FEDERAL RESERVE BANK OF NEW YORK

[Circular No. **10333** January 16, 1990]

CAPITAL ADEQUACY

Proposed Transition Capital Guidelines and Guidelines for New Leverage Constraint

Comments Requested by March 9

To All State Member Banks and Bank Holding Companies in the Second Federal Reserve District, and Others Concerned:

Our Circular No. 10320, dated December 1, 1989, contained an announcement by the Board of Governors of the Federal Reserve System of its intention to seek public comment on proposed transition capital standards for State member banks and bank holding companies through the end of 1990; the Board's statement also set forth preliminary views on the appropriate leverage standard in conjunction with the risk-based capital framework after year-end 1990.

The Board is now formally seeking public comment on these matters. In that connection, the Board has issued the following statement:

> The Federal Reserve Board has requested public comment on proposed transition capital standards for state member banks and bank holding companies through the end of 1990. The proposed guidelines also set forth the Board's preliminary views on the appropriate leverage standard to be applied to banking organizations in conjunction with the risk-based capital framework after year-end 1990.
>
> Comments should be received by the Board on this matter no later than March 9, 1990.
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> On November 22, 1989, the Board announced its proposed transition capital standards, and indicated that it would seek public comment on the standards by year-end.

Printed on the following pages is an excerpt from the *Federal Register* of January 5, 1990, containing the Board's official notice. Comments thereon should be submitted by March 9 and may be sent to the Board, as indicated in the notice, or to our Bank Analysis Department.

E. Gerald Corrigan,
President.

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FEDERAL RESERVE SYSTEM

12 CFR Parts 208 and 225

[Regulation H, Regulation Y; Docket No. R-0683]

Capital; Capital Adequacy Guidelines

December 29, 1989.

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Notice of proposed guidelines.

SUMMARY: When the Board of Governors of the Federal Reserve System ("Board") issued final risk-based capital guidelines on January 19, 1989, it indicated that the existing 5.5 percent and 6 percent primary and total capital to total assets (leverage) ratios would stay in effect at least until the end of 1990, when the interim minimum risk-based capital ratios take effect. The Board also indicated that it would consider proposing a revised leverage constraint that, if adopted, would replace the existing leverage guidelines. It was contemplated that the definition of capital for the new leverage guidelines would be consistent with the risk-based capital definition.

The Board is now proposing for public comment transition capital guidelines to be applied through the end of 1990, as well as guidelines for a new leverage constraint. The Board believes that these steps, taken together, should assist state-chartered member banks and bank holding companies (collectively "banking organizations") in formulating their capital planning process and in strengthening their capital base.

Under the proposal, a banking organization may choose up to the end of 1990 to conform to either the existing minimum capital adequacy ratios (5.5 percent primary capital and 6 percent total capital to total assets) or to the 7.25 percent year-end 1990 risk-based capital standard. In addition, the Board is proposing to establish and apply during this period a minimum ratio of 3 percent Tier 1 capital to total assets (leverage ratio). For leverage purposes, Tier 1 would be defined consistent with the year-end 1992 risk-based capital guidelines.

The Board is also proposing to drop the existing 5.5 percent primary and 6.0 percent total capital to total assets leverage ratios after year-end 1990. The 3 percent Tier 1 leverage ratio would then constitute the minimum capital to total assets standard for banking organizations.

Under the Board's proposal, these standards would be minimum requirements. Any institution operating at or near these levels would be expected to have well-diversified risk, including no undue interest rate risk exposure, excellent asset quality, high liquidity, good earnings and, in general, would have to be considered a strong banking organization, rated composite 1 under the appropriate bank or bank holding company rating system. Any institution experiencing or anticipating significant growth would be expected to maintain capital well above the minimum levels as has been the case in the past. For example, most such banking organizations have generally operated at capital levels ranging from 100 to 200 basis points above the stated minimums. Higher capital ratios could be required if warranted by the particular circumstances or risk profiles of individual banking organizations. In all cases, banking institutions should hold capital commensurate with the level and nature of all of the risks, including the volume and severity of problem loans, to which they are exposed.

Whenever appropriate, in particular when an organization is undertaking expansion, seeking to engage in new activities or otherwise facing unusual or abnormal risks, the Board will continue to consider, on a case-by-case basis, the level of an organization's tangible Tier 1 leverage ratio (after deducting all intangibles) in making an overall assessment of capital. This is consistent with the Federal Reserve's risk-based capital guidelines and long-standing Board policy and practice under the current leverage guidelines. Organizations experiencing growth, whether internally or by acquisition, are expected to maintain strong capital positions substantially above minimum supervisory levels, without significant reliance on intangible assets.

DATE: Comments should be submitted on or before March 9, 1990.

ADDRESS: Comments, which should refer to Docket No. R-0683, may be mailed to the Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551, to the attention of Mr. William W. Wiles, Secretary; or delivered to room B-2223, Eccles Building, between 8:45 a.m. and 5:15 p.m. Comments may be inspected in room B-1122 between 9:00 a.m. and 5:00 p.m., except as provided in § 261.8 of the Board's Rules Regarding Availability of Information, 12 CFR 261.8.

FOR FURTHER INFORMATION CONTACT: Richard Spillenkothen, Deputy Associate Director (202/452-2594), Roger Cole, Assistant Director (202/452-2618), Rhoger H. Pugh, Manager (202/728-5883), or Norah Barger, Senior Financial Analyst (202/452-2402), Division of Banking Supervision and Regulation, Board of Governors; Michael J. O'Rourke, Senior Attorney (202/452-3288) or Mark J. Tenhundfeld, Attorney (202/452-3612), Legal Division, Board of Governors; or Donald E. Schmid, Manager (212/720-6611) or Manuel J. Schnaidman, Senior Financial Analyst (212/720-6710), Federal Reserve Bank of New York. For the hearing impaired *only*, Telecommunication Device for the Deaf (TDD), Earnestine Hill or Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION:

I. Background

The Federal Reserve's risk-based capital guidelines adopted January 27, 1989 (54 FR 4186) set forth an interim target risk-based ratio effective year-end 1990 and a final risk-based standard effective year-end 1992. In issuing its risk-based capital guidelines, the Board indicated that the existing 5.5 and 6.0 percent primary and total capital to total assets (leverage) ratios would stay in effect, at least until the end of 1990. A principal reason for this was to retain a capital constraint until the interim minimum risk-based capital ratios take effect.

The Board also indicated that even after minimum risk-based capital ratios become effective, retention of an overall leverage constraint might be deemed appropriate because the risk-based capital framework does not incorporate a comprehensive measure of interest rate risk. A minimum ratio of capital to total assets would help to address this potential problem by imposing an overall limitation on the extent to which a banking organization could leverage its equity capital base.

In addition to interest rate risk, capital ratios may also not take full or explicit account of certain other risk factors that can affect a banking organization's risk profile. These factors include funding and market risks; investment or loan portfolio concentrations; asset quality; and the adequacy of internal policies, systems, and controls. These factors, which must be taken into account in determining the overall risk profile and capital adequacy of a banking organization, also suggest the need to generally encourage banking organizations to operate well above minimum supervisory ratios.

In issuing its risk-based capital guidelines, the Board indicated that retention of the existing leverage ratios would provide an element of stability during the risk-based capital transition period. The Board further stated that if retention of an overall leverage

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standard were deemed appropriate in the long-run, the Federal Reserve would consider replacing the existing primary and total capital to total assets leverage ratios with a standard that incorporates a definition of capital that is consistent with the definitions contained in the risk-based capital framework. At the time, the Board indicated that a leverage standard based upon a revised definition of capital, and used in conjunction with a strong risk-based capital requirement, could be set at a level different from the existing leverage standard it would replace.

The Board is now proposing for public comment transition capital guidelines to be applied through the end of 1990, as well as guidelines for a new leverage constraint which the Board believes should replace the existing leverage guidelines at the end of 1990. Taken together, these steps should assist banking organizations in their capital planning process and, where necessary, their efforts to raise additional capital and strengthen their capital base.

II. Proposed Transition and Leverage Standards

A. Transition Standards

The Board is proposing that during the first phase of the risk-based capital transition period, which ends at year-end 1990, a banking organization may conform to either the existing minimum capital adequacy ratios of 5.5 percent primary capital and 6 percent total capital to total assets, or to the 7.25 percent year-end 1990 minimum risk-based capital standard. It should be emphasized that banking organizations are not required to meet the interim risk-based standard prior to its year-end 1990 effective date. Rather, organizations have the option of complying with the risk-based standard during 1990 in lieu of meeting the existing primary and total capital adequacy guidelines. Regardless of which of these options a banking organization chooses, during this period banking organizations would also have to meet the new proposed leverage standard set forth below.

B. New Leverage Standard

The Board is also proposing to establish and apply during 1990 and thereafter a minimum Tier 1 capital to total assets (leverage) ratio of 3 percent. For this purpose, the definition of Tier 1 capital for year-end 1992, as set forth in the risk-based capital guidelines, will be used.[1] Total assets would be defined for this purpose as total consolidated assets (defined net of the allowance for loan and lease losses), less goodwill and any other intangible assets or investments in subsidiaries that the primary regulator determines should be deducted from Tier 1 capital on a case-by-case basis.

Finally, the Board is also proposing that at the end of 1990 the existing leverage ratios, that is, the 5.5 percent and 6.0 percent primary and total capital to total assets leverage ratios, would be dropped. The 3 percent Tier 1 capital to total assets ratio would then constitute the leverage standard for banking organizations, and would be used thereafter in conjunction with the risk-based ratio in determining the overall capital adequacy of banking organizations.

The proposed Tier 1 leverage ratio differs in a number of respects from the current primary and total capital ratios as defined under the Federal Reserve's existing leverage guidelines. For example, primary capital includes the allowance for loan and lease losses (without limitation), and total capital includes limited amounts of subordinated debt. Neither of these elements, both of which are deemed to be Tier 2 components under the risk-based capital framework, is included in the definition of capital for the newly proposed Tier 1 leverage ratio. Moreover, the current primary and total capital leverage standards do not contain an absolute minimum for the level of permanent shareholders' equity in relation to assets—a minimum that is established by the proposed Tier 1 leverage standard. Thus, the proposed Tier 1 leverage ratio reflects the amount of core equity that is available to support unanticipated losses—a key prudential measure for determining the health of individual banking organizations. In addition to these benefits, adoption of Tier 1 for the purpose of comparing capital to total assets will have the advantage of bringing the definition of capital for leverage purposes into line with the definition of capital for risk-based capital purposes.

The Board emphasizes that in all cases, the standards set forth above are supervisory minimums. An institution operating at or near these levels is expected to have well-diversified risk, including no undue interest rate risk exposure; excellent asset quality; high liquidity; good earnings; and in general be considered a strong banking organization, rated composite 1 under the CAMEL rating system for banks or the BOPEC rating system for bank holding companies. Institutions with high or inordinate levels of risk are expected to operate well above minimum capital standards. As has been the case in the past, institutions experiencing or anticipating significant growth are also expected to maintain capital well above the minimum levels. For example, most such banking organizations generally have operated at capital levels ranging from 100 to 200 basis points above the stated minimums. Higher capital ratios could be required if warranted by the particular circumstances or risk profiles of individual banking organizations. In all cases, banking institutions should hold capital commensurate with the level and nature of all of the risks, including the volume and severity of problem loans, to which they are exposed.

Whenever appropriate, in particular when an organization is undertaking expansion, seeking to engage in new activities or otherwise facing unusual or abnormal risks, the Board will continue to consider, on a case-by-case basis, the level of an organization's tangible Tier 1 leverage ratio (after deducting all intangibles) in making an overall assessment of capital. This is consistent with the Federal Reserve's risk-based capital guidelines and long-standing Board policy and practice under the current leverage guidelines. Organizations experiencing growth, whether internally or by acquisition, are expected to maintain strong capital positions substantially above minimum supervisory levels, without significant reliance on intangible assets.

III. Regulatory Flexibility Act Analysis

The Federal Reserve Board does not believe that adoption of this proposal would have a significant economic impact on a substantial number of small business entities (in this case, small banking organizations), in accord with the spirit and purposes of the Regulatory

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[1] At the end of 1992, Tier 1 capital for state member banks includes common equity, minority interests in equity accounts of consolidated subsidiaries, and qualifying noncumulative perpetual preferred stock, less goodwill. It excludes any other intangible assets and investments in subsidiaries that the Federal Reserve determines should be deducted from capital for supervisory purposes on a case-by-case basis. For bank holding companies, Tier 1 capital at the end of 1992 includes common equity, minority interests in equity accounts of consolidated subsidiaries, and qualifying cumulative and noncumulative perpetual preferred stock. (Perpetual preferred stock is limited to 25 percent of Tier 1 capital.) In addition, Tier 1 excludes goodwill as well as any other intangibles and investments in subsidiaries that the primary regulator determines should be deducted from capital on a case-by-case basis. (This summary of Tier 1 capital definitions is purely illustrative in nature. Comprehensive Tier 1 capital definitions are set forth in Appendix A to part 208 of the Board's Regulation H for state member banks and in Appendix A to part 225 of the Board's Regulation Y for bank holding companies.)

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Flexibility Act (5 U.S.C. 601 et seq.). In addition, consistent with current policy, these guidelines generally will not apply to bank holding companies with consolidated assets of less than $150 million. Moreover, rather than requiring all banking organizations to raise additional capital, the guidelines are directed at institutions whose capital positions are less than fully adequate in relation to their risk and leverage profiles.

List of Subjects

12 CFR Part 208

Banks, Banking, Capital adequacy, Federal Reserve System, Reporting and recordkeeping requirements, State member banks.

12 CFR Part 225

Banks, Banking, Capital adequacy, Federal Reserve System, Holding companies, Reporting and recordkeeping requirements, State member banks.

For the reasons set forth in this notice, and pursuant to the Board's authority under section 5(b) of the Bank Holding Company Act of 1956 (12 U.S.C. 1844(b)), and section 910 of the International Lending Supervision Act of 1983 (12 U.S.C. 3909), the Board proposes to amend 12 CFR parts 208 and 225 as follows:

PART 208—MEMBERSHIP OF STATE BANKING INSTITUTIONS IN THE FEDERAL RESERVE SYSTEM

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

Authority: Sections 9, 11(a), 11(c), 19, 21, 25, and 25(a) of the Federal Reserve Act, as amended (12 U.S.C. 321–338, 248(a), 248(c), 461, 481–486, 601, and 611, respectively); sections 4 and 13(j) of the Federal Deposit Insurance Act, as amended (12 U.S.C. 1814 and 1923(j), respectively); section 7(a) of the International Lending Supervision Act of 1978 (12 U.S.C. 3105); sections 907–910 of the International Banking Act of 1983 (12 U.S.C. 3906–3909); sections 2, 12(b), 12(g), 12(i), 15B(c)(5), 17, 17A, and 23 of the Securities Exchange Act of 1934 (15 U.S.C. 78b, 78*l*(b), 78*l*(g), 78*l*(i), 78*l*–4(c)(5), 78q, 78q–1, and 78w, respectively); and section 5155 of the Revised Statutes (12 U.S.C. 36) as amended by the McFadden Act of 1927.

2. Section 208.13 is revised to read as follows:

§ 208.13 Capital adequacy.

The standards and guidelines by which the capital adequacy of state member banks will be evaluated by the Board are set forth in Appendix A to part 208 for risk-based capital purposes, and, with respect to the ratios relating capital to total assets, in Appendix B to part 208 and in Appendix B to the Board's Regulation Y, 12 CFR part 225.

Appendix A—[Amended]

3. Footnote 1 to *"I. Overview" of* Appendix A to part 208 is revised to read as follows:

[1] Supervisory ratios that relate capital to total assets for state member banks are outlined in Appendix B of this part and in Appendix B to part 225 of the Federal Reserve's Regulation Y, 12 CFR part 225.

4. The last sentence of the first paragraph to *"IV. Minimum Supervisory Ratios and Standards"* is removed; a new paragraph is added immediately following the first paragraph; the existing second paragraph now becomes the third paragraph and remains unchanged. The new second paragraph reads as follows:

Institutions with high or inordinate levels of risk are expected to operate well above minimum capital standards. Banks experiencing or anticipating significant growth are also expected to maintain capital well above the minimum levels. For example, most such institutions generally have operated at capital levels ranging from 100 to 200 basis points above the stated minimums. Higher capital ratios could be required if warranted by the particular circumstances or risk profiles of individual banks. In all cases, banks should hold capital commensurate with the level and nature of all of the risks, including the volume and severity of problem loans, to which they are exposed.

5. A second paragraph is added to "IV. B. Transition Arrangements" of Appendix A to part 208 to read as follows:

Through year-end 1990 banks have the option of complying with the minimum 7.25 percent year-end 1990 risk-based capital standard in lieu of the minimum 5.5 percent primary and 6 percent total capital to total assets capital ratios set forth in Appendix B to part 225 of the Federal Reserve's Regulation Y. In addition, as more fully set forth in Appendix B to this part, banks are expected to maintain a minimum ratio of 3 percent Tier l capital to total assets during this transition period.

6. Appendix B is added after "Attachment VI.—Summary" to part 208 to read as set forth below.

Appendix B to Part 208—Capital Adequacy Guidelines for State Member Banks: Tier 1 Leverage Measure

I. Overview

The Board of Governors of the Federal Reserve System has adopted a minimum ratio of Tier 1 capital to total assets to assist in the assessment of the capital adequacy of state member banks.[1] The principal objective of this measure is to place a constraint on the maximum degree to which a state member bank can leverage its equity capital base.

The guidelines apply to all state member banks on a consolidated basis and are to be used in the examination and supervisory process as well as in the analysis of applications acted upon by the Federal Reserve. The Board will review the guidelines from time to time and will consider the need for possible adjustments in light of any significant changes in the economy, financial markets, and banking practices.

II. The Tier 1 Leverage Ratio

The Board has established a minimum level of Tier 1 capital to total assets of 3 percent. An institution operating at or near these levels is expected to have well-diversified risk, including no undue interest rate risk exposure; excellent asset quality; high liquidity; good earnings; and in general be considered a strong banking organization, rated composite 1 under the CAMEL rating system of banks. Institutions not meeting these characteristics, as well as institutions with supervisory, financial, or operations weaknesses, are expected to operate well above minimum capital standards. Institutions experiencing or anticipating significant growth also are expected to maintain capital well above the minimum levels. For example, most such banks generally have operated at capital levels ranging from 100 to 200 basis points above the stated minimums. Higher capital ratios could be required if warranted by the particular circumstances or risk profiles of individual banks. In all cases, banking institutions should hold capital commensurate with the level and nature of all of the risks, including the volume and severity of problem loans, to which they are exposed.

A bank's Tier 1 leverage ratio is calculated by dividing its Tier 1 capital (the numerator of the ratio) by its average total consolidated assets (the denominator of the ratio). The ratio will also be calculated using period-end assets whenever necessary on a case-by-case basis. For the purpose of this leverage ratio, the definition of Tier 1 capital for year-end 1992 as set forth in the risk-based capital guidelines contained in Appendix A of this Part will be used.[2] Average total consolidated assets are defined as the quarterly average total assets (defined net of the allowance for loan and lease losses) reported on the bank's Reports of Condition and Income ("Call Report"), less goodwill and any other intangible assets and investments in subsidiaries that the Federal Reserve determines should be deducted from Tier l capital on a case-by-case basis.[3]

[1] Supervisory risk-based capital ratios that relate capital to weighted risk assets for state member banks are outlined in Appendix A to this part.

[2] At the end of 1992, Tier 1 capital for state member banks includes common equity, minority interests in equity accounts of consolidated subsidiaries, and qualifying noncumulative perpetual preferred stock, less goodwill. In general, no other deductions from capital are made automatically. However, the Federal Reserve may, on a case-by-case basis, exclude certain other intangibles and investments in subsidiaries as appropriate.

[3] Deductions from Tier 1 capital and other adjustments are discussed more fully in section II.B. of Appendix A to this part.

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Whenever appropriate, in particular when a bank is undertaking expansion, seeking to engage in new activities or otherwise facing unusual or abnormal risks, the Board will continue to consider, on a case-by-case basis, the level of an individual bank's tangible Tier 1 leverage ratio (after deducting all intangibles) in making an overall assessment of capital. This is consistent with the Federal Reserve's risk-based capital guidelines and long-standing Board policy and practice with regard to leverage guidelines. Banks experiencing growth, whether internally or by acquisition, are expected to maintain strong capital positions substantially above minimum supervisory levels, without significant reliance on intangible assets.

PART 225—BANK HOLDING COMPANIES AND CHANGE IN BANK CONTROL

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

Authority: 12 U.S.C. 1817(j)(13), 1818, 1843(c)(8), 1844(b), 3106, 3108, 3907, 3909.

Appendix A—[Amended]

2. Footnote 1 to "*I. Overview*" of Appendix A to part 225 is revised to read as follows:

[1] Supervisory ratios that relate capital to total assets for bank holding companies are outlined in Appendices B and D of this part.

3. The last sentence of the first paragraph to "*IV. Minimum Supervisory Ratios and Standards*" is removed; a new paragraph is added immediately following the first paragraph; the existing second paragraph now becomes the third paragraph and remains unchanged. The new second paragraph reads as follows:

Institutions with high or inordinate levels of risk are expected to operate well above minimum capital standards. Banking organizations experiencing or anticipating significant growth are also expected to maintain capital well above the minimum levels. For example, most such organizations generally have operated at capital levels ranging from 100 to 200 basis points above the stated minimums. Higher capital ratios could be required if warranted by the particular circumstances or risk profiles of individual banking organizations. In all cases, organizations should hold capital commensurate with the level and nature of all of the risks, including the volume and severity of problem loans, to which they are exposed.

4. A second paragraph is added to "IV. B. Transition Arrangements" of Appendix A to part 225 to read as follows:

Through year-end 1990 banking organizations have the option of complying with the minimum 7.25 percent year-end 1990 risk-based capital standard in lieu of the minimum 5.5 percent primary and 6 percent total capital to total assets ratios set forth in Appendix B of this Part. In addition, as more fully set forth in Appendix D to this Part, banking organizations are expected to maintain a minimum ratio of 3 percent Tier l capital to total assets during this transition period.

Appendix B—[Amended]

5. Three new sentences are added to the end of the first paragraph of Appendix B to part 225 to read as follows:

* * * In this regard, the Board has determined that during the transition period through year-end 1990 for implementation of the risk-based capital guidelines contained in Appendix A to this part and in Appendix A to part 208, a banking organization may choose to fulfill the requirements of the guidelines relating capital to total assets contained in this Appendix in one of two manners. Until year-end 1990, a banking organization may choose to conform to either the 5.5 percent and 6 percent minimum primary and total capital standards set forth in this Appendix or the 7.25 percent year-end 1990 minimum risk-based capital standard set forth in Appendix A to this part and Appendix A to part 208. Those organizations that choose to conform during this period to the 7.25 percent year-end 1990 risk-based capital standard will be deemed to be in compliance with the capital adequacy guidelines set forth in this Appendix.

6. Appendix D is added after Appendix C to part 225 to read as set forth below.

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

I. Overview

The Board of Governors of the Federal Reserve System has adopted a minimum ratio of Tier 1 capital to total assets to assist in the assessment of the capital adequacy of bank holding companies ("banking organizations").[1] The principal objective of this measure is to place a constraint on the maximum degree to which a banking organization can leverage its equity capital base.

The guidelines apply on a consolidated basis to bank holding companies with consolidated assets of $150 million or more. For bank holding companies with less than $150 million in consolidated assets, the guidelines will be applied on a bank-only basis unless: (a) The parent bank holding company is engaged in nonbank activity involving significant leverage; [2] or (b) the parent company has a significant amount of outstanding debt that is held by the general public.

The Tier 1 leverage guidelines are to be used in the inspection and supervisory process as well as in the analysis of applications acted upon by the Federal Reserve. The Board will review the guidelines from time to time and will consider the need for possible adjustments in light of any significant changes in the economy, financial markets, and banking practices.

II. The Tier 1 Leverage Ratio

The Board has established a minimum level of Tier l capital to total assets of 3 percent. A banking organization operating at or near these levels is expected to have well-diversified risk, including no undue interest rate risk exposure; excellent asset quality; high liquidity; good earnings; and in general be considered a strong banking organization, rated composite l under the BOPEC rating system for bank holding companies. Organizations not meeting these characteristics, as well as institutions with supervisory, financial, or operations weaknesses, are expected to operate well above minimum capital standards. Organizations experiencing or anticipating significant growth also are expected to maintain capital well above the minimum levels. For example, most such organizations generally have operated at capital levels ranging from 100 to 200 basis points above the stated minimums. Higher capital ratios could be required if warranted by the particular circumstances or risk profiles of individual banking organizations. In all cases, banking organizations should hold capital commensurate with the level and nature of all of the risks, including the volume and severity of problem loans, to which they are exposed.

A banking organization's Tier 1 leverage ratio is calculated by dividing its Tier 1 capital (the numerator of the ratio) by its average total consolidated assets (the denominator of the ratio). The ratio will also be calculated on the basis of period-end assets whenever necessary on a case-by-case basis. For the purpose of this leverage ratio, the definition of Tier l capital for year-end 1992 as set forth in the risk-based capital guidelines contained in Appendix A to this part will be used.[3] Average total consolidated assets are defined as the quarterly average total assets (defined net of the allowance for loan and lease losses) reported on the banking organization's Consolidated Financial Statements ("FR Y-9C Report"), less goodwill and any other intangible assets or investments in

[1] Supervisory risk-based capital ratios that relate capital to weighted risk assets for bank holding companies are outlined in Appendix A to this Part.

[2] A parent company that is engaged in significant off-balance sheet activities would generally be deemed to be engaged in activities that involve significant leverage.

[3] At the end of 1992, Tier 1 capital for bank holding companies includes common equity, minority interests in equity accounts of consolidated subsidiaries, and qualifying cumulative and noncumulative perpetual preferred stock. (Perpetual preferred stock is limited to 25 percent of Tier 1 capital.) In addition, Tier 1 excludes goodwill. In general, no other deductions from capital are made automatically. However, the Federal Reserve may, on a case-by-case basis, exclude certain other intangibles and investments in subsidiaries as appropriate.

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subsidiaries that the Federal Reserve determines should be deducted from Tier 1 capital on a case-by-case basis.[4]

Whenever appropriate, in particular when an organization is undertaking expansion, seeking to engage in new activities or otherwise facing unusual or abnormal risks, the Board will continue to consider, on a case-by-case basis, the level of an individual organization's tangible Tier 1 leverage ratio (after deducting all intangibles) in making an overall assessment of capital. This is consistent with the Federal Reserve's risk-based capital guidelines and long-standing Board policy and practice with regard to leverage guidelines. Organizations experiencing growth, whether internally or by acquisition, are expected to maintain strong capital positions substantially above minimum supervisory levels, without significant reliance on intangible assets.

Board of Governors of the Federal Reserve System, December 29, 1989.

William W. Wiles,

Secretary of the Board.

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[4] Deductions from Tier 1 capital and other adjustments are discussed more fully in section II.B. of Appendix A to this part.

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