregate amount of term subordinated debt (excluding mandatory convertible debt) and intermediate-term preferred stock that may be treated as supplementary capital is limited to 50 percent of tier 1 capital (net of goodwill, other intangible assets required to be deducted in accordance with section II.B.1.b. of this appendix, and deferred tax assets required to be deducted in accordance with section II.B.4. of this appendix).

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By order of the Board of Governors of the Federal Reserve System, November 19, 2001.

/signed/

Jennifer J. Johnson,

Secretary of the Board.