



## FEDERAL RESERVE BANK OF DALLAS

2200 N. PEARL ST.  
DALLAS, TX 75201-2272

February 28, 2006

**Notice 06-14**

**TO:** The Chief Executive Officer of each  
financial institution and others concerned  
in the Eleventh Federal Reserve District

### **SUBJECT**

#### **Approval of Final Rule Expanding the Definition of a Small Bank Holding Company**

### **DETAILS**

The Board of Governors of the Federal Reserve System has amended the asset size threshold and other criteria for determining whether a bank holding company (BHC) qualifies for the Board's Small Bank Holding Company Policy Statement (Regulation Y, Appendix C) (policy statement) and an exemption from the Board's consolidated risk-based and leverage capital adequacy guidelines for BHCs (Regulation Y, Appendices A and D) (capital guidelines). The Board is adopting this final rule to address the effects of inflation, industry consolidation, and normal asset growth of BHCs since the Board introduced the policy statement in 1980.

The final rule increases the asset size threshold from \$150 million to \$500 million in consolidated assets for determining whether a BHC may qualify for the policy statement and an exemption from the capital guidelines; modifies the qualitative criteria used in determining whether a BHC that is under the asset size threshold nevertheless would not qualify for the policy statement or the exemption from the capital guidelines; and clarifies the treatment under the policy statement of subordinated debt associated with trust preferred securities. The final rule becomes effective March 30, 2006.

### **ATTACHMENT**

A copy of the Board's notice as it appears on pages 9897–903, Vol. 71, No. 39 of the *Federal Register* dated February 28, 2006, is attached.

### **MORE INFORMATION**

For more information, please contact Dorsey Davis, Banking Supervision Department, (214) 922-6051. Previous Federal Reserve Bank notices are available on our web site at [www.dallasfed.org/banking/notices/index.html](http://www.dallasfed.org/banking/notices/index.html) or by contacting the Public Affairs Department at (214) 922-5254.

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# Rules and Regulations

Federal Register

Vol. 71, No. 39

Tuesday, February 28, 2006

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## FEDERAL RESERVE SYSTEM

### 12 CFR Part 225

[Regulation Y; Docket No. 1235]

#### **Capital Adequacy Guidelines for Bank Holding Companies; Small Bank Holding Company Policy Statement; Definition of a Qualifying Small Bank Holding Company**

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

**ACTION:** Final rule.

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**SUMMARY:** The Board of Governors of the Federal Reserve System (Board) is amending the asset size threshold and other criteria for determining whether a bank holding company (BHC) qualifies for the Board's Small Bank Holding Company Policy Statement (Regulation Y, Appendix C) (Policy Statement) and an exemption from the Board's consolidated risk-based and leverage capital adequacy guidelines for BHCs (Regulation Y, Appendices A and D) (Capital Guidelines). The Board is adopting this final rule to address the effects of inflation, industry consolidation, and normal asset growth of BHCs since the Board introduced the Policy Statement in 1980. The final rule increases the asset size threshold from \$150 million to \$500 million in consolidated assets for determining whether a BHC may qualify for the Policy Statement and an exemption from the Capital Guidelines; modifies the qualitative criteria used in determining whether a BHC that is under the asset size threshold

nevertheless would not qualify for the Policy Statement or the exemption from the Capital Guidelines; and clarifies the treatment under the Policy Statement of subordinated debt associated with trust preferred securities.

**DATES:** This final rule is effective March 30, 2006.

**FOR FURTHER INFORMATION CONTACT:**

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**SUPPLEMENTARY INFORMATION:**

**I. Background**

The Board issued the Policy Statement in 1980 to facilitate the transfer of ownership of small community-based banks in a manner that is consistent with bank safety and soundness. The Board generally has discouraged the use of debt by BHCs to finance the acquisition of banks or other companies because high levels of debt at a BHC can impair the ability of the BHC to serve as a source of strength to its subsidiary banks. The Board has recognized, however, that the transfer of ownership of small banks often requires the use of acquisition debt. Accordingly, the Board adopted the Policy Statement to permit the formation and expansion of small BHCs with debt levels that are higher than what would be permitted for larger BHCs. The Policy Statement contains several conditions and restrictions that are designed to ensure that small BHCs that operate with the higher levels of debt permitted by the Policy Statement do not present an undue risk to the safety and soundness of their subsidiary banks.

Currently, the Policy Statement applies to BHCs with pro forma consolidated assets of less than \$150 million that (i) are not engaged in any nonbanking activities involving significant leverage; (ii) are not engaged in any significant off-balance sheet activities; and (iii) do not have a

significant amount of outstanding debt that is held by the general public ("qualifying small BHCs"). Under the Policy Statement, qualifying small BHCs may use debt to finance up to 75 percent of the purchase price of an acquisition (that is, they may have a debt-to-equity ratio of up to 3:1), but are subject to a number of ongoing requirements. The principal ongoing requirements are that a qualifying small BHC (i) reduce its parent company debt in such a manner that all debt is retired within 25 years of being incurred; (ii) reduce its debt-to-equity ratio to .30:1 or less within 12 years of the debt being incurred; (iii) ensure that each of its subsidiary insured depository institutions is well capitalized; and (iv) refrain from paying dividends until such time as it reduces its debt-to-equity ratio to 1.0:1 or less. The Policy Statement also specifically provides that a qualifying small BHC may not use the expedited applications procedures or obtain a waiver of the stock redemption filing requirements applicable to BHCs under the Board's Regulation Y (12 CFR 225.4(b), 225.14, and 225.23) unless the BHC has a pro forma debt-to-equity ratio of 1.0:1 or less.

The Board adopted the risk-based capital guidelines in 1989 to assist in the assessment of the capital adequacy of BHCs. The risk-based capital guidelines establish for BHCs minimum ratios of tier 1 capital and total capital to risk-weighted assets. One of the Board's principal objectives in adopting the risk-based capital guidelines was to make regulatory capital requirements more sensitive to differences in risk profiles among banking organizations. Supplemental to the risk-based capital guidelines, the Board in 1991 adopted the tier 1 leverage measure, a minimum ratio of tier 1 capital to total average assets, to further assist in the assessment of the capital adequacy of BHCs with the principal objective of placing a constraint on the maximum degree to which a banking organization can leverage its equity capital base. Because qualifying small BHCs may, consistent with the Policy Statement, operate at a level of leverage that generally is inconsistent with the Capital Guidelines, the Capital Guidelines provide an exemption for qualifying small BHCs.

On September 8, 2005, the Board requested comment on a proposed rule that would raise, to \$500 million, the asset size threshold for determining whether a small BHC would be subject to the Policy Statement and exempt from the Capital Guidelines (70 FR 53320, September 8, 2005). The Board also proposed several modifications to

the criteria under which a BHC that is under the asset size threshold would be ineligible for application of the Policy Statement and would be subject to the Capital Guidelines. The proposed rule also clarified that subordinated debt associated with issuances of trust preferred securities generally would be considered debt for most purposes under the Policy Statement, but provided a transition period for certain currently outstanding subordinated debt associated with these securities.

**II. Summary of Comments and Final Rule**

The Board received twenty-nine comments on the proposed rule. Commenters included financial institutions, industry associations, and individuals. All commenters generally supported the proposed increase in the asset threshold for determining whether a BHC would qualify for the Policy Statement and an exemption from the Capital Guidelines; however, some commenters urged the Board to increase the asset threshold to \$1 billion. Some commenters also recommended that the Board create an indexing mechanism under which the threshold would be raised automatically over time to reflect some measure of the rate of inflation. Some commenters also raised questions about or recommended changes to the proposed qualification criteria under which small BHCs would fail to qualify for the application of the Policy Statement and would be subject to the Capital Guidelines. Finally, a number of commenters recommended changes to the proposed criteria for exempting subordinated debt associated with trust preferred securities during the transition period and extending the transition period. The comments received on the proposed rule are discussed in greater detail below.

*New Asset Threshold of \$500 Million*

As noted above, commenters generally supported the Board's proposal to raise the asset threshold under the Policy Statement from \$150 million to \$500 million. Six commenters, however, expressed the view that the proposed increase in the asset threshold from \$150 million to \$500 million would be inadequate and asserted that the threshold should be increased to \$1 billion. In support of their view, these commenters generally argued that, until a BHC reaches the \$1 billion asset level, it does not have the necessary access to the equity markets that would enable it to finance an acquisition with a lower proportion of debt-to-equity.

After carefully considering the comments received in light of the Board's supervisory experience and the purposes of the Policy Statement and Capital Guidelines, the Board has determined to raise the asset threshold to \$500 million in consolidated assets as proposed. The Board is concerned that a further expansion at this time of the definition of qualifying small BHCs beyond \$500 million could adversely impact bank safety and soundness and impair the Board's ability to monitor the financial condition of BHCs. The existence of the Policy Statement and the exemption from the Capital Guidelines for qualifying small BHCs are major departures from the Board's general policy of limiting BHC leverage and reflect a careful balance of the special difficulties small banks may face in the transfer of ownership with the prudential and supervisory concerns of the Board. Consolidated capital standards are a key aspect of the Board's supervisory program and play an important role in helping ensure that a BHC—whether large or small—is able to serve as a source of strength for its subsidiary depository institutions. For this reason, the Board believes that exemptions from these standards (and related reporting obligations) should be narrowly tailored and granted only when clearly warranted. This is particularly true for small BHCs because the Board's risk-focused supervision program for smaller BHCs (whether or not qualifying small BHCs for the purposes of the Policy Statement) relies heavily on off-site monitoring rather than on-site examiner reviews.

Moreover, raising the asset threshold to \$500 million as set forth in this final rule will allow approximately 85 percent of all BHCs to qualify for the Policy Statement, a substantial increase from the 55 percent that were eligible to qualify under the \$150 million threshold.

Finally, since the Policy Statement was originally adopted, the legal framework governing the ownership and branching of banking organizations has changed dramatically, increasing market liquidity. The Board's supervisory experience indicates that many banks with assets in excess of \$500 million are attractive for acquisition by organizations that have the means to make acquisitions without the use of excessive debt.

The Board expects to review at least once every five years the asset threshold in the final rule to determine whether this threshold should be further adjusted. In considering whether to modify the asset threshold, the Board will consider several factors which may

include, among other things, the rate of growth of aggregate bank assets, the overall financial condition of the banking industry, and structural changes in the role of banking organizations in the overall economy. The Board believes that this periodic review will allow the Board to consider the full range of factors that may be relevant to identifying the level below which a BHC should be subject to the Policy Statement and exempt from the Capital Guidelines. In this regard, the Board believes that measures of price inflation are not necessarily appropriate determinants of what constitutes a small BHC for capital and prudential purposes.

#### *Other Criteria for Identifying a Qualifying Small BHC*

The Board also proposed to modify the qualitative criteria for determining whether a BHC that otherwise meets the asset threshold nevertheless should not qualify for application of the Policy Statement and exemption from the Capital Guidelines to reflect changes to the banking industry over the last two decades, including the nature of the operations of many smaller BHCs. As proposed, BHCs with less than \$500 million in consolidated assets would not qualify for the Policy Statement and would be subject to the Capital Guidelines if the BHC (i) is engaged in significant nonbanking activities either directly or through a nonbank subsidiary, (ii) conducts significant off-balance sheet activities, including securitizations or managing or administering assets for third parties, either directly or through a nonbank subsidiary, or (iii) has a material amount of debt or equity securities (other than trust preferred securities) outstanding that are registered with the Securities and Exchange Commission (SEC).

A few commenters indicated that more clarity would be helpful in quantifying "significant" nonbanking activities, "significant" off-balance sheet activities, or "material" amounts of debt and equity securities. For example, one commenter suggested the use of more absolute quantitative thresholds or limits, such as total nonbank assets, off-balance sheet items, or debt or equity securities as a percentage of Tier 1 capital. Commenters also suggested that the term "nonbanking activities" be more specifically defined and exclude nonbanking activities that have been found to be "closely related to banking" under the Board's Regulation Y (See 12 CFR 225.28).

Some commenters also requested that the Federal Reserve allow a small BHC to operate under the Policy Statement if

the BHC conducts significant nonbanking activities but the activities are found, based on supervisory review, to not pose material additional operational risks.<sup>1</sup> Two commenters noted that SEC registration can be triggered by increases in an institution's shareholder base through inheritance or other inter-generational transfers and, on this basis, argued that the criterion related to SEC-registered debt or equity should be deleted.

After carefully considering the issues raised by commenters, the Board has adopted the changes, as proposed. The Board believes that the changes best reflect the Board's prudential and supervisory interests in ensuring that BHCs remain well capitalized, subject to appropriate financial reporting requirements to facilitate the supervisory process, and able to serve as a source of strength to their subsidiary banks. The Board also believes these changes are necessary or appropriate to reflect changes in the banking industry over the last two decades, including the nature of the operations of many small BHCs. The enactment of the Gramm-Leach-Bliley Act in 1999 expanded significantly the range of nonbanking activities in which BHCs may engage, both directly and through nonbank subsidiaries of the holding company. Such activities may result in a higher level of operational, legal or reputational risk to the banking organization than balance sheet measures would indicate and, in some cases, may contribute significantly to an organization's overall financial performance.<sup>2</sup>

The revision of the criterion to exclude from the Policy Statement any BHC that has outstanding a material amount of SEC-registered debt or equity securities reflects the fact that SEC registrants typically exhibit a degree of complexity of operations and access to multiple funding sources that warrants excluding them from the Policy Statement and subjecting them to the Capital Guidelines. Moreover, the application of consolidated reporting requirements to these BHCs should not

<sup>1</sup> Two commenters urged that any final rule clearly provide that a small BHC is not prohibited from operating under the Policy Statement if it conducts trust activities through trust departments of its subsidiary bank or through a nonbank subsidiary of that bank. The term "nonbank subsidiary" as used in the Policy Statement refers to a subsidiary of a BHC other than a bank or a subsidiary of a bank.

<sup>2</sup> The examples provided in the proposed rule—securitizations and managing or administering assets for third parties—simply highlight two off-balance sheet activities that may involve substantial risk. These examples are not intended to be exclusive and other activities may well present similar concerns.

impose significant additional burden, as they are required to have consolidated financial statements for SEC reporting purposes. What constitutes a "significant" amount of nonbanking activities or a "material" amount of SEC-registered debt or equity for a particular BHC depends on the size, activities and condition of the relevant BHC. In the Board's view, differing levels of risk in varying business lines and practices among institutions precludes the use of fixed measurable parameters of significance or materiality across all institutions. For this reason, the rule provides the Federal Reserve with supervisory flexibility in determining, on a case-by-case basis, the significance or materiality of activities or securities outstanding such that the BHC should be excluded from the Policy Statement and subject to the Capital Guidelines. The Board notes that the current Policy Statement also uses a "significant" standard and that application of this standard through the supervisory process has not created substantial difficulty over the years. As a general matter, the Board believes that relatively few small BHCs are likely to be excluded from the Policy Statement and become subject to the Capital Guidelines due to qualitative criteria included in the final rule.

The Board has amended the Policy Statement and the Capital Guidelines to make explicit the Federal Reserve's existing authority to require on a case-by-case basis that a qualifying small BHC meet consolidated capital requirements when such action is warranted for supervisory reasons, as well as the ability of a qualifying small BHC to voluntarily elect to comply with the Capital Guidelines.

#### *Treatment of Subordinated Debt Associated With Trust Preferred Securities*

Currently, for purposes of the Policy Statement, subordinated debt on the parent company's balance sheet that is issued in connection with trust preferred securities is not treated as debt; however, the cash-flow impact of such subordinated debt is included in the Board's review of the financial condition of a BHC.<sup>3</sup> The proposed rule provided that subordinated debt associated with trust preferred securities would be considered debt for most purposes under the Policy Statement. In

<sup>3</sup> Trust preferred securities are undated cumulative preferred securities issued out of a special purpose entity, usually in the form of a trust, in which a BHC owns all of the common securities. The special purpose entity's sole asset is a deeply subordinated note issued by the BHC that typically has a fixed maturity of 30 years.

particular, such subordinated debt would be included as debt in determining whether (i) a qualifying small BHC's acquisition debt is 75 percent or less of the purchase price; or (ii) a qualifying small BHC's debt-to-equity ratio is greater than 1.0:1 (the ratio above which a qualifying small BHC is subject to dividend restrictions and is not permitted to use the expedited applications processing procedures or obtain a waiver of stock redemption filing requirements under Regulation Y).<sup>4</sup> However, subordinated debt associated with trust preferred securities would not be included as debt in determining compliance with the 12-year debt reduction and 25-year debt retirement requirements of the Policy Statement.

In order to provide for more equitable treatment between qualifying small BHCs and larger BHCs that are subject to the Capital Guidelines,<sup>5</sup> the proposed rule provided that, for purposes of determining compliance with Policy Statement requirements, a qualifying small BHC could exclude from debt an amount of subordinated debt associated with trust preferred securities equaling up to 25 percent of the small BHC's stockholders' equity (as defined in the Policy Statement) less parent company goodwill.<sup>6</sup> In addition, in order to give qualifying small BHCs sufficient time to conform their debt structures, the Board proposed to provide for a five-year transition period during which all subordinated debt associated with trust preferred securities issued on or prior to the publication date of the proposed rule (September 8, 2005) would not be considered debt under the Policy Statement. However, the proposed rule also provided that this temporary non-debt status would terminate if the qualifying small BHC issued additional subordinated debt associated with a new issuance of trust preferred securities after the date of the proposed rule.

<sup>4</sup> The Board also would consider subordinated debt associated with the issuance of trust preferred securities as covered by any supervisory debt commitments with the Federal Reserve.

<sup>5</sup> A BHC that is subject to the Capital Guidelines generally may count an amount of qualifying trust preferred securities as tier 1 capital up to 25 percent of the sum of the BHC's core capital elements. 12 CFR part 225, appendix A, § II.A.1.b.

<sup>6</sup> For example, assume the parent company only financial statements of a qualifying small BHC include subordinated debt associated with trust preferred securities of \$200, other debt of \$75, stockholders' equity of \$300, and goodwill of \$100. The numerator of the debt to equity ratio of the company for purposes of the Policy Statement would equal \$225 or  $(\$75 + (\$200 - ((\$300 - \$100) \times .25)))$ . The denominator of the debt to equity ratio would be \$300.

Overall, commenters did not object to the proposed treatment of subordinated debt under the Policy Statement. However, several commenters recommended changes to the transition period and related conditions for existing subordinated debt associated with trust preferred securities. For example, one commenter recommended that existing subordinated debt of this type should be permanently grandfathered, while another recommended extending the transition period to ten years so that small BHCs would have more time to conform their debt structures. Several others recommended that the transition period be amended to include debt outstanding on the date of issuance of the *final* rule (or even up to 90 days after its issuance) so that companies would have time to restructure or complete issuances pending on the date of the proposed rule without being penalized under the rule change. Commenters also recommended that small BHCs be allowed to refinance existing trust preferred securities during the transition period to lower their interest costs without losing the exempted status of any associated subordinated debt.

Several hundred BHCs with assets under \$500 million have issued trust preferred securities to date. The Board believes that permanently grandfathering existing subordinated debt associated with trust preferred securities would provide these small BHCs with an unfair competitive advantage and would not be prudent for supervisory purposes. The Board continues to believe that five years is sufficient time for small BHCs to conform their existing debt structures. Such a transition period generally would be consistent with the five-year transition period afforded to larger BHCs to meet the Board's risk-based capital guidelines with respect to trust preferred securities.<sup>7</sup> However, in order to provide for equitable treatment of trust preferred issuances pending on the date of the proposed rule, the Board has decided to provide for a five-year transition period during which subordinated debt associated with trust preferred securities issued on or prior to December 31, 2005, would not be considered debt under the Policy Statement. Small BHCs may also refinance existing issuances of trust preferred securities without losing the exempt status of the related subordinated debt under the Policy Statement during the transition period

<sup>7</sup> See 12 CFR part 225, appendix A, § II.A.1.b.ii.

as long as the amount of the subordinated debt does not increase.

#### Small BHC Regulatory Reporting

To assist the Federal Reserve in monitoring the financial health and operations of BHCs, the Board requires all BHCs to file certain regulatory reports with the Federal Reserve. One of the most important of the Federal Reserve reporting requirements is the Financial Statements for Bank Holding Companies (FR Y-9 series of reports; OMB No. 7100-0128). Currently, BHCs that have consolidated assets of less than \$150 million (and that also meet qualitative criteria similar to those in the Policy Statement) generally submit limited summary parent-only financial data semiannually on the FR Y-9SP. Currently, BHCs with consolidated assets of \$150 million or more must submit parent only financial data on the FR Y-9LP and consolidated financial data on the FR Y-9C quarterly.

The Federal Reserve has issued a notice whereby it has proposed to revise the reporting requirements for the FR Y-9 series of reports for 2006 (2006 proposal).<sup>8</sup> If these reporting revisions are adopted, they would increase the FR Y-9SP reporting threshold from \$150 million to \$500 million in consolidated assets and conform the FR Y-9SP reporting exception criteria to the proposed qualitative exception criteria under the Policy Statement and the Capital Guidelines. Under the 2006 proposal, BHCs that meet the criteria for filing the FR Y-9SP would be exempt from filing the FR Y-9LP and FR Y-9C. Conversely, BHCs subject to the Capital Guidelines, including small BHCs that do not qualify under the revised Policy Statement and qualifying small BHCs that voluntarily elect to comply with the Capital Guidelines, would file the FR Y-9LP and the FR Y-9C on a quarterly basis.

#### Conforming Amendments

A number of documentation, filing, and other provisions in Regulation Y are triggered by the consolidated asset threshold established by the Board's Small Bank Holding Company Policy Statement. These provisions include, for example, the notice procedures for one-bank holding company formations in 12 CFR 225.17(a)(6). The Board has made technical and conforming amendments to these provisions to provide that qualifying small BHCs may take advantage of the streamlined informational and notice requirements embodied in these rules. These

technical and conforming amendments are a logical outgrowth of the revisions to the Policy Statement and the Capital Guidelines issued for public comment and, moreover, will provide relief to most bank holding companies with consolidated total assets of between \$150 million and \$500 million.

#### Regulatory Flexibility Act Analysis

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*), the Board has determined the rule would not have a significant impact on a substantial number of small entities, as defined in the Regulatory Flexibility Act. In this regard, the rule would reduce regulatory burden by exempting most BHCs with total consolidated assets of between \$150 million and \$500 million from the application of the Board's Capital Guidelines. Although the rule will treat subordinated debt associated with trust preferred securities as debt for most purposes under the Policy Statement, the final rule provides a substantial five-year transition period for subordinated debt associated with trust preferred securities issued on or prior to December 31, 2005.

#### Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3506; 5 CFR 1320 Appendix A.1.), the Board has reviewed this rulemaking under the authority delegated to the Board by the Office of Management and Budget. The Board has determined that the 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.*).

#### Plain Language

Section 722 of the Gramm-Leach-Bliley Act requires the Federal banking agencies to use "plain language" in all proposed and final rules published after January 1, 2000. Accordingly, the Board has sought to present the rule in a simple and straightforward manner.

#### List of Subjects in 12 CFR Part 225

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

#### Federal Reserve System

#### 12 CFR Chapter II

#### Authority and Issuance

■ For the reasons set forth in the preamble, part 225 of chapter II of title 12 of the Code of Federal Regulations is amended as set forth below:

#### 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 § 225.2, footnote 2 is revised to read as follows:

#### § 225.2 Definitions.

\* \* \* \* \*

<sup>2</sup> For purposes of this subpart and subparts B and C of this part, a bank holding company with consolidated assets of less than \$500 million that is subject to the Small Bank Holding Company Policy Statement in Appendix C of this part will be deemed to be "well-capitalized" if the bank holding company meets the requirements for expedited/waived processing in Appendix C.

\* \* \* \* \*

■ 3. Section 225.4(b)(2)(iii) is revised as follows:

#### § 225.4 Corporate practices.

\* \* \* \* \*

(b) \* \* \*

(2) \* \* \*

(iii) (A) If the bank holding company has consolidated assets of \$500 million or more, consolidated *pro forma* risk-based capital and leverage ratio calculations for the bank holding company as of the most recent quarter, and, if the redemption is to be debt funded, a parent-only *pro forma* balance sheet as of the most recent quarter; or

(B) If the bank holding company has consolidated assets of less than \$500 million, a *pro forma* parent-only balance sheet as of the most recent quarter, and, if the redemption is to be debt funded, one-year income statement and cash flow projections.

\* \* \* \* \*

■ 4. Section 225.14(a)(1)(v) is revised as follows:

#### § 225.14 Expedited action for certain bank acquisitions by well-run bank holding companies.

(a) \* \* \*

(1) \* \* \*

(v)(A) If the bank holding company has consolidated assets of \$500 million or more, an abbreviated consolidated *pro forma* balance sheet as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction, consolidated *pro forma* risk-based capital ratios for the acquiring bank holding company as of the most recent quarter, and a

<sup>8</sup> 70 FR 66423, November 2, 2005. Comments on this proposal were due by January 3, 2006.

description of the purchase price and the terms and sources of funding for the transaction;

(B) If the bank holding company has consolidated assets of less than \$500 million, a pro forma parent-only balance sheet as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction, and a description of the purchase price, the terms and sources of funding for the transaction, and the sources and schedule for retiring any debt incurred in the transaction;

\* \* \* \* \*

■ 5. In § 225.17, footnote 5 is revised to read as follows:

**§ 225.17 Notice procedure for one-bank holding company formations.**

\* \* \* \* \*

<sup>5</sup> For a banking organization with consolidated assets, on a pro forma basis, of less than \$500 million (other than a banking organization that will control a de novo bank), this requirement is satisfied if the proposal complies with the Board's Small Bank Holding Company Policy Statement (Appendix C of this part).

\* \* \* \* \*

■ 6. Section 225.23(a)(1)(iii)(A) and (B) are revised as follows:

**§ 225.23 Expedited action for certain nonbanking proposals by well-run bank holding companies.**

- (a) \* \* \*
- (1) \* \* \*
- (iii) \* \* \*

(A) If the bank holding company has consolidated assets of \$500 million or more, an abbreviated consolidated pro forma balance sheet for the acquiring bank holding company as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction, consolidated pro forma risk-based capital ratios for the acquiring bank holding company as of the most recent quarter, a description of the purchase price and the terms and sources of funding for the transaction, and the total revenue and net income of the company to be acquired;

(B) If the bank holding company has consolidated assets of less than \$500 million, a pro forma parent-only balance sheet as of the most recent quarter showing credit and debit adjustments that reflect the proposed transaction, a description of the purchase price and the terms and sources of funding for the transaction and the sources and schedule for retiring any debt incurred in the transaction, and the total assets, off-balance sheet items, revenue and net income of the company to be acquired;

\* \* \* \* \*

■ 7. Appendix A to part 225 is amended as follows:

- a. In section I, the fifth undesignated paragraph is revised.
- b. In section I, footnote 4 is removed and reserved.
- c. In section IV.A, footnote 64 is revised.

**Appendix A to Part 225—Capital Adequacy Guidelines for Bank Holding Companies: Risk-Based Measure**

**I. Overview**

\* \* \* \* \*

The risk-based guidelines apply on a consolidated basis to any bank holding company with consolidated assets of \$500 million or more. The risk-based guidelines also apply on a consolidated basis to any bank holding company with consolidated assets of less than \$500 million if the holding company (i) is engaged in significant nonbanking activities either directly or through a nonbank subsidiary; (ii) conducts significant off-balance sheet activities (including securitization and asset management or administration) either directly or through a nonbank subsidiary; or (iii) has a material amount of debt or equity securities outstanding (other than trust preferred securities) that are registered with the Securities and Exchange Commission (SEC). The Federal Reserve may apply the risk-based guidelines at its discretion to any bank holding company, regardless of asset size, if such action is warranted for supervisory purposes.<sup>4</sup>

\* \* \* \* \*

<sup>4</sup> [Reserved].

\* \* \* \* \*

**IV. Minimum Supervisory Ratios and Standards**

\* \* \* \* \*

*A. Minimum Risk-Based Ratio After Transition Period*

\* \* \* \* \*

<sup>64</sup> As noted in section I, bank holding companies with less than \$500 million in consolidated assets would generally be exempt from the calculation and analysis of risk-based ratios on a consolidated holding company basis, subject to certain terms and conditions.

\* \* \* \* \*

■ 8. Appendix C to part 225 is amended as follows:

- a. In section 1, the first undesignated paragraph is revised.
- b. In section 1, footnote 1 is removed and reserved.
- c. In section 2.A., a new paragraph is added after the first paragraph in footnote 3.

**Appendix C to Part 225—Small Bank Holding Company Policy Statement**

\* \* \* \* \*

1. \* \* \*

This policy statement applies only to bank holding companies with pro forma

consolidated assets of less than \$500 million that (i) are not engaged in significant nonbanking activities either directly or through a nonbank subsidiary; (ii) do not conduct significant off-balance sheet activities (including securitization and asset management or administration) either directly or through a nonbank subsidiary; and (iii) do not have a material amount of debt or equity securities outstanding (other than trust preferred securities) that are registered with the Securities and Exchange Commission. The Board may in its discretion exclude any bank holding company, regardless of asset size, from the policy statement if such action is warranted for supervisory purposes.<sup>1</sup>

\* \* \* \* \*

<sup>1</sup> [Reserved].

\* \* \* \* \*

2. \* \* \*

A. \* \* \*

3 \* \* \*

Subordinated debt associated with trust preferred securities generally would be treated as debt for purposes of paragraphs 2.C., 3.A., 4.A.i, and 4.B.i. of this policy statement. A bank holding company, however, may exclude from debt an amount of subordinated debt associated with trust preferred securities up to 25 percent of the holding company's equity (as defined below) less goodwill on the parent company's balance sheet in determining compliance with the requirements of such paragraphs of the policy statement. In addition, a bank holding company subject to this Policy Statement that has not issued subordinated debt associated with a new issuance of trust preferred securities after December 31, 2005 may exclude from debt any subordinated debt associated with trust preferred securities until December 31, 2010. Bank holding companies subject to this Policy Statement may also exclude from debt until December 31, 2010, any subordinated debt associated with refinanced issuances of trust preferred securities originally issued on or prior to December 31, 2005, provided that the refinancing does not increase the bank holding company's outstanding amount of subordinated debt. Subordinated debt associated with trust preferred securities will not be included as debt in determining compliance with any other requirements of this policy statement.

\* \* \* \* \*

■ 9. Appendix D to part 225 is amended as follows:

- a. In section I., paragraph b. is revised.
- b. In section I.b., footnote 2 is removed and reserved.

**Appendix D to Part 225—Capital Adequacy Guidelines for Bank Holding Companies: Tier 1 Leverage Measure**

**I. Overview**

\* \* \* \* \*

b. The tier 1 leverage guidelines apply on a consolidated basis to any bank holding company with consolidated assets of \$500 million or more. The tier 1 leverage guidelines also apply on a consolidated basis to any bank holding company with



consolidated assets of less than \$500 million if the holding company (i) is engaged in significant nonbanking activities either directly or through a nonbank subsidiary; (ii) conducts significant off-balance sheet activities (including securitization and asset management or administration) either directly or through a nonbank subsidiary; or (iii) has a material amount of debt or equity securities outstanding (other than trust preferred securities) that are registered with the Securities and Exchange Commission. The Federal Reserve may apply the tier 1 leverage guidelines at its discretion to any bank holding company, regardless of asset size, if such action is warranted for supervisory purposes.<sup>2</sup>

\* \* \* \* \*

<sup>2</sup> [Reserved].

\* \* \* \* \*

By order of the Board of Governors of the Federal Reserve System, February 22, 2006.

**Jennifer J. Johnson,**  
*Secretary of the Board.*

[FR Doc. 06-1837 Filed 2-27-06; 8:45 am]

**BILLING CODE 6210-02-P**