

**FEDERAL RESERVE BANK
OF NEW YORK**

[Circular No. **10736**]
November 2, 1994]

RISK-BASED CAPITAL GUIDELINES
Joint Proposal to Amend the Risk-Based Capital Guidelines
Comments Invited by December 13

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

The Board of Governors of the Federal Reserve System and the Office of the Comptroller of the Currency have issued a joint *Federal Register* notice to amend their respective risk-based capital guidelines in order to modify the definition of the OECD-based group of countries so as to exclude from that group any country that has rescheduled its external sovereign debt within the previous five years. Countries included in the group are eligible for lower risk weights in determining their credit risk.

Printed on the following pages is the text of the joint notice, which has been reprinted from the *Federal Register* of October 14. Comments thereon should be submitted by December 13, 1994, and may be sent to the appropriate agency, as specified in the notice, or to our Banking Studies Department.

WILLIAM J. McDONOUGH,
President.

Proposed Rules

Federal Register

Vol. 59, No. 198

Friday, October 14, 1994

DEPARTMENT OF THE TREASURY

Office of the Comptroller of the
Currency

12 CFR Part 3

[Docket No. 94-16]

RIN 1557-AB14

FEDERAL RESERVE SYSTEM

12 CFR Parts 208 and 225

[Regulations H and Y; Docket No. R-0849]

Capital; Capital Adequacy Guidelines

AGENCIES: The Office of the Comptroller of the Currency (OCC), Department of the Treasury and the Board of Governors of the Federal Reserve System (FRB).

ACTION: Notice of proposed rulemaking.

SUMMARY: The OCC and FRB (the agencies) are proposing to amend their respective risk-based capital guidelines to modify the definition of the OECD-based group of countries. Claims on the governments and banks of this group generally receive lower risk weights than corresponding claims on the governments and banks of non-OECD-based countries. The agencies are proposing this amendment on the basis of an announcement, made on July 15, 1994, by the Basle Committee on Banking Supervision (Basle Committee) that, subject to national consultation, the Basle Committee plans to introduce a change to the Basle Accord in 1995. The effect of the proposed modification would be to exclude from the OECD-based group of countries which are eligible for the lower risk weights any country that has rescheduled its external sovereign debt within the previous five years.

DATES: Comments must be received on or before December 13, 1994.

ADDRESSES: Interested parties are invited to submit written comments to any or all of the agencies. Each agency will share the comments that it receives with the other agencies.

OCC: Written comments should be submitted to Docket No. 94-16, Communications Division, Ninth Floor, Office of the Comptroller of the Currency, 250 E. Street, Washington, D.C., 20219, Attention: Karen Carter. Comments will be available for inspection and photocopying at that address.

FRB: Comments should refer to Docket No. R-0849 and may be mailed to William W. Wiles, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, D.C. 20551. Comments may also be delivered to Room B-2222 of the Eccles Building between 8:45 a.m. and 5:15 p.m. weekdays, or to the guard station in the Eccles Building courtyard on 20th Street, N.W. (between Constitution Avenue and C Street) at any time. Comments may be inspected in Room MP-500 of the Martin Building between 9:00 a.m. and 5:00 p.m. weekdays, except as provided in 12 CFR 261.8 of the Board's Rules regarding availability of information.

FOR FURTHER INFORMATION CONTACT:

OCC: Geoffrey White, Senior International Economic Advisor, International Banking and Finance Division, (202) 874-4730; Ronald Shimabukuro, Senior Attorney, Bank Operations and Assets Division, (202) 874-4460; or Roger Tufts, Senior Economic Advisor, Office of the Chief National Bank Examiner, (202) 874-5070.

FRB: Roger Cole, Deputy Associate Director (202/452-2618), Norah Barger, Manager (202/452-2402), Robert Motyka, Supervisory Financial Analyst (202/452-3621), Division of Banking Supervision and Regulation; or Greg Baer, Managing Senior Counsel (202/452-3236), Legal Division. For the hearing impaired only, Telecommunication Device for the Deaf, Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION:

I. Background

In 1988 the central bank governors of the G-10 countries endorsed international capital standards (the Basle Accord)¹ establishing a risk-based

¹ The Basle Accord was proposed by the Basle Committee, which comprises representatives of the central banks and supervisory authorities from the G-10 countries (Belgium, Canada, France, Germany,

framework for measuring the capital adequacy of internationally-active banks. Under the framework, risk-weighted assets are calculated by assigning assets and off-balance-sheet items to broad categories based primarily on their credit risk, that is, the risk that a banking organization will incur a loss due to an obligor or counterparty default on a transaction. Risk weights range from zero percent, for assets with minimal credit risk (such as U.S. Treasury securities), to 100 percent, which is the risk weight that applies to most private sector claims, including all commercial loans.

While the Basle Accord primarily focuses on credit risk, it also incorporates country transfer risk considerations.² In addressing transfer risk, the Basle Committee members examined several methods for assigning obligations of foreign countries to the various risk categories. Ultimately, the Basle Committee decided to use a defined group of countries considered to be of high credit standing as the basis for differentiating claims on foreign governments and banks. For this purpose, the Basle Committee determined this group as the full members of the Organization for Economic Cooperation and Development (OECD), as well as countries that have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the IMF's General Arrangements to Borrow.³ These

Italy, Japan, the Netherlands, Sweden, Switzerland, the United Kingdom, and the United States) and Luxembourg.

In 1989 the Board adopted risk-based capital guidelines implementing the Basle Accord for state member banks and bank holding companies.

² Transfer risk generally refers to the possibility that an asset cannot be serviced in the currency of payment because of a lack of, or restraints on, the availability of needed foreign exchange in the country of the obligor.

³ The OECD is an international organization of countries which are committed to market-oriented economic policies, including the promotion of private enterprise and free market prices; liberal trade policies; and the absence of exchange controls. Full members of the OECD at the time the Basle Accord was endorsed included Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. In May 1994, Mexico was accepted as a full member of the OECD. In addition, Saudi Arabia has concluded special lending arrangements associated with the International Monetary Fund's General Arrangements to Borrow.

countries are referred to as the OECD-based group of countries⁴ and encompass most of the major industrial countries, including all members of the G-10 and the European Union.

Under both the Basle Accord and the agencies' guidelines, claims on the governments and banks of the OECD-based group of countries generally receive lower risk weights than corresponding claims on the governments and banks of non-OECD countries. Specifically, the agencies' guidelines provide for the following treatment:

- Direct claims on, and the portions of claims that are directly and unconditionally guaranteed by, OECD-based central governments (including central banks) are assigned to the zero percent risk weight category. Claims on central governments outside the OECD-based group are assigned to the zero percent risk weight category only if such claims are denominated in the national currency and funded by liabilities in the same currency.
- Claims conditionally guaranteed by OECD-based central governments and claims collateralized by securities issued or guaranteed by OECD-based central governments generally are assigned to the 20 percent risk weight category. The same types of claims on non-OECD countries are assigned to the 100 percent risk category.
- Long-term claims on OECD banks are assigned to the 20 percent risk-weight category. Long-term claims on non-OECD banks are assigned to the 100 percent risk category. (Short-term claims on all banks, whether they are members of the OECD-based group of countries or not, are assigned a 20 percent risk weight.)
- General obligation bonds that are obligations of states or other political subdivisions of the OECD-based group of countries are assigned to the 20 percent risk category. Revenue bonds of such political subdivisions are assigned to the 50 percent risk category. Both general obligation and revenue bonds of political subdivisions of non-OECD countries are assigned to the 100 percent risk category.

Recently, the OECD has taken steps to expand its membership. In light of these steps, the Basle Committee was urged to clarify an ambiguity in the Basle Accord as to whether the OECD members eligible for the lower risk weights

⁴FRB regulations define this group as the "OECD-based group of countries." OGC regulations define a member of this group as an "OECD-based country." While the choice of words is slightly different, the definitions are effectively the same, and the use of either definition in this preamble should be taken to refer to both.

include only those members that were in the OECD when the Basle Accord was endorsed in 1988 or all members, regardless of entry date into the OECD. The Basle Committee also reviewed the overall appropriateness of the criteria the Basle Accord uses to determine whether claims on a foreign government or bank qualify for placement in a lower risk category. As part of this review, the Basle Committee reassessed whether membership in the OECD (or the conclusion of special lending arrangements with the IMF) would, by itself, be sufficient to ensure that only countries with relatively low transfer risk would continue to be eligible for lower risk weight treatment.

On July 15, 1994, the Basle Committee made an announcement that clarified that the reference in the Basle Accord to OECD members applies to all current members of the organization. The announcement also stated that it is the Basle Committee's intention, subject to national consultation, to record a change to the Basle Accord in 1995 that would modify the definition of the OECD-based group of countries for risk-based capital purposes. The change, if adopted, would exclude from lower risk weight treatment any country within the OECD-based group of countries that has rescheduled its external sovereign debt within the previous five years. The Basle Committee announcement was endorsed by the G-10 Governors.

II. The Agencies' Proposal

In view of the Basle Committee's announcement, the agencies are proposing to amend their respective risk-based capital guidelines to modify the definition of the OECD-based group of countries. Under the proposal, the OECD-based group of countries would continue to include countries that are currently full members of the OECD, regardless of entry date, as well as countries that have concluded special lending arrangements with the IMF associated with the Fund's General Arrangements to Borrow, but would exclude any country within this group that has rescheduled its external sovereign debt within the previous five years. The effect of the proposed modification would be to clarify that membership in the OECD-based group of countries must coincide with relatively low transfer risk in order for a country to be eligible for differentiated capital treatment.

For purposes of this proposal, an event of rescheduling of external sovereign debt generally would include renegotiations of terms arising from the country's inability or unwillingness to meet its external debt service

obligations. Renegotiations of debt in the normal course of business generally does not indicate transfer risk of the kind that would preclude an OECD-based country from qualifying for lower risk weight treatment. One example of such a routine renegotiation would be a renegotiation to allow the borrower to take advantage of a change in market conditions, such as a decline in interest rates.

The agencies invite comment on all aspects of this proposal.

III. Regulatory Flexibility Act

The agencies hereby certify 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 Flexibility Act (5 U.S.C. 601 et seq.). In addition, because the risk-based capital standards generally do not apply to bank holding companies with consolidated assets of less than \$150 million, this proposal will not affect such companies. Accordingly, no regulatory flexibility analysis is required.

IV. Paperwork Reduction Act

The agencies have determined that adoption of the proposed amendments would not increase the regulatory paperwork burden of banking organizations pursuant to the provisions of the Paperwork Reduction Act (44 U.S.C. 3501 et seq.).

Executive Order 12866

The OCC has determined that this proposed rule is not a significant regulatory action, as that term is defined by Executive Order 12866.

List of Subjects

12 CFR Part 3

Administrative practice and procedure, Capital, National banks, Reporting and recordkeeping requirements, Risk.

12 CFR Part 208

Accounting, Agriculture, Banks, banking, Capital adequacy, Confidential business information, Currency, Federal Reserve System, Reporting and recordkeeping requirements, Securities, State member banks.

12 CFR Part 225

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

Authority and Issuance**Office of the Comptroller of the Currency
12 CFR Chapter I**

For the reasons set out in the joint preamble, title 12, chapter I, part 3 of the Code of Federal Regulations is proposed to be amended as set forth below.

**PART 3—MINIMUM CAPITAL RATIOS;
ISSUANCE OF DIRECTIVES**

1. The authority citation for Part 3 is revised to read as follows:

Authority: 12 U.S.C. 93a, 161, 1818, 1828(n), 1828 note, 1831n note, 3907 and 3909.

2. In section 1 of appendix A to part 3, paragraph (c)(16) is revised to read as follows:

Appendix A to Part 3—Risk-Based Capital Guidelines*Section 1. Purpose, Applicability of Guidelines, and Definitions.*

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(c) * * *

(16) *OECD-based country* means a member of the grouping of countries that are full members of the Organization of Economic Cooperation and Development, plus countries that have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the IMF's General Arrangements to Borrow, but excludes any country that has rescheduled its external sovereign debt within the previous five years. These countries are hereinafter referred to as "OECD countries".

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Dated: October 4, 1994

Eugene A. Ludwig,
Comptroller of the Currency.

Federal Reserve System**12 CFR Chapter II**

For the reasons set forth in the joint preamble, the Board proposes to amend 12 CFR parts 208 and 225 as set forth below:

**PART 208—MEMBERSHIP OF STATE
BANKING INSTITUTIONS IN THE
FEDERAL RESERVE SYSTEM
(REGULATION H)**

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

Authority: 12 U.S.C. 36, 248 (a) and (c), 321-338a, 371d, 461, 481-486, 601, 611, 1814, 1823(j), 1828(o), 1831o, 1831p-1, 3105, 3310, 3331-3351, and 3906-3909; 15 U.S.C. 78b, 78l(b), 78l(g), 78l(i), 78o-4(c)(5), 78q, 78q-1 and 78w; 31 U.S.C. 5318.

2. Appendix A to part 208 is amended by revising footnote 22 in section III.B.1. to read as follows:

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

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²² The OECD-based group of countries comprises all full members of the Organization for Economic Cooperation and Development (OECD), as well as countries that have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the IMF's General Arrangements to Borrow, but excludes any country that has rescheduled its external sovereign debt within the previous five years. The OECD includes the following countries: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. Saudi Arabia has concluded special lending arrangements with the IMF associated with the IMF's General Arrangements to Borrow.

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**PART 225—BANK HOLDING
COMPANIES AND CHANGE IN BANK
CONTROL (REGULATION Y)**

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

Authority: 12 U.S.C. 1817(j)(13), 1818, 1831i, 1843(c)(8), 1844(b), 1972(l), 3106, 3108, 3310, 3331-3351, 3907, and 3909.

2. Appendix A to part 225 is amended by revising footnote 25 in section III.B.1. to read as follows:

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

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²⁵ The OECD-based group of countries comprises all full members of the Organization for Economic Cooperation and Development (OECD), as well as countries that have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the IMF's General Arrangements to Borrow, but excludes any country that has rescheduled its external sovereign debt within the previous five years. The OECD includes the following countries: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. Saudi Arabia has concluded special lending arrangements with the IMF associated with the IMF's General Arrangements to Borrow.

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By the order of the Board of Governors of the Federal Reserve System, October 6, 1994.

Jennifer J. Johnson,

Deputy Secretary of the Board.

[FR Doc. 94-25299 Filed 10-13-94; 8:45 am]

BILLING CODES: 4810-33-P; 6210-01-P