Federal Deposit Insurance Corporation
550 17th Street NW, Washington, DC 20429-9990

Financial Institution Letter
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REGULATORY CAPITAL RULES
Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, and Transition Provisions

Summary: The federal bank regulatory agencies (the agencies) have jointly issued the attached Notice of Proposed Rulemaking (proposed rule) that would revise the general risk-based capital rules to incorporate certain revisions by the Basel Committee on Banking Supervision to the Basel capital framework (Basel III). The proposed rule would generally revise the definition of regulatory capital components and related calculations.

Statement of Applicability to Institutions Under $1 Billion in Total Assets: This Financial Institution Letter (FIL) is applicable to all banks. Attached to this FIL is an addendum that also is included in the proposed rule. The addendum offers a summary of the proposed rule designed to clearly and succinctly describe how it would typically apply to smaller, less complex banking organizations. Additional technical assistance explaining the proposed rule also will be made available.

Distribution:
FDIC-Supervised Banks (Commercial and Savings

Suggested Routing:
Chief Executive Officer
Chief Financial Officer
Chief Risk Officer

Related Topics:
Risk-Based Capital Rules
12 CFR Part 325
Basel III

Attachment:
Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, and Transition Provisions (PDF Help)

Contact:
Bobby Bean, Associate Director, Capital Markets Branch, at bbean@fdic.gov or (202) 898-6705
Ryan Billingsley, Senior Policy Analyst, at rbillingsley@fdic.gov or (202) 898-3797
Karl Reitz, Senior Policy Analyst, at kreitz@fdic.gov or (202) 898-6775

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Highlights:
The proposed rule:

- Revises the definition of regulatory capital components and related calculations.
- Adds a new common equity tier 1 capital ratio.
- Increases the minimum tier 1 capital ratio requirement from 4 percent to 6 percent.
- Imposes different limitations to qualifying minority interest in regulatory capital than those currently applied;
- Incorporates the revised regulatory capital requirements into the Prompt Corrective Action (PCA) framework.
- Implements a new capital conservation buffer that would limit payment of capital distributions and certain discretionary bonus payments to executive officers and key risk takers if the banking organization does not hold certain amounts of common equity tier 1 capital in addition to those needed to meet its minimum risk-based capital requirements.
- Provides a transition period for several aspects of the proposed rule, including the phase-out period for certain non-qualifying capital instruments, the new minimum capital ratio requirements, the capital conservation buffer, and the regulatory capital adjustments and deductions.
- For advanced approaches banks, introduces a countercyclical capital buffer and a supplemental leverage ratio.

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Key Aspects of the Proposed Rule on *Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, and Transition Provisions*

The agencies are issuing a notice of proposed rulemaking (NPR, proposal, or proposed rule) to revise the general risk-based capital rules to incorporate certain revisions by the Basel Committee on Banking Supervision to the Basel capital framework (Basel III). The proposed rule would:

- Revise the definition of regulatory capital components and related calculations;
- Add a new regulatory capital component: common equity tier 1 capital;
- Increase the minimum tier 1 capital ratio requirement;
- Impose different limitations to qualifying minority interest in regulatory capital than those currently applied;
- Incorporate the new and revised regulatory capital requirements into the Prompt Corrective Action (PCA) capital categories;
- Implement a new capital conservation buffer framework that would limit payment of capital distributions and certain discretionary bonus payments to executive officers and key risk takers if the banking organization does not hold certain amounts of common equity tier 1 capital in addition to those needed to meet its minimum risk-based capital requirements; and
- Provide for a transition period for several aspects of the proposed rule, including a phase-out period for certain non-qualifying capital instruments, the new minimum capital ratio requirements, the capital conservation buffer, and the regulatory capital adjustments and deductions.

This addendum presents a summary of the proposed rule that is more relevant for smaller, non-complex banking organizations that are ***not*** *subject to the market risk rule or the advanced approaches capital rule. The agencies intend for this addendum to act as a guide for these banking organizations, helping them to navigate the proposed rule and identify the changes most relevant to them. The addendum does not, however, by itself provide a complete understanding of the proposed rules and the agencies expect and encourage all institutions to review the proposed rule in its entirety.*

1. Revisions to the Minimum Capital Requirements

The NPR proposes definitions of common equity tier 1 capital, additional tier 1 capital, and total capital. These proposed definitions would alter the existing definition of capital by imposing, among other requirements, additional constraints on including of minority interests, mortgage servicing assets (MSAs), deferred tax assets (DTAs) and certain investments in unconsolidated financial institutions in regulatory capital. In addition, the NPR would require that most regulatory capital deductions be made from common equity tier 1 capital. The NPR would also require that most of a banking organization's accumulated other comprehensive income (AOCI) be included in regulatory capital.

Under the NPR, a banking organization would maintain the following **minimum** capital requirements:
(1) A ratio of common equity tier 1capital to total risk-weighted assets of 4.5 percent.
(2) A ratio of tier 1 capital to total risk-weighted assets of 6 percent.
(3) A ratio of total capital to total risk-weighted assets of 8 percent.
(4) A ratio of tier 1 capital to adjusted average total assets of 4 percent. [1]

The new minimum capital requirements would be implemented over a transition period, as outlined in the proposed rule. For a summary of the transition period, refer to section 7 of this Addendum. As noted in the NPR, banking organizations are generally expected, as a prudential matter, to operate well above these minimum regulatory ratios, with capital commensurate with the level and nature of the risks they hold.

2. Capital Conservation Buffer

In addition to these minimum capital requirements, the NPR would establish a capital conservation buffer. Specifically, banking organizations would need to hold common equity tier 1 capital in excess of their minimum risk-based capital ratios by at least 2.5 percent of risk-weighted assets in order to avoid limits on capital distributions (including dividend payments, discretionary payments on tier 1 instruments, and share buybacks) and certain discretionary bonus payments to executive officers, including heads of major business lines and similar employees.

Under the NPR, a banking organization's **capital conservation buffer** would be the smallest of the following ratios: a) its common equity tier 1 capital ratio (in percent) minus 4.5 percent; b) its tier 1 capital ratio (in percent) minus 6 percent; and c) its total capital ratio (in percent) minus 8 percent.

To the extent a banking organization's **capital conservation buffer** falls short of 2.5 percent of risk-weighted assets, the banking organization's maximum payout amount for capital distributions and discretionary bonus payments (calculated as the maximum payout ratio multiplied by the sum of eligible retained income, as defined in the NPR) would decline. The following table shows the maximum payout ratio, depending on the banking organization's capital conservation buffer.

Table 1

Capital Conservation Buffer (as a percentage of risk-weighted assets)	Maximum payout ratio (as a percentage or eligible retained income)
Greater than 2.5 percent	No payout limitation applies
Less than or equal to 2.5 percent and greater than 1.875 percent	60 percent
Less than or equal to 1.875 percent and greater than 1.25 percent	40 percent
Less than or equal to 1.25 percent and greater than 0.625 percent	20 percent
Less than or equal to 0.625 percent	0 percent

Eligible retained income for purposes of the proposed rule would mean a banking organization's net income for the four calendar quarters preceding the current calendar quarter, based on the banking organization's most recent quarterly regulatory reports, net of any capital distributions and associated tax effects not already reflected in net income.

Under the NPR, the **maximum payout amount** for the current calendar quarter would be equal to the banking organization's eligible retained income, multiplied by the applicable maximum payout ratio in **Table 1**.

The proposed rule would prohibit a banking organization from making capital distributions or certain discretionary bonus payments during the current calendar quarter if: (A) its eligible retained income is negative; **and** (B) its capital conservation buffer ratio was less than 2.5 percent as of the end of the previous quarter.

The NPR does not diminish the agencies' authority to place additional limitations on capital distributions.

3. Adjustments to Prompt Corrective Action (PCA) Thresholds

The NPR proposes to revise the PCA capital category thresholds to levels that reflect the new capital ratio requirements. The NPR also proposes to introduce the common equity tier 1 capital ratio as a PCA capital category threshold. In addition, the NPR proposes to revise the existing definition of tangible equity. Under the NPR, tangible equity would be defined as tier 1 capital (composed of common equity tier 1 and additional tier 1 capital) plus any outstanding perpetual preferred stock (including related surplus) that is not already included in tier 1 capital.

Table 2. Proposed PCA Threshold Requirements*

PCA Capital Category	Threshold Ratios			
	Total Risk-based Capital ratio	Tier 1 Risk-based Capital ratio	Common Equity Tier 1 Risk-based Capital ratio	Tier 1 Leverage ratio
Well capitalized	10%	8%	6.5%	5%
Adequately capitalized	8%	6%	4.5%	4%
Undercapitalized	< 8%	< 6%	< 4.5%	<4%

Significantly undercapitalized	< 6%	< 4%	< 3%	<3%
Critically undercapitalized	Tangible Equity/Total Assets</= 2%			

*Proposed effective date: January 1, 2015. This date coincides with the phasing in of the new minimum capital requirements, which would be implemented over a transition period.

4. Definition of Capital

The NPR proposes to revise the definition of capital to include the following regulatory capital components: common equity tier 1 capital, additional tier 1 capital, and tier 2 capital. These are summarized below (see summary table attached). Section 20 of the proposed rule describes the capital components and eligibility criteria for regulatory capital instruments. Section 20 also describes the criteria that each primary federal supervisor would consider when determining whether a capital instrument should be included in a specific regulatory capital component.

a. Common Equity Tier 1 Capital

The NPR defines common equity tier 1 capital as the sum of the common equity tier 1 elements, less applicable regulatory adjustments and deductions. Common equity tier 1 capital elements would include:

1. Common stock instruments (that satisfy specified criteria in the proposed rule) and related surplus (net of any treasury stock);

2. Retained earnings;

3. Accumulated other comprehensive income (AOCI); and

4. Common equity minority interest (as defined in the proposed rule) subject to the limitations outlined in section 21 of the proposed rule.

b. Additional Tier 1 Capital

The NPR would define additional tier 1 capital as the sum of additional tier 1 capital elements and related surplus, less applicable regulatory adjustments and deductions. Additional tier 1 capital elements would include:

1. Noncumulative perpetual preferred stock (that satisfy specified criteria in the proposed rule) and related surplus;

2. Tier 1 minority interest (as defined in the proposed rule), subject to limitations described in section 21 of the proposed rule, not included in the banking organization's common equity tier 1 capital; and

3. Instruments that currently qualify as tier 1 capital under the agencies' general risk-based capital rules and that were issued under the Small Business Job's Act of 2010, or, prior to October 4, 2010, under the Emergency Economic Stabilization Act of 2008.

c. Tier 2 Capital

The proposed rule would define tier 2 capital as the sum of tier 2 capital elements and related surplus, less regulatory adjustments and deductions. The tier 2 capital elements would include:

1. Subordinated debt and preferred stock (that satisfy specified criteria in the proposed rule). This will include most of the subordinated debt currently included in tier 2 capital according to the agencies' existing risk-based capital rules;

2. Total capital minority interest (as defined in the proposed rule), subject to the limitations described in section 21 of the proposed rule, and not included in the banking organization's tier 1 capital;

3. Allowance for loan and lease losses (ALLL) not exceeding 1.25 percent of the banking organization's total risk-weighted assets; and

4. Instruments that currently qualify as tier 2 capital under the agencies' general risk-based capital rules and that were issued under the Small Business Job's Act of 2010, or, prior to October 4, 2010, under the Emergency Economic Stabilization Act of 2008.

d. Minority Interest

The NPR proposes a calculation method that limits the amount of minority interest in a subsidiary that is not owned by the banking organization that may be included in regulatory capital.

Under the NPR, **common equity tier 1 minority interest** would mean any minority interest arising from the issuance of common shares by a fully consolidated subsidiary. Common equity tier 1 minority interest may be recognized in common equity tier 1 **only if both** of the following are true:

1. The instrument giving rise to the minority interest would, if issued by the banking organization itself, meet all of the criteria for common stock instruments.

2. The subsidiary is itself a depository institution.

If not recognized in common equity tier 1, the minority interest may be eligible for inclusion in additional tier 1 capital or tier 2 capital.

For a capital instrument that meets all of the criteria for common stock instruments, the amount of common equity minority interest includable in the banking organization's common equity tier 1 capital is equal to:

The common equity tier 1 minority interest of the subsidiary

Minus

(**The percentage of the subsidiary's common equity tier 1 capital that is not owned by the banking organization**)

multiplied by the difference between

(**common equity tier 1 capital of the subsidiary**

and the lower of

- **7% of the risk weighted assets of the banking organization that relate to the subsidiary** *or*,

- **7% of the risk weighted assets of the subsidiary)**

For **tier 1 minority interest**, the NPR proposes the same calculation method, but substitutes tier 1 capital in place of common equity tier 1 capital and 8.5 percent in place of 7 percent in the illustration above (and assuming the banking organization has a common equity tier 1 capital ratio of at least 7 percent). In the case of tier 1 minority interest, there is no requirement that the subsidiary be a depository institution. However, the NPR would require that any instrument giving rise to the minority interest must meet all of the criteria for either a common stock instrument or an additional tier 1 capital instrument.

For **total capital minority interest**, the NPR proposes an equivalent calculation method (by substituting total capital in place of common equity tier 1 capital and 10.5 percent in place of 7 percent in the illustration above; and assuming the banking organization has a common equity tier 1 capital ratio of at least 7 percent). In the case of total capital minority interest, there is no requirement that the subsidiary be a depository institution. However, the NPR would require that any instrument giving rise to the minority interest must meet all of the criteria for either a common stock instrument, an additional tier 1 capital instrument, or a tier 2 capital instrument.

e. Regulatory capital adjustments and deductions

A. Regulatory deductions from common equity tier 1 capital.

The NPR would require that a banking organization deduct the following from the sum of its common equity tier 1 capital elements:

- Goodwill and all other intangible assets (other than MSAs), net of any associated deferred tax liabilities (DTLs). Goodwill for purposes of this deduction includes any goodwill embedded in the valuation of a significant investment in the capital of an unconsolidated financial institution in the form of common stock.
- DTAs that arise from operating loss and tax credit carryforwards net of any valuation allowance and net of DTLs (see section 22 of the proposed rule for the requirements on the netting of DTLs).
- Any gain-on-sale associated with a securitization exposure.
- Any defined benefit pension fund net asset [2], net of any associated deferred tax liability. [3] *(The pension deduction does **not** apply to insured depository institutions that have their own defined benefit pension plan.)*

B. Regulatory adjustments to common equity tier 1 capital.

The NPR would require that for the following items, a banking organization deduct any associated unrealized gain and add any associated unrealized loss to the sum of common equity tier 1 capital elements:

- Unrealized gains and losses on cash flow hedges included in AOCI that relate to the hedging of items that are not recognized at fair value on the balance sheet.
- Unrealized gains and losses that have resulted from changes in the fair value of liabilities that are due to changes in the banking organization's own credit risk.

C. Additional deductions from regulatory capital

Under the NPR, a banking organization would be required to make the following deductions with respect to investments in its own capital instruments:

- Deduct from common equity tier 1 elements investments in the banking organization's own common stock instruments (including any contractual obligation to purchase), whether held directly or indirectly.
- Deduct from additional tier 1 capital elements, investments in (including any contractual obligation to purchase) the banking organization's own additional tier 1 capital instruments, whether held directly or indirectly.
- Deduct from tier 2 capital elements, investments in (including any contractual obligation to purchase) the banking organization's own tier 2 capital instruments, whether held directly or indirectly.

D. Corresponding deduction approach.

Under the NPR, a banking organization would use the corresponding deduction approach to calculate the required deductions from regulatory capital for:

- Reciprocal cross-holdings;
- Non-significant investments in the capital of unconsolidated financial institutions; and,
- Non-common stock significant investments in the capital of unconsolidated financial institutions.

Under the corresponding deduction approach, a banking organization would be required to make any such deductions from the same component of capital for which the underlying instrument would qualify if it were issued by the banking organization itself. In addition, if the banking organization does not have a sufficient amount of such component of capital to effect the deduction, the shortfall will be deducted from the next higher (that is, more subordinated) component of regulatory capital (for example, if the exposure may be deducted from additional tier 1 capital but the banking organization does not have sufficient additional tier 1 capital, it would take the deduction from common equity tier 1 capital). The NPR provides additional information regarding the corresponding deduction approach for those banking organizations with such holdings and investments.

Reciprocal crossholdings in the capital of financial institutions: The NPR would require a banking organization to deduct investments in the capital of other financial institutions it holds reciprocally [4].

Non-significant investments in the capital of unconsolidated financial institutions: [5] The proposed rule would require a banking organization to deduct any non-significant investments in the capital of unconsolidated financial institutions that, in the aggregate, exceed 10 percent of the sum of the banking organization's common equity tier 1 capital elements less all deductions and other regulatory adjustments required under sections 22(a) through 22(c)(3) of the proposed rule (the 10 percent threshold for non-significant investments in unconsolidated financial institutions).

- The amount to be deducted from a specific capital component is equal to (i) the amount of a banking organization's non-significant investments exceeding the 10 percent threshold for non-significant investments *multiplied* by (ii) the ratio of the non-significant investments in unconsolidated financial institutions in the form of such capital component to the amount of the banking organization's total non-significant investments in unconsolidated financial institutions.

- The banking organization's non-significant investments in the capital of unconsolidated financial institutions not exceeding the 10 percent threshold for non-significant investments must be assigned the appropriate risk weight under the Standardized Approach NPR.

Significant investments in the capital of unconsolidated financial institutions that are not in the form of common stock: A banking organization must deduct its significant investments in the capital of unconsolidated financial institutions not in the form of common stock.

E. Threshold Deductions:

The NPR would require a banking organization to deduct from common equity tier 1 capital elements each of the following assets (together, the threshold deduction items) that, individually, are above 10 percent of the sum of the banking organization's common equity tier 1 capital elements, less all required adjustments and deductions required under sections 22(a) through 22(c) of the proposed rule (the 10 percent common equity deduction threshold):

- DTAs arising from temporary differences that the banking organization could not realize through net operating loss carrybacks, net of any associated valuation allowance, and DTLs, subject to the following limitations:

    - Only the DTAs and DTLs that relate to taxes levied by the same taxation authority and that are eligible for offsetting by that authority may be offset for purposes of this deduction.

    - The DTLs offset against DTAs must exclude amounts that have already been netted against other items that are either fully deducted (such as goodwill) or subject to deduction (such as MSA).

- MSAs, net of associated DTLs.

- Significant investments in the capital of unconsolidated financial institutions in the form of common stock.

In addition, the aggregate amount of the threshold deduction items in this section cannot exceed 15 percent of the banking organization's common equity tier 1 capital net of all deductions (the 15 percent common equity deduction threshold). That is, the banking organization must deduct from common equity tier 1 capital elements, the amount of the threshold deduction items that are not deducted after the application of the 10 percent common equity deduction threshold, and that, in aggregate, exceed 17.65 percent of the sum of the banking organization's common equity tier 1 capital elements, less all required adjustments and deductions required under sections 22(a) through 22(c) of the proposed rule and less the threshold deduction items in full.

5. Changes in Risk-weighted Assets:

The amounts of the threshold deduction items within the limits and not deducted, as described above, would be included in the risk-weighted assets of the banking organization and assigned a risk weight of 250 percent. In addition, certain exposures that are currently deducted under the general risk-based capital rules, for example certain credit enhancing interest-only strips, would receive a 1,250% risk weight.

6. Timeline and Transition Period

The NPR would provide for a multi-year implementation as summarized in the table below:

Table 3 - Phase-in Schedule							
Year (as of Jan. 1)	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**
Minimum common equity tier 1 ratio	3.5%	4.0%	4.5%	4.5%	4.5%	4.5%	4.5%
Common equity tier 1 capital conservation buffer				0.625%	1.25%	1.875%	2.50%
Common equity tier 1 plus capital conservation buffer	3.5%	4.0%	4.5%	5.125%	5.75%	6.375%	7.0%
Phase-in of deductions from common equity tier 1 (including threshold deduction items that are over the limits)		20%	40%	60%	80%	100%	100%
Minimum tier 1 capital	4.5%	5.5%	6.0%	6.0%	6.0%	6.0%	6.0%
Minimum tier 1 capital plus capital conservation buffer				6.625%	7.25%	7.875%	8.5%
Minimum total capital	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%
Minimum total capital plus conservation buffer	8.0%	8.0%	8.0%	8.625%	9.25%	9.875%	10.5%

As provided in Basel III, capital instruments that no longer qualify as additional tier 1 or tier 2 capital will be phased out over a 10 year horizon beginning in 2013. However, trust preferred securities are phased out as required under the Dodd-Frank Act.

Attached to this Addendum is a summary of the proposed revision to the components of capital introduced by the NPR.

Attachment: Summary of Capital Components in this NPR

Components and Tiers	**Explanation**
(1) COMMON EQUITY TIER 1 CAPITAL	
(a) + Qualifying common stock instruments	Instruments must meet all of the common equity tier 1 criteria (Note 1)
(b) + Retained earnings	
(c) + AOCI	With the exception in Note 2 below, AOCI flows through to common equity tier 1 capital.
(d) + Qualifying common equity tier 1 minority interest	Subject to specific calculation method and limitation.
(e) - Regulatory deductions from common equity tier 1 capital	Deduct: Goodwill and intangible assets (other than MSAs); DTAs that arise from operating loss and tax credit carryforwards; any gain on sale from a securitization; investments in the banking organization's own common stock instruments.
	See explanation below (Note 2).

(f) +/- Regulatory adjustments to common equity tier 1 capital	
(g) - common equity tier 1 capital deductions per the corresponding deduction approach	See section 4.e.D above.
(h) - Threshold deductions	Deduct amount of threshold items that are above the 10 and 15 percent common equity tier 1 thresholds. (See section 4.e. above).
= common equity tier 1 capital	
(2) ADDITIONAL TIER 1 CAPITAL	
(a) + additional tier 1 capital instruments	Instruments must meet all of the additional tier 1 criteria (Note 1).
(b) + Tier 1 minority interest that is not included in common equity tier 1 capital	Subject to specific calculation and limitation
(c) + Non-qualifying tier 1 capital instruments subject to transition phase-out and SBLF related instruments	(Note 3)
(d) - Investments in a banking organization's own additional tier 1 capital instruments	
(e) - Additional tier 1 capital deductions per the corresponding deduction approach	See section 4.e.D above.
= Additional tier 1 capital	
(3) TIER 2 CAPITAL	
(a) + Tier 2 capital instruments	Instruments must meet all of the tier 2 criteria (Note 1)
(b) + Total capital minority interest that is not included in tier 1	Subject to specific calculation and limitation.
(c) + ALLL	Up to 1.25% of risk weighted assets
(d) - Investments in a banking organization's own tier 2 capital instruments	
(e) - Tier 2 capital deductions per the Corresponding Deduction Approach	See section 4.e.D above.
(f) + Non-qualifying tier 2 capital instruments subject to transition phase-out and SBLF related instruments	(Note 3)
= Tier 2 capital	
TOTAL CAPITAL = common equity tier 1 + additional tier 1 + tier 2	

Notes to Table:

Note 1: Includes surplus related to the instruments.

Note 2: **Regulatory adjustments**: A banking organization must deduct any unrealized gain and add any unrealized loss for cash flow hedges included in AOCI relating to hedging of items not fair valued on the balance sheet and for unrealized gains and losses that have resulted from changes in the fair value of liabilities that are due to changes in the banking organization's own credit risk.

Note 3: **Grandfathered SBLF related instruments**: These are instruments issued under the Small Business Lending Facility (SBLF); or prior Oct. 4, 2010 under the Emergency Economic Stabilization Act of 2008. If the instrument qualified as tier 1 capital under rules at the time of issuance, it would count as additional tier 1 under this proposal. If the instrument qualified as tier 2 under the rules at that time, it would count as tier 2 under this proposal.

Attachment: Comparison of Current Rules vs. Proposal

Minimum regulatory capital requirements			
	Current minimum ratios	**Proposed minimum ratios**	**Comments**
Common equity tier 1 capital / risk weighted assets	N/A	4.5%	
Tier 1 capital / risk weighted assets	4%	6%	
Total capital / risk weighted assets	8%	8%	
Leverage ratio	≥ 4% (or ≥ 3%)	≥ 4%	Minimum required level will not vary depending on the supervisory rating
Capital buffers			
	Current treatment	**Proposed treatment**	**Comment**
Capital conservation buffer	N/A	Capital conservation buffer equivalent to 2.5% of risk-weighted assets; composed of common equity tier 1 capital	Not holding the capital conservation buffer may result in restrictions on capital distributions and certain discretionary bonus payments
Prompt Corrective Action			
	Current PCA levels	**Proposed PCA levels**	**Comment**
Common equity tier 1 capital	N/A	Well capitalized: ≥ 6.5%; Adequately capitalized: ≥ 4.5%; Undercapitalized: < 4.5%; Significantly undercapitalized: < 3%	Proposed adequately capitalized PCA level aligned to new minimum ratio
Tier 1 capital	Well capitalized: ≥ 6%; Adequately capitalized: ≥ 4%; Undercapitalized < 4%; Significantly undercapitalized: < 3%	Well capitalized: ≥ 8%; Adequately capitalized: ≥ 6%; Undercapitalized < 6%; Significantly undercapitalized: < 4%	Proposed adequately capitalized PCA level aligned to new minimum ratio
Total capital	Well capitalized: ≥ 10%; Adequately capitalized: ≥ 8%; Undercapitalized < 8%; Significantly undercapitalized: < 6%	Well capitalized: ≥ 10%; Adequately capitalized: ≥ 8%; Undercapitalized < 8%; Significantly undercapitalized: < 6%	

Leverage ratio	Well capitalized: ≥ 5%; Adequately capitalized: ≥ 4% (or ≥ 3%); Undercapitalized < 4% (or < 3%); Significantly undercapitalized: < 3%	Well capitalized: ≥ 5%; Adequately capitalized: ≥ 4%; Undercapitalized < 4%; Significantly undercapitalized: < 3%	PCA adequately capitalized level will not vary depending on the supervisory rating
Critically undercapitalized category	*Tangible equity to total assets ratio ≤ 2*	*Tangible equity to total assets ≤ 2*	*Tangible equity under the proposal would be defined as tier 1 capital plus non-tier 1 perpetual preferred stock*

Regulatory Capital Components			
	Current definition / instruments	**Proposed definition / instruments**	**Comments**
Common equity tier 1 capital	No specific definition	Mostly retained earnings and common stock that meets specified eligibility criteria (plus limited amounts of minority interest in the form of common stock) less the majority of the regulatory deductions	Common stock instruments traditionally issued by U.S. banking organizations expected generally to qualify as common equity tier 1 capital
Additional tier 1 capital	No specific definition	Equity capital instruments that meet specified eligibility criteria (plus limited amounts of minority interest in the form of tier 1 capital instruments)	Non-cumulative perpetual preferred stock traditionally issued by U.S. banking organizations expected to generally qualify; trust preferred instruments traditionally issued by certain bank holding companies would not qualify
Tier 2 capital	Certain capital instruments (e.g., subordinated debt) and limited amounts of ALLL	Capital instruments that meet specified eligibility criteria (e.g., subordinated debt) and limited amounts of ALLL	Traditional subordinated debt instruments are expected to remain tier 2 eligible; there is no specific limitation on the amount of tier 2 capital that can be included in total capital under the proposal
Regulatory deductions and adjustments			
	Current treatment	**Proposed treatment**	**Comment**
Regulatory deductions	Current deductions from regulatory capital include goodwill and other intangibles, DTAs (above certain levels), and MSAs (above certain levels)	Proposed deductions from common equity tier 1 capital include goodwill and other intangibles, DTAs (above certain levels), MSAs (above certain levels) and investments in unconsolidated financial institutions (above certain levels)	Vast majority of regulatory deductions are made at the common equity tier 1 capital level (as opposed to the tier 1 level); the proposed deductions for MSAs and DTAs in the proposed rule are significantly more stringent than the current deductions
Regulatory adjustments	Current adjustments include the neutralization of unrealized gains and losses on available for sale debt securities for regulatory capital purposes	Under the proposal, AOCI would generally flow through to regulatory capital	Under the proposed treatment unrealized gains and losses on available for sale debt securities would not be neutralized for regulatory capital purposes
MSAs, certain DTAs arising from temporary differences, and certain	MSAs and DTAs that are not deducted are subject to a 100 percent risk weight	Items that are not deducted are subject to a 250 percent risk weight	Under the proposal, these items are subject to deduction if they exceed

significant investments in the common stock of unconsolidated financial institutions			certain specified common equity deduction thresholds
The portion of a CEIO that does not constitute an after-tax-gain-on-sale	Dollar-for-dollar capital requirement for amounts not deducted based on a concentration limit	Subject to a 1250 percent risk weight	

[1] Banking organizations should be aware that their leverage ratio requirements would be affected by the new definition of tier 1 capital under this proposal. See section 4 of this addendum on the definition of capital.

[2] With prior approval of the primary federal supervisor, the banking organization may reduce the amount to be deducted by the amount of assets of the defined benefit pension fund to which it has unrestricted and unfettered access, provided that the banking organization includes such assets in its risk-weighted assets as if the banking organization held them directly. For this purpose, unrestricted and unfettered access means that the excess assets of the defined pension fund would be available to protect depositors or creditors of the banking organization in a receivership, insolvency, liquidation, or similar proceeding.

[3] The deferred tax liabilities for this deduction exclude those deferred tax liabilities that have already been netted against DTAs.

[4] An instrument is held reciprocally if the instrument is held pursuant to a formal or informal arrangement to swap, exchange, or otherwise intend to hold each other's capital instruments.

[5] With prior written approval of the primary federal supervisor, for the period of time stipulated by the primary federal supervisor, a banking organization would not be required to deduct exposures to the capital instruments of unconsolidated financial institutions if the investment is made in connection with the banking organization providing financial support to a financial institution in distress.