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**DEPARTMENT OF TREASURY**

**Office of the Comptroller of the Currency**

**12 CFR Part 3**

**Docket ID OCC-2018-0019**

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**FEDERAL RESERVE SYSTEM**

**12 CFR Parts 217 and 252**

**Regulation Q; Docket No. R-1655**

**RIN 7100-AF43**

**FEDERAL DEPOSIT INSURANCE CORPORATION**

**12 CFR Part 324**

**RIN 3064-AE79**

**Regulatory Capital Treatment for Investments in Certain Unsecured Debt Instruments of Global Systemically Important U.S. Bank Holding Companies, Certain Intermediate Holding Companies, and Global Systemically Important Foreign Banking Organizations; Total-Loss Absorbing Capacity Requirements**

**AGENCY:** Office of the Comptroller of the Currency, Treasury (OCC); the Board of Governors of the Federal Reserve System (Board); and the Federal Deposit Insurance Corporation (FDIC).

**ACTION:** Final rule.

**SUMMARY:** The OCC, Board, and FDIC (collectively, the agencies) are adopting a final rule that applies to advanced approaches banking organizations with the aim of reducing both interconnectedness within the financial system and systemic risk. The final rule requires deduction from a banking organization's regulatory capital for certain investments in unsecured

debt instruments issued by foreign or U.S. global systemically important banking organizations (GSIBs) for the purposes of meeting minimum total loss absorbing capacity (TLAC) requirements and, where applicable, long-term debt requirements, or for investments in unsecured debt instruments issued by GSIBs that are *pari passu* or subordinated to such debt instruments. In addition, the Board is adopting changes to its TLAC rules to clarify requirements and correct drafting errors.

**DATES:** The final rule is effective on April 1, 2021.

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**I. *Introduction***

The Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (Board), and Federal Deposit Insurance Corporation (FDIC) (together, the agencies) are issuing a final rule to revise the regulatory capital rule in a manner substantially

consistent with a proposed rule issued in April 2019 (proposal).<sup>1</sup> The final rule addresses the regulatory capital treatment of investments by advanced approaches banking organizations in unsecured debt instruments issued by foreign or U.S. global systemically important banking organizations (GSIBs) for the purposes of meeting minimum total loss absorbing capacity (TLAC) requirements and, as applicable, long-term debt requirements, or of investments in unsecured debt instruments issued by GSIBs that are *pari passu* or subordinated to such debt instruments (covered debt instruments).<sup>2</sup> Consistent with the proposal, the exposures of an advanced approaches banking organization to covered debt instruments generally are subject to deduction from the banking organization’s regulatory capital. The final rule includes certain

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<sup>1</sup> See 84 FR 13814 (April 8, 2019).

<sup>2</sup> When the proposal was issued, a banking organization was an “advanced approaches banking organization” if it had total assets of at least \$250 billion, or if it had consolidated on-balance sheet foreign exposures of at least \$10 billion, or if it was a subsidiary of a depository institution, bank holding company, savings and loan holding company or intermediate holding company that was an advanced approaches banking organization. See 78 FR 62018, 62204 (October 11, 2013), 78 FR 55340, 55523 (September 10, 2013). See also 12 CFR part 3 (OCC); 12 CFR part 217 (Board); and 12 CFR part 324 (FDIC). In November 2019, the agencies issued a final rule to revise the criteria for determining the applicability of regulatory capital and liquidity requirements for large U.S. banking organizations and the U.S. intermediate holding companies of certain foreign banking organizations, including the application of the advanced approaches (interagency tailoring final rule). Under this final rule, advanced approaches banking organizations include those banking organizations subject to Category I standards (those banking organizations that qualify as U.S. GSIBs) or Category II standards (banking organizations with (1) at least \$700 billion in total consolidated assets or (2) at least \$75 billion in cross-jurisdictional activity and more than \$100 billion in total consolidated assets), and a subsidiary depository institution of such a banking organization. See 84 FR 59230 (November 1, 2019).

adjustments to the proposal in response to comments. The final rule aims to reduce both interconnectedness within the financial system and systemic risk.

## **II. Background**

### **A. Capital Requirements**

The agencies' regulatory capital rule (capital rule) imposes minimum capital requirements on banking organizations measured through risk-based and leverage capital ratios.<sup>3</sup> These regulatory capital ratios consist of regulatory capital measures relative to risk-weighted assets and total assets, respectively.<sup>4</sup> The numerators of the regulatory capital ratios include various adjustments and deductions to balance-sheet-based regulatory capital components.

The capital rule includes two broad categories of deductions from regulatory capital related to investments in the capital instruments of financial institutions by advanced approaches

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<sup>3</sup> Banking organizations subject to the agencies' capital rule include national banks, state member banks, insured state nonmember banks, savings associations, and top-tier bank holding companies, intermediate holding companies, and savings and loan holding companies domiciled in the United States, but exclude banking organizations subject to the Board's Small Bank Holding Company and Savings and Loan Holding Company Policy Statement (12 CFR part 225, appendix C), qualifying community banking organizations that elect to comply with the agencies' community bank leverage ratio framework, and certain savings and loan holding companies that are substantially engaged in insurance underwriting or commercial activities or that are estate trusts, and bank holding companies and savings and loan holding companies that are employee stock ownership plans.

<sup>4</sup> See 12 CFR 3.10(a) (OCC); 12 CFR 217.10(a) (Board); and 12 CFR 324.10(a) (FDIC). In addition to the generally applicable leverage ratio, advanced approaches banking organizations are subject to a supplementary leverage ratio, which measures a banking organization's tier 1 capital relative to its on-balance sheet and certain off-balance sheet exposures.

banking organizations.<sup>5</sup> First, it requires a banking organization to deduct any investment in its own regulatory capital instruments and any investment in regulatory capital instruments held reciprocally with another financial institution (reciprocal cross holding).<sup>6</sup> Second, it requires a banking organization to deduct investments in capital instruments issued by unconsolidated financial institutions that would qualify as regulatory capital if issued by the banking organization itself.<sup>7</sup> For the purpose of the latter deduction, a banking organization may be required to deduct the entire amount of the investment, or it may be required to deduct only the portion of the investment that exceeds a certain threshold.<sup>8</sup> These deductions are intended to reduce interconnectedness and contagion risk among financial institutions by discouraging banking organizations from investing in the capital of other financial institutions.

For deductions related to investments in the capital of unconsolidated financial institutions, a banking organization must deduct from the component of regulatory capital for which the instrument qualifies or would qualify if it were issued by the banking organization that is holding the exposure.<sup>9</sup> For example, an advanced approaches banking organization that owns 10 percent or less of the common stock of an unconsolidated financial institution is said to have a

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<sup>5</sup> A different deduction framework applies to non-advanced approaches banking organizations. *See* 84 FR 35234 (July 22, 2019).

<sup>6</sup> *See* 12 CFR 3.22(c)(1) (OCC); 12 CFR 217.22(c)(1) (Board); and 12 CFR 324.22(c)(1) (FDIC).

<sup>7</sup> *See* 12 CFR 3.22(c)(2) (OCC); 12 CFR 217.22(c)(2) (Board); and 12 CFR 324.22(c)(2) (FDIC).

<sup>8</sup> *See* 12 CFR 3.22(c)(3), (c)(5), and (c)(6) (OCC); 12 CFR 217.22(c)(3), (c)(5), and (c)(6) (Board); and 12 CFR 324.22(c)(3), (c)(5), and (c)(6) (FDIC).

<sup>9</sup> *See* 12 CFR Part 3, subparts D, E, or F, as applicable (OCC); 12 CFR Part 217, subparts D, E, and F, as applicable (Board); and 12 CFR Part 324, subparts D, E, or F, as applicable (FDIC).

“non-significant investment” in the capital of the unconsolidated financial institution. If the advanced approaches banking organization invests in tier 2 instruments issued by the unconsolidated financial institution, then it must deduct from its own tier 2 capital the amount, if any, by which the investment, combined with other non-significant investments in the capital of other unconsolidated financial institutions, exceeds 10 percent of the sum of the banking organization’s common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under section \_\_.22(a) through \_\_.22(c)(3), net of associated deferred tax liabilities (DTLs) (10 percent threshold for non-significant investments). Any non-significant investments in the capital of unconsolidated financial institutions that are not deducted from regulatory capital are risk-weighted in accordance with the capital rule.<sup>10</sup>

## **B. TLAC Rule**

In December 2016, the Board issued a final rule to require the largest domestic and foreign banking organizations operating in the United States to maintain a minimum amount of total loss-absorbing capacity (TLAC), consisting of tier 1 capital (excluding minority interest) and certain long-term debt instruments (TLAC rule).<sup>11</sup> The TLAC rule applies to a U.S. top-tier bank holding company identified under the Board’s rules as a global systemically important bank holding company (covered BHC) or a top-tier U.S. intermediate holding company subsidiary of a

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<sup>10</sup> See 12 CFR Part 3, subparts D, E, or F, as applicable (OCC); 12 CFR Part 217, subparts D, E, and F, as applicable (Board); and 12 CFR Part 324, subparts D, E, or F, as applicable (FDIC).

<sup>11</sup> See 82 FR 8266 (January 24, 2017); 12 CFR part 252, subparts G and P. The TLAC rule’s TLAC and long-term debt requirements took effect on January 1, 2019.



global systemically important foreign banking organization (foreign GSIB) with \$50 billion or more in U.S. non-branch assets (covered IHC) (collectively, covered banking organizations).

The objective of the TLAC rule is to enhance financial stability by reducing the impact of the failure of covered banking organizations by requiring such organizations to have sufficient loss-absorbing capacity on both a going-concern and a gone-concern basis. The TLAC rule includes requirements that a covered banking organization maintain outstanding minimum levels of TLAC and long-term debt.<sup>12</sup> TLAC is the sum of the tier 1 capital instruments issued directly by the covered banking organization (excluding minority interest) and the long-term debt issued directly by the covered banking organization. Under the TLAC rule, long-term debt is generally unsecured debt that is issued directly by a covered banking organization, has no features that would interfere with an orderly resolution proceeding, has a remaining maturity of at least one year, and is governed by U.S. law, among other provisions.<sup>13</sup>

Long-term debt instruments under the TLAC rule are capable of absorbing losses in resolution (i.e., on a gone-concern basis). This is because the debt holders' claim on a banking organization's assets may not receive full payment in a resolution, receivership, insolvency, or

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<sup>12</sup> See 12 CFR 252.62 and 252.63; 12 CFR 252.162 and 252.165. The requirements applicable under the TLAC rule to covered BHCs and covered IHCs are similar but not identical.

<sup>13</sup> Long-term debt issued by a covered IHC to affiliates of the covered IHC is subject to notable additional requirements, including the inclusion of a provision allowing the Board to order the conversion of the debt into common equity tier 1 capital of the covered IHC. See 12 CFR 252.163.

similar proceeding.<sup>14</sup> This potential loss-absorbing capacity of long-term debt is part of the rationale for the deduction approach for investments in such debt instruments under this final rule.<sup>15</sup>

Given the ability of long-term debt to absorb the losses of a covered banking organization in a resolution, receivership, insolvency, or similar proceeding, the Board proposed regulatory capital deductions for investments by Board-regulated banking organizations in long-term debt issued under the TLAC rule when it initially proposed the TLAC rule in 2015.<sup>16</sup> The Board did not finalize these limitations when it issued the final TLAC rule because it needed additional time to work with the OCC and the FDIC to develop a proposed interagency approach regarding the regulatory capital treatment for investments in certain debt instruments issued by covered banking organizations.

### ***III. Overview of Notice of Proposed Rulemaking and Comments***

In April 2019, the agencies issued a proposal to address, for purposes of the capital rule, the systemic risks posed by an advanced approaches banking organization's investments in covered debt instruments and to create an incentive for advanced approaches banking organizations to limit their exposure to GSIBs. The deductions required under the proposal

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<sup>14</sup> The internal debt conversion provision included in covered IHC long-term debt issued to affiliates performs a similar function outside of a resolution proceeding.

<sup>15</sup> Long-term debt under the TLAC rule may also qualify as tier 2 capital under the capital rule, if it satisfies the eligibility criteria for tier 2 capital.

<sup>16</sup> The proposal of the TLAC rule in 2015 was issued solely by the Board. Therefore, the proposed regulatory capital deductions in that proposal would have only applied to Board-regulated banking organizations, which include bank holding companies, intermediate holding companies, savings and loan holdings companies, and state member banks.

would have affected the capital ratios of advanced approaches banking organizations. Without the proposed changes, investments in covered debt instruments issued by covered BHCs, foreign GSIBs, and covered IHCs are generally not subject to deduction and would generally be subject to a risk weight of 100 percent.

An investment in a covered debt instrument, as defined in the proposal, by an advanced approaches banking organization would have been treated as an investment in a tier 2 capital instrument for purposes of the existing deduction framework. As a result, an investment in a covered debt instrument would have been subject to deduction from the advanced approaches banking organization's own tier 2 capital.

The existing corresponding deduction approach in the capital rule would have been amended to apply any required deduction by advanced approaches banking organizations of an investment in a covered debt instrument that exceeded certain thresholds, consistent with the deduction framework for investments in the capital of unconsolidated financial institutions. In addition, the existing deduction approaches under the capital rule would have been amended to apply to an advanced approaches banking organization's reciprocal cross holdings of covered debt instruments; that is, an advanced approaches banking organization would have deducted from its own tier 2 capital any reciprocal cross holdings of covered debt instruments with another banking organization. The existing deduction approaches under the capital rule would have also been amended to apply to a covered BHC's investments in its own covered debt instruments. Similarly, the existing deduction approaches under the capital rule would have also been amended to apply to a covered IHC subject to the advanced approaches (advanced approaches covered IHC) and its investments in its own covered debt instruments.

The proposal also included certain exclusions from deduction. Importantly, the proposal would have allowed advanced approaches banking organizations to exclude from deduction investments in covered debt instruments, subject to certain qualifying and measurement criteria, that are five percent or less of the sum of advanced approaches banking organization's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under section \_\_.22(a) through \_\_.22(c)(3), net of associated DTLs (five percent exclusion). As discussed in the preamble to the proposal, the agencies designed the exclusion from deduction to support deep and liquid markets for covered debt instruments issued by GSIBs. In the case of a U.S. GSIB, it would have applied the proposed exclusion only to "excluded covered debt instruments," which were defined in the proposal as covered debt instruments held for 30 business days or less and held for the purpose of short-term resale or with the intent of benefiting from actual or expected short-term price movements, or to lock in arbitrage profits. This provision was intended to limit the five percent exclusion for U.S. GSIBs to covered debt instruments held in connection with market making activities. Advanced approaches banking organizations that are not U.S. GSIBs would not have been subject to this limit on the use of the five percent exclusion. Under the proposal's five percent exclusion, all advanced approaches banking organizations could exclude covered debt instruments measured on a gross long basis from the deduction framework up to a cap of five percent of the banking organization's common equity tier 1 capital.

The proposal would have revised section \_\_.22(c), (f), and (h) of the capital rule to incorporate the proposed deduction approach for investments in covered debt instruments, and added several new definitions to section \_\_.2 to effectuate these deductions. Further, the

definition of “investment in the capital of an unconsolidated financial institution” would have been amended to correct a typographical error.

Collectively, the agencies received ten public comment letters from trade associations, public interest groups, private individuals, and other interested parties. As further detailed below, commenters generally supported the overarching goal of the proposal to reduce interconnectedness by creating an incentive for advanced approaches banking organizations to limit their exposure to GSIBs. However, commenters also expressed certain general concerns with the proposal and noted specific concerns with certain technical aspects of it.

The agencies are jointly finalizing a regulatory capital treatment for investments in covered debt instruments that applies to advanced approaches banking organizations. The final rule is substantially consistent with the proposal, with certain modifications in response to comments as well as some technical clarifications.

#### **IV. *Summary of the Final Rule***

The final rule applies to advanced approaches banking organizations and generally requires deductions from capital for direct, indirect, and synthetic exposures to covered debt instruments and any other unsecured debt instruments *pari passu* or subordinated to covered debt instruments.<sup>17</sup> Under the final rule, an advanced approaches banking organization treats investments in covered debt instruments as investments in tier 2 capital instruments for purposes

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<sup>17</sup> As discussed further in section V.C.2 below, the final rule excludes certain unsecured debt instruments issued by foreign GSIBs from the scope of the final rule. Specifically, the final rule generally excludes from the definition of covered debt instrument an unsecured debt instrument that cannot be written down or converted into equity (i.e., bailed in) under a special resolution regime.

of applying the corresponding deduction approach in the capital rule. Deduction from capital is required for:

- Investments in a covered BHC's or advanced approaches covered IHC's own covered debt instruments, as applicable;
- Reciprocal cross holdings with another financial institution of covered debt instruments;
- Investments in covered debt instruments of a financial institution while also holding 10 percent or more of the financial institution's common stock; and
- Investments in covered debt instruments that, together with investments in the capital of unconsolidated financial institutions, exceed 10 percent of the investing advanced approaches banking organization's common equity tier 1 capital.
- Under the final rule, an advanced approaches banking organization may exclude from deduction investments in certain covered debt instruments up to five percent of its common equity tier 1 capital, as measured on a gross long basis.<sup>18</sup> Usage of the five percent exclusion is tailored, depending on whether the advanced approaches banking organization is a U.S. GSIB.

For U.S. GSIBs, only "excluded covered debt instruments" are eligible for the five percent exclusion in the final rule. Generally, "excluded covered debt instruments" in the final rule are investments in covered debt instruments that are held in accordance with market making activities, as identified using criteria from the regulations implementing section 13 of the Bank

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<sup>18</sup> See 12 CFR 3.22(h)(2) (OCC); 12 CFR 217.22(h)(2) (Board); 12 CFR 324.2(h)(2) (FDIC).

Holding Company Act (commonly known as the Volcker Rule) as discussed in more detail in section V.E. below. A U.S. GSIB's direct or indirect exposure to a covered debt instrument is an excluded covered debt instrument if the exposure is held for 30 or fewer business days and held in connection with market making-related activities. A U.S. GSIB's holding of a synthetic exposure to a covered debt instrument is not limited to 30 business days in order to qualify as an excluded covered debt instrument.

For advanced approaches banking organizations that are not U.S. GSIBs, any direct, indirect, or synthetic exposure to a covered debt instrument issued by an unconsolidated financial institution that is a non-significant investment is eligible for the five percent exclusion in the final rule.

The final rule revises section \_\_.22(c), (f), and (h) of the capital rule to incorporate the deduction approach for investments in covered debt instruments. As with the proposal, several new definitions are added to section \_\_.2 in the final rule to effectuate these deductions. More information on these specific revisions to the capital rule are provided below.

**V. *Regulatory Capital Treatment for Advanced Approaches Banking Organizations' Investments in Covered Debt Instruments***

**A. Scope of Application**

The proposal would have applied the deduction framework for covered debt instruments to advanced approaches banking organizations. Since the proposal was issued, the agencies issued the interagency tailoring final rule that included revisions to the scope of advanced

approaches banking organizations.<sup>19</sup> As a result of the interagency tailoring final rule, “advanced approaches banking organizations” include those banking organizations subject to Category I standards (i.e., those banking organizations that qualify as U.S. GSIBs), Category II standards (i.e., banking organizations with (1) at least \$700 billion in total consolidated assets or (2) at least \$75 billion in cross-jurisdictional activity and at least \$100 billion in total consolidated assets), or a subsidiary depository institution of a banking organization subject to Category I or II standards. Some commenters suggested that the agencies should apply the proposal to all banking organizations subject to the capital rule. Other commenters suggested the agencies apply the proposal to all banking organizations subject to Category I through IV standards, as defined in the interagency tailoring final rule.<sup>20</sup>

After considering the comments, the agencies are continuing to limit the scope of this rule to advanced approaches banking organizations, as revised by the interagency tailoring final rule. As explained in the proposal, the systemic risk associated with banking organizations’ investments in covered debt instruments is greatest for the banking organizations covered by the proposal. However, the agencies acknowledge the possibility of potential systemic risks associated with other banking organizations’ investments in covered debt instruments and will continue to evaluate whether additional steps are warranted to address such risks.

## **B. Deduction from Tier 2 Capital**

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<sup>19</sup> See 84 FR 59230 (November 1, 2019).

<sup>20</sup> See 12 CFR 3.2 (OCC); 12 CFR 217.2 (Board); 12 CFR 324.2 (FDIC).



Under the agencies' capital rule, a banking organization must deduct from regulatory capital any investments in its own capital instruments and in the capital of other financial institutions that it holds reciprocally. Other investments in the capital of unconsolidated financial institutions are subject to deduction to the extent they exceed certain thresholds.

Under the proposal, an investment in a covered debt instrument by an advanced approaches banking organization would have been treated as an investment in a tier 2 capital instrument for purposes of the deduction framework, and therefore, would have been subject to deduction from the advanced approaches banking organization's own tier 2 capital. The existing corresponding deduction approach in the capital rule would have been amended to apply to any deduction by advanced approaches banking organizations of an investment in a covered debt instrument that exceeded certain thresholds, as if the covered debt instrument were a tier 2 capital instrument. In addition, the existing deduction approaches under the capital rule would have been amended to apply to a covered BHC's or advanced approaches covered IHC's investments in its own covered debt instruments, and to advanced approaches banking organizations' reciprocal cross holdings of covered debt instruments with other financial institutions. Such investments and cross holdings would be deducted from an advanced approaches banking organization's own tier 2 capital, as applicable.

Some commenters expressed concerns that deducting a covered debt instrument from an advanced approaches banking organization's own tier 2 capital is insufficiently restrictive. As an alternative, these commenters recommended that advanced approaches banking organizations deduct investments in covered debt instruments from their own common equity tier 1 capital. Some commenters suggested that the prohibition of all holdings of covered debt instruments by

advanced approaches banking organizations would be more appropriate. Other commenters expressed concerns that deducting a covered debt instrument from an advanced approaches banking organization's own tier 2 capital is overly restrictive. These commenters asserted that a covered BHC or advanced approaches covered IHC should be able to effectuate deductions from its own TLAC-eligible long-term debt rather than its own tier 2 capital.

Requiring deduction of a covered debt instrument from tier 2 capital should be a sufficiently prudent and simple approach that discourages advanced approaches banking organizations' investments in such instruments and thereby supports the objectives of reducing both interconnectedness within the financial system and systemic risk. Effectuating deductions from a covered BHC's or advanced approaches covered IHC's own TLAC-eligible debt, rather than own tier 2 capital, could disproportionately favor the largest and most internationally active banking organizations. A less complex banking organization, such as a non-GSIB advanced approaches banking organization, would make all deductions related to an investment in a covered debt instrument from its own tier 2 capital, since non-GSIBs are not required to issue TLAC-eligible debt. Further, allowing covered BHCs and advanced approaches covered IHCs to deduct from their own TLAC-eligible debt creates additional balance sheet capacity for these banking organizations to invest in covered debt instruments issued by other GSIBs relative to non-GSIB advanced approaches banking organizations, thereby undermining a goal of the final rule to reduce interconnectedness among large and internationally active banking organizations. The disproportionate effects of allowing deduction from own TLAC-eligible debt would be further exacerbated if the agencies were to expand the scope of the final rule in the future as described above.

As such, the agencies are finalizing, as proposed, the requirement that an advanced approaches banking organization treat an investment in a covered debt instrument as an investment in a tier 2 capital instrument, and therefore, deduct such investment from its own tier 2 capital.

### **C. Amendments to Definitions**

The proposal would have added or amended certain definitions in section \_\_.2 of the capital rule to implement the proposed deduction approach.

#### *1. Definition of “Covered Debt Instrument” for Covered BHC and Covered IHC Issuance*

Under the proposal, a “covered debt instrument” would have been defined to include an unsecured debt instrument that is:

(1) Issued by a covered BHC and that is an “eligible debt security” for purposes of the TLAC rule,<sup>21</sup> or that is *pari passu* or subordinated to any “eligible debt security” issued by the covered BHC; or

(2) Issued by a covered IHC and that is an “eligible Covered IHC debt security” for purposes of the TLAC rule,<sup>22</sup> or that is *pari passu* or subordinated to any “eligible Covered IHC debt security” issued by the covered IHC.

Under the proposal, a covered debt instrument would not have included a debt instrument that qualifies as tier 2 capital under the capital rule.

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<sup>21</sup> See 12 CFR 252.61.

<sup>22</sup> See 12 CFR 252.161.

Some commenters requested that *pari passu* or subordinated unsecured debt instruments be excluded from the definition of “covered debt instrument.” Commenters argued that it is not practical to determine whether a given instrument is *pari passu* or subordinated to TLAC-eligible debt issued by a covered BHC or covered IHC and whether a given debt instrument was an eligible long-term debt instrument under the TLAC rule. Further, commenters argued that because the TLAC rule limits the amount of debt that a covered BHC or covered IHC can issue that is not TLAC-eligible but is *pari passu* with or subordinated to TLAC-eligible debt, significant amounts of such debt should not be outstanding.

Treating unsecured debt instruments that are *pari passu* or subordinated to TLAC-eligible debt instruments as “covered debt instruments” is important, given that these liabilities will incur losses ahead of or proportionally with TLAC-eligible debt. Excluding these *pari passu* and subordinated instruments from the regulatory deduction treatment would understate the degree of risk of these investments. Advanced approaches banking organizations should be able to determine whether an instrument qualifies as TLAC under applicable standards, or whether an instrument is *pari passu* or subordinated to a company’s TLAC-eligible debt instruments based on public information and routine due diligence. Accordingly, the agencies are finalizing as proposed the above prongs of the definition of covered debt instrument for covered BHC and covered IHC debt issuances.

## *2. Definition of “Covered Debt Instrument” for Foreign GSIB Issuance*

A “covered debt instrument” also would have included any unsecured debt instrument issued by a foreign GSIB or any of its subsidiaries, other than its covered IHC, for the purpose of absorbing losses or recapitalizing the issuer or any of its subsidiaries in connection with a

resolution, receivership, insolvency, or similar proceeding of the issuer or any of its subsidiaries (foreign TLAC-eligible debt). Further, covered debt instruments would have also included any debt instrument that is *pari passu* or subordinated to any foreign TLAC-eligible debt, other than an unsecured debt instrument that is included in the regulatory capital of the issuer.

Commenters suggested that the scope of the definition of “covered debt instrument” should be revised to include only foreign TLAC-eligible debt as determined under applicable home-country standards.<sup>23</sup> Commenters stated that the proposed scope of the definition is broader than necessary because the issuance of such liabilities is subject to the Financial Stability Board (FSB)’s TLAC term sheet’s limitation on issuance of excluded liabilities.<sup>24</sup> Some

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<sup>23</sup> The Basel Committee’s *TLAC Holdings* standard excludes from the definition of “other TLAC liabilities” instruments that are *pari passu* to (1) excluded liabilities and (2) other instruments that are eligible for recognition as external TLAC by virtue of the exemptions to the subordination requirements in the Financial Stability Board’s TLAC term sheet. *See* section 66.c of the *TLAC Holdings* standard. Only a proportion of instruments that are eligible to be recognized as external TLAC by virtue of the subordination exemptions may be considered TLAC under the *TLAC Holdings* standard. The proportion equals the ratio of (1) the debt instruments issued by a GSIB that rank *pari passu* to excluded liabilities and that are recognized as external TLAC by the GSIB, to (2) the debt instruments issued by the GSIB that rank *pari passu* to excluded liabilities and that would be recognized as external TLAC if the subordination requirement was not applied. As stated in the proposal, the agencies believe that implementation of the proportional deduction approach used in the Basel Committee’s *TLAC Holdings* standard would have introduced too much complexity and operational burden to the capital rule; the final rule does not implement the proportional deduction approach. *See* Basel Committee for Banking Supervision and Regulation, “TLAC Holdings” (October 12, 2016), available at [https://www.bis.org/bcbs/publ/d387.pdf\\_\(TLAC Holdings standard\)](https://www.bis.org/bcbs/publ/d387.pdf_(TLAC%20Holdings%20standard)).

<sup>24</sup> *See* Financial Stability Board, “Principles on Loss-absorbing and Recapitalisation Capacity of G-SIBs in Resolution - Total Loss-absorbing Capacity (TLAC) Term Sheet,” (November 9, 2015), available at <https://www.fsb.org/wp-content/uploads/TLAC-Principles-and-Term-Sheet-for-publication-final.pdf>.

commenters suggested that liabilities issued by foreign GSIBs that are “excluded liabilities” under the FSB’s TLAC term sheet should be excluded from the proposal’s definition of covered debt instrument and therefore exempted from the deduction framework.<sup>25</sup>

Some commenters reiterated that it is not practical for banking organizations to determine whether a given instrument is *pari passu* or subordinated to foreign TLAC-eligible debt as such a determination requires complex analyses of foreign law with respect to insolvency regimes and creditor hierarchies. Commenters also asserted that there could be unintended consequences of including instruments that are *pari passu* or subordinated to foreign TLAC-eligible debt, including interference with ordinary interbank transactions. As a result, banking organizations would make conservative assumptions and treat all unsecured debt instruments issued by foreign GSIBs as subject to the deduction framework. Therefore, commenters suggested that the final rule should not include instruments *pari passu* or subordinated to foreign TLAC-eligible debt in the definition of “covered debt instruments.”

For the same reasons discussed above with respect to instruments issued by covered BHCs and covered IHCs, the final rule defines debt instruments that are *pari passu* or subordinated to foreign TLAC-eligible debt as “covered debt instruments.” As discussed, such

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<sup>25</sup> Under the FSB’s TLAC term sheet, “excluded liabilities” do not qualify as TLAC and therefore are not subject to deduction under the *TLAC Holdings* standard, even if they rank *pari passu* or subordinated to a TLAC instrument. Excluded liabilities include deposits, liabilities arising from derivatives, and structured notes, among other items. The TLAC rule prohibits or limits covered banking organizations from entering into financial arrangements that may compromise an orderly resolution process, including limiting the amount of liabilities to unaffiliated companies.

instruments would incur losses ahead of or proportionally with foreign TLAC-eligible debt and therefore should be subject to the deduction framework.

However, the agencies recognize the commenters' concerns and revise in two ways the definition of covered debt instruments issued by foreign GSIBs and their subsidiaries, other than covered IHCs. First, the final rule provides that an instrument is a covered debt instrument if it is "eligible for use to comply with an applicable law or regulation" requiring the issuance of a minimum amount of instruments to absorb losses or to recapitalize the issuer or any of its subsidiaries in connection with a resolution, receivership, insolvency, or similar proceeding. The proposal's definition would not have explicitly considered whether the instrument is eligible for use to comply with such a law or regulation.

Second, the final rule revises the definition of a covered debt instrument to exclude certain unsecured debt instruments from the scope of the definition. If the issuer may be subject to a special resolution regime, in its jurisdiction of incorporation or organization, that addresses the failure or potential failure of a financial company and foreign TLAC-eligible debt is eligible under that special resolution regime to be written down or converted into equity or any other capital instrument, then an instrument is *pari passu* or subordinated to foreign TLAC-eligible debt if that instrument is eligible to be written down or converted into equity or another capital instrument under that special resolution regime ahead of or proportionally with any foreign TLAC-eligible debt. These revisions reflect the FSB's TLAC term sheet's focus on having

instruments and liabilities that should be readily available for bail-in, and that instruments that cannot be bailed in effectively rank senior to foreign TLAC-eligible debt in bail-in.<sup>26</sup>

These revisions should reduce the burden associated with determining whether unsecured debt instruments are *pari passu* or subordinated to foreign TLAC-eligible debt. For purposes of the final rule, an advanced approaches banking organization can rely on the terms of any special resolution regime and other applicable laws or regulations for purposes of determining the applicability of the final rule’s deduction framework for an unsecured debt instrument. For example, if the applicable law or regulation specifies the seniority of instruments that must be issued, the advanced approaches banking organization can rely on that specification of seniority in determining whether a different instrument is *pari passu* or subordinated to TLAC-eligible debt instruments.

These revisions also address concerns raised by commenters that the proposal could have interfered with ordinary interbank transactions. For example, if the special resolution regime applicable to a foreign GSIB provides that deposits are excluded from bail-in, those deposits are not covered debt instruments subject to the final rule’s deduction framework.

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<sup>26</sup> Generally, a resolution regime that is consistent with the FSB’s *Key Attributes of Effective Resolution Regimes for Financial Institutions* would be a special resolution regime that addresses the failure or potential failure of a financial company. See Financial Stability Board, “Key Attributes of Effective Resolution Regimes for Financial Institutions,” (October 15, 2014), [https://www.fsb.org/wp-content/uploads/r\\_141015.pdf](https://www.fsb.org/wp-content/uploads/r_141015.pdf). Current examples of special resolution regimes that address the failure or potential failure of a financial company are those included in the International Swaps and Derivatives Association (ISDA) 2015 Universal Resolution Stay Protocol and the ISDA 2018 U.S. Resolution Stay Protocol. See ISDA 2015 Universal Resolution Stay Protocol (November 4, 2015), <http://assets.isda.org/media/ac6b533f-3/5a7c32f8-pdf>; ISDA 2018 U.S. Resolution Stay Protocol (July 31, 2018), [https://www.isda.org/a/CIjEE/3431552\\_40ISDA-2018-U.S.-Protocol-Final.pdf](https://www.isda.org/a/CIjEE/3431552_40ISDA-2018-U.S.-Protocol-Final.pdf).



### *3. Other Definitions*

Similar to the measurement of investments in the capital of unconsolidated financial institutions, an “investment in a covered debt instrument” would have been defined in the proposal as a net long position in a covered debt instrument, including direct, indirect, and synthetic exposures to such covered debt instruments. Investments in covered debt instruments would have excluded underwriting positions held for five business days or less. In addition, the proposal would have amended the definitions of “indirect exposure” and “synthetic exposure” in the capital rule to add exposures to covered debt instruments.<sup>27</sup> The agencies received no comments on these technical elements of the proposal, and are finalizing, as proposed, the definitions for “investment in a covered debt instrument,” “indirect exposure,” and “synthetic exposure.”

#### **D. Investments in Covered Banking Organizations’ Own Covered Debt Instruments and Reciprocal Cross Holdings**

Under the agencies’ capital rule, a banking organization must deduct from regulatory capital an investment in its own capital instruments and investments in the capital of other financial institutions that it holds reciprocally under sections \_\_.22(c)(1) and (3), respectively. The proposal would have amended section 217.22(c)(1) to require a covered BHC or a covered IHC to deduct from tier 2 capital its investments in its own covered debt instruments. The proposal also would have amended section \_\_.22(c)(3) to require advanced approaches banking

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<sup>27</sup> See 12 CFR 3.2 (OCC); 12 CFR 217.2 (Board); and 12 CFR 324.2 (FDIC) (“investment in the capital of an unconsolidated financial institution,” “investment in the banking organization’s own capital instrument,” “indirect exposure,” and “synthetic exposure”).

organizations to deduct from tier 2 capital any investment in a covered debt instrument that is held reciprocally with another financial institution.

As described earlier, some commenters expressed concerns that deducting a covered debt instrument from an advanced approaches banking organization's own tier 2 capital is overly restrictive, including in cases of deductions for investments in its own covered debt instruments, as applicable, and reciprocal cross holdings with other financial institutions. These commenters asserted that a covered BHC or a covered IHC should be able to effectuate deductions from its own TLAC-eligible long-term debt rather than its own tier 2 capital for these investments.

Requiring a deduction of a covered debt instrument from tier 2 capital for deductions related to investments in an advanced approaches banking organization's own covered debt instruments and reciprocal cross holdings should be a sufficiently prudent and simple approach that discourages advanced approaches banking organizations' investments in such instruments, as applicable, and thereby supports the objectives of reducing both interconnectedness within the financial system and systemic risk. As mentioned earlier, effectuating deductions from a covered BHC's or a covered IHC's own TLAC-eligible debt, rather than its own tier 2 capital, could disproportionately favor the largest and most internationally active banking organizations. As such, the agencies are finalizing, as proposed, that an advanced approaches banking organization will generally deduct investments in own covered debt instruments, as applicable, and reciprocal cross holdings with other financial institutions in covered debt instruments from its own tier 2 capital.

Commenters asked that the final rule include a separate deduction threshold for market making activities in an advanced approaches banking organization's own covered debt

instruments capped at five percent of a covered BHC's or advanced approaches covered IHC's own common equity tier 1 capital. Commenters stated that such a threshold is necessary to better facilitate deep and liquid markets for TLAC-eligible debt instruments. Further, commenters claimed that GSIBs are often the biggest market makers in their own covered debt instruments and, under the U.S. GAAP accounting standard, their own holdings of covered debt instruments are not always eliminated in full in consolidation. In cases where a GSIB's investments in its own covered debt instruments are not fully extinguished, the exposure amount can be greater than zero and therefore subject to deduction from tier 2 capital under the proposal.

Commenters stated that a separate five percent threshold for market making in an advanced approaches banking organization's own covered debt instruments in the final rule would prevent a capital deduction for such investments. However, finalizing the rule with a separate threshold for investments in an advanced approaches banking organization's own covered debt instruments could create additional balance sheet capacity for covered BHCs and advanced approaches covered IHCs to increase their investments in covered debt instruments issued by other GSIBs. Such an approach would not align with the proposal's goal of reducing interconnectedness and systemic risk among large and internationally active banking organizations. Therefore, the final rule does not implement this suggested change.

#### **E. Significant and Non-Significant Investments in Covered Debt Instruments**

Under sections \_\_.22(c)(5) and (6) of the capital rule, an advanced approaches banking organization must deduct from regulatory capital certain investments in the capital of unconsolidated financial institutions. The calculation of the deduction depends on whether the banking organization has a "significant" or a "non-significant" investment, with "significant"

defined as ownership of more than 10 percent of the common stock of the unconsolidated financial institution and “non-significant” defined as ownership of 10 percent or less of the common stock of the unconsolidated financial institution.<sup>28</sup> When a banking organization has a “significant investment” in an unconsolidated financial institution, the banking organization must deduct from regulatory capital any investment in the capital of the unconsolidated financial institution that is not in the form of common stock as measured on a net long basis, and the banking organization must also deduct from regulatory capital any investment in the capital of the unconsolidated financial institution in the form of common stock that exceeds 10 percent of the advanced approaches banking organization’s own common equity tier 1 capital as measured on a net long basis.<sup>29</sup> If an advanced approaches banking organization has one or more “non-significant investments” in unconsolidated financial institutions, it must aggregate such investments and deduct from regulatory capital any amount that exceeds the 10 percent threshold for non-significant investments, as measured on a net long basis.<sup>30</sup>

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<sup>28</sup> See 12 CFR 3.2 (OCC); 12 CFR 217.2 (Board); 12 CFR 324.2 (FDIC) (“significant investment in the capital of an unconsolidated financial institution” and “non-significant investment in the capital of an unconsolidated financial institution”).

<sup>29</sup> See 12 CFR 3.22(c)(6) and (d)(2)(i)(C) (OCC); 12 CFR 217.22(c)(6) and (d)(2)(i)(C) (Board); and 12 CFR 324.22(c)(6) and (d)(2)(i)(C) (FDIC). In addition to the 10 percent threshold, a banking organization could be subject to additional deductions for significant investments in financial institutions in the form of common stock, if the amount not deducted under the 10 percent limit, combined with mortgage servicing assets and deferred tax assets that are not deducted, exceed 15 percent of the banking organization’s common equity tier 1 capital. See 12 CFR 3.22(d) (OCC); 12 CFR 217.22(d) (Board); and 12 CFR 324.22(d) (FDIC).

<sup>30</sup> See 12 CFR 3.22(c)(5) (OCC); 12 CFR 217.22(c)(5) (Board); and 12 CFR 324.2(c)(5) (FDIC).

The proposal would have amended the capital rule to require an advanced approaches banking organization with an investment in a covered debt instrument issued by an unconsolidated financial institution to deduct the investment from tier 2 capital if the advanced approaches banking organization has a significant investment in the capital of the unconsolidated financial institution. The agencies received no comments on deductions for significant investments in the capital of an unconsolidated financial institution and are finalizing this aspect of the rule as proposed.

The proposal would have amended the capital rule to require an advanced approaches banking organization with an investment in a covered debt instrument in a financial institution in which the advanced approaches banking organization does not also have a significant investment in the form of common stock to include such investment in the covered debt instrument in the aggregate amount of non-significant investments in the capital of unconsolidated financial institutions. As under the existing capital rule, the proposal would have required an advanced approaches banking organization to deduct from regulatory capital the amount by which the aggregate amount of non-significant investments in the capital of unconsolidated financial institutions and such covered debt instruments exceeds the 10 percent threshold for non-significant investments. Any investment in a covered debt instrument subject to deduction would have been deducted according to the corresponding deduction approach described below in section V.F. Any investment in a covered debt instrument not subject to deduction would have been included in risk-weighted assets, generally with a 100 percent risk weight.

Some commenters suggested that the agencies recalibrate the 10 percent threshold for non-significant investments in consideration of the expanded scope of instruments that would be

included within that threshold under the proposal. For example, some commenters asked the agencies to expand the non-significant investments threshold to 10 percent of an advanced approaches banking organization's own total capital from 10 percent of its own common equity tier 1 capital. Changing the non-significant investments threshold in the manner the commenters suggested could undermine a main goal of the proposal—to reduce interconnectedness among large and internationally active banking organizations. Accordingly, the final rule requires an advanced approaches banking organization with an investment in a covered debt instrument in a financial institution in which the advanced approaches banking organization does not have a significant investment to include such investment in the aggregate amount of non-significant investments in the capital of unconsolidated financial institutions, as proposed. Further, the final rule requires an advanced approaches banking organization to deduct from regulatory capital the amount by which the aggregate amount of non-significant investments in the capital of unconsolidated financial institutions exceeds the 10 percent threshold for non-significant investments, as proposed.

The proposal would have included limited exclusions from the 10 percent threshold for non-significant investments' deduction approach. The exclusions would have depended on whether an advanced approaches banking organization is a U.S. GSIB or a subsidiary of a U.S. GSIB (U.S. GSIB banking organization). To help support a deep and liquid market for covered debt instruments, the proposal would have permitted U.S. GSIB banking organizations to exclude limited amounts of market making exposures (“excluded covered debt instruments”) from the 10 percent threshold for non-significant investments deduction. For example, a U.S. GSIB could have excluded covered debt instruments from the aggregate amount of non-significant investments in the capital of unconsolidated financial institutions. The aggregate

amount of the exclusion, measured on a gross long basis, was limited to five percent of the GSIB's own common equity tier 1 capital (market making exclusion). If the aggregate amount of excluded covered debt instruments were more than five percent of the common equity tier 1 capital, then the excess over five percent would have been subject to deduction from tier 2 capital on a gross long basis. In addition, if an excluded covered debt instrument were held for more than 30 business days or ceased to be held in connection with market making activities, then the excluded covered debt instrument would have been subject to deduction from tier 2 capital on a gross long basis. Finally, in order to dissuade regulatory arbitrage, the proposal would not have allowed U.S. GSIB banking organizations to subsequently move "excluded covered debt instruments" from the market making exclusion to the 10 percent threshold for non-significant investments.

Commenters stressed the importance of derivatives to market making activities in securities, particularly covered debt instruments issued by GSIBs. In market making transactions, U.S. GSIBs will often act as financial intermediaries between clients, transferring risks related to covered debt instruments. This risk transfer is often conducted through offsetting derivative transactions or directly buying and selling covered debt instruments. Commenters stated that this market making activity supports deep and liquid markets for covered debt instruments by allowing investors to reduce (or gain) exposure to covered debt instruments without actually selling (or buying) the securities. Derivatives are essential to such activities because they allow market makers to establish and hedge these exposures.

As such, these commenters asserted that the agencies should eliminate the proposed 30-business-day requirement because it would make the proposed market making exclusion

unavailable for many market making activities that support the depth and liquidity of the markets for TLAC-eligible debt, in particular synthetic exposures from derivatives used in market making activities. These commenters noted that bona fide market making activities, including derivative- and hedging-related activities, often involve holding exposures for longer than 30 business days. Commenters further indicated that the 30-business-day requirement would also create incentives for U.S. GSIB banking organizations to arbitrage the final rule by exiting and reestablishing hedge positions to avoid a mandatory deduction from tier 2 capital if the position is held for more than 30 business days. Commenters indicated that re-establishing hedge positions would result in costs to banking organizations and clients without reducing the risks associated with the transactions. Additionally, these commenters indicated that the vast majority of market making activity in covered debt instruments is in the form of derivative exposures. Therefore, retaining the 30-business-day requirement would arguably make the five percent exclusion inoperable for most market making activities in covered debt instruments. As an alternative to the proposed market making standard and the proposed 30-business-day requirement, commenters suggested the agencies use the regulatory framework implementing the Volcker Rule to identify which positions in covered debt instruments are held for market making purposes and eliminate the 30-business-day requirement. These commenters stated that this approach would promote effectiveness, simplicity, and efficiency in the regulation.

After considering commenters' suggestions to eliminate the proposed 30-business-day requirement for market making in covered debt instruments, the agencies have revised the proposal by removing the 30-business-day requirement for market making in the form of



“synthetic exposures” as defined in the agencies’ capital rule.<sup>31</sup> Synthetic market making exposures, such as derivatives, may frequently be held for more than 30 business days. Removing the 30-business-day requirement for synthetic exposures would, relative to the proposal, better align with the proposal’s goal of supporting deep and liquid markets for covered debt instruments by allowing synthetic exposures arising from market making activities to be included in the market making exclusion, subject to limits. As discussed, this exclusion is limited to five percent of common equity tier 1 capital, measured on a gross long basis. These limits are consistent with financial stability goals of avoiding asset fire sales in times of stress, encouraging risk-mitigating hedges, and reducing interconnectedness while still supporting deep and liquid markets for TLAC-eligible debt instruments. Accordingly, the final rule reflects this change. However, the agencies continue to believe that the 30-business-day requirement is an appropriate metric to identify market making positions in “direct” investments in covered debt instruments (i.e., holding the instrument on the banking organization’s balance sheet) and “indirect” investments in covered debt instruments (i.e., exposure to the instrument through investment funds).<sup>32</sup> Direct investments in covered debt instruments held in connection with market making should turn over regularly and the agencies seek to dis-incentivize long-term direct and indirect exposures to covered debt instruments, given the risk of write-down or conversion to equity of such instruments.

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<sup>31</sup> See 12 CFR 3.2 (OCC); 12 CFR 217.2 (Board); 12 CFR 324.2 (FDIC) (“synthetic exposure”).

<sup>32</sup> See 12 CFR 3.2 (OCC); 12 CFR 217.2 (Board); 12 CFR 324.2 (FDIC) (“investment in the capital of an unconsolidated financial institution” and “indirect exposure”).

Therefore, the final rule retains the 30-business-day requirement for “direct” and “indirect” investments in excluded covered debt instruments, but not for “synthetic” investments in excluded covered debt instruments. This change from the proposal should balance the goals of limiting interconnectedness among the largest and most internationally active banking organizations and promoting the liquidity of TLAC-eligible debt instruments. Additionally, the agencies clarify that there is no requirement under the final rule to assign investments in covered debt instruments held in connection with market making as “excluded covered debt instruments.” To the extent a U.S. GSIB banking organization has available capacity, all investments in covered debt instruments could be held on a net long basis as non-significant investments in the capital of an unconsolidated financial institution subject to the 10 percent threshold for non-significant investments.

After consideration of comments, the agencies also have revised the rule to use the Volcker Rule exemption for market making activities to identify covered debt instruments held for market making for purposes of qualifying for the final rule’s market making exclusion. Relative to the proposal, this change should decrease compliance burden by allowing banking organizations to use a single methodology for identifying market making activities, rather than two similar, but non-identical regulatory standards.

This approach would capture essentially the same set of exposures as the proposal’s standard. However, the final rule’s definition of “excluded covered debt instrument” differs

from the proposal by referring to the relevant provisions of each agency's rule implementing the market making exemption in the Volcker Rule.<sup>33</sup>

The proposal also included a simpler deduction approach for advanced approaches banking organizations that are not U.S. GSIB banking organizations given that these banking organizations pose less systemic risk than U.S. GSIBs. Unlike a U.S. GSIB, these banking organizations can include any non-significant investments in covered debt instruments of unconsolidated financial institutions in the five percent exclusion (i.e., use of the exclusion is not restricted to only those investments held in connection to market making activities). Any amount in excess of this five percent exclusion would be subject to the 10 percent threshold for non-significant investments deduction on a net long basis. The agencies did not receive comments on this provision of the proposal. Therefore, the final rule implements the five percent exclusion for advanced approaches banking organizations that are not U.S. GSIBs as proposed.

As noted above, an advanced approaches banking organization could exclude certain investments in covered debt instruments, as applicable, from the 10 percent threshold for non-significant investments calculation and potential deduction under section \_\_.22(c)(4) if the aggregate amount of covered debt instruments, measured by gross long position, were five percent or less of its common equity tier 1 capital. To achieve consistency with the *TLAC Holdings* standard and with the calculation of the 10 percent threshold for non-significant investments deduction, the agencies are modifying the calculation for determining the amount of

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<sup>33</sup> See 12 CFR 44.4 (OCC); 12 CFR 248.4 (Board); 12 CFR 351.4 (FDIC).

covered debt instruments that can be omitted from the 10 percent threshold for non-significant investments calculation. Under the final rule, an advanced approaches banking organization can omit covered debt instruments from the 10 percent threshold calculation and potential deduction under section \_\_.22(c)(4) if the aggregate amount of covered debt instruments, measured by gross long position, is five percent or less of the sum of the banking organization's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under section \_\_.22(a) through \_\_.22(c)(3), net of associated deferred tax liabilities (DTLs). This includes, for example, deductions related to goodwill, intangibles, and deferred tax assets, and adjustments related to accumulated net gains and losses on cash flow hedges. The agencies believe that to achieve consistency and clarity throughout the deduction framework, the amount of covered debt instruments that can be omitted from the 10 percent threshold for non-significant investments calculation should be computed using the same basis as the 10 percent threshold for non-significant investments calculation itself.

The agencies intend to monitor advanced approaches banking organizations' holdings of covered debt instruments in the form of synthetic exposures to ensure that the capital held for these positions is commensurate with risk and that such holdings do not raise safety and soundness concerns. Further, to better understand advanced approaches banking organizations' risk from exposures to the capital of unconsolidated financial institutions, the agencies may issue an information collection proposal to collect quarterly data on advanced approaches banking organizations' non-significant investments in the capital of unconsolidated financial institutions and excluded covered debt instruments, as applicable.

Some commenters disagreed with the proposal’s design of the exclusions for covered debt instruments, which measures positions on a gross long basis. These commenters suggested that the measurement of the exclusions for covered debt instruments be based on the “net long position,” in accordance with the agencies’ capital rule, which allows gross long positions to be offset against qualifying short positions.<sup>34</sup> The commenters noted that the 10 percent threshold for non-significant investments is based on the “net long position” and suggested that the exclusions for covered debt instrument be consistent with that standard. Further, commenters stated that finalizing the exclusions for covered debt instruments based on a net long position measurement basis would allow advanced approaches banking organizations to better support the depth and liquidity of market making in TLAC-eligible debt instruments, because market making activities are typically well hedged and a “net long position” would allow more positions to qualify for the exclusions.

The final rule maintains measurement of the exclusions for covered debt instruments based on the gross long position. Moving to a “net long position” measurement could undermine the agencies’ goal of reducing interconnectedness among large and internationally active banking organizations as it would allow such banking organizations to accumulate exposure to covered debt instruments significantly beyond the threshold envisioned in the proposal. Further, advanced approaches banking organizations are able to assign hedged covered debt instrument exposures to the 10 percent threshold for non-significant investments on a net long basis. The optional exclusions remain available to support market making activities such as accumulating

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<sup>34</sup> See 12 CFR 3.22(h) (OCC); 12 CFR 217.22(h) (Board); 12 CFR 324.22(h) (FDIC).

short term cash positions to meet customer demand and to acquire additional long positions in covered debt instruments to facilitate market stabilization during times of stress. Such an approach is consistent with financial stability goals of avoiding asset fire sales in times of stress, encouraging risk-mitigating hedges, and reducing interconnectedness while still supporting deep and liquid markets for TLAC-eligible debt instruments.

#### **F. Corresponding Deduction Approach**

Under the corresponding deduction approach, a banking organization must apply any required deduction to the component of capital for which the underlying instrument would qualify if it were issued by the banking organization.<sup>35</sup> If the banking organization does not have enough of the component of capital to fully effect the deduction, the corresponding deduction approach provides that any amount of the investment that has not already been deducted would be deducted from the next, more subordinated component of capital.<sup>36</sup> If, for example, a banking organization has insufficient amounts of tier 2 capital and additional tier 1 capital to effect a required deduction, the banking organization would need to deduct from common equity tier 1 capital the amount of the investment that exceeds the tier 2 and additional tier 1 capital of the banking organization.<sup>37</sup> The proposal would have amended the corresponding deduction approach in section \_\_.22(c)(2) of the capital rule to specify that an investment in a covered debt

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<sup>35</sup> See 12 CFR 3.22(c)(2) (OCC); 12 CFR 217.22(c)(2) (Board); and 12 CFR 324.22(c)(2) (FDIC).

<sup>36</sup> See 12 CFR 3.22(c)(2) and (f) (OCC); 12 CFR 217.22(c)(2) and (f) (Board); and 12 CFR 324.22(c)(2) and (f) (FDIC).

<sup>37</sup> See 12 CFR 3.22(f) (OCC); 12 CFR 217.22(f) (Board); and 12 CFR 324.22(f) (FDIC).

instrument by an advanced approaches banking organization would have been subject to the corresponding deduction approach, with the covered debt instrument treated as a tier 2 capital instrument. Some commenters disagreed with this approach and, instead, asked the agencies to treat investments in covered debt instruments as a common equity tier 1 capital instrument or, as applicable, allow deductions under the corresponding deduction approach from own TLAC-eligible debt instruments.

As stated earlier, requiring a deduction of a covered debt instrument from tier 2 capital should serve as a sufficiently prudent and simple approach that dis-incentivizes advanced approaches banking organizations' investments in such instruments and thereby supports the objectives of reducing both interconnectedness within the financial system and systemic risk. Accordingly, the agencies are finalizing the proposal's amendments to the corresponding deduction approach in section \_\_.22(c)(2) of the capital rule

#### **G. Net Long Position Calculation**

The proposal would have followed the same general approach as currently provided under the agencies' capital rule regarding the calculation of the amount of any deduction and the treatment of guarantees and indirect investments for purposes of the deductions. Under the capital rule, the amount of a banking organization's investment in its own capital instrument or in the capital of an unconsolidated financial institution subject to deduction is the banking organization's net long position in the capital instrument as calculated under section \_\_.22(h) of the capital rule. Under section \_\_.22(h), a banking organization may net certain qualifying short positions in a capital instrument against a gross long position in the same instrument to determine the net long position.

The proposal would have modified section \_\_.22(h) of the capital rule such that an advanced approaches banking organization would determine its net long position in an exposure to its own covered debt instrument, as applicable, or in a covered debt instrument issued by an unconsolidated financial institution in the same manner as currently provided for investments in an institution’s own capital instruments or investments in the capital of an unconsolidated financial institution, respectively. Consistent with the capital rule, the calculation of a net long position under the proposal would have taken into account direct investments in covered debt instruments as well as indirect exposures to covered debt instruments held through investment funds.

A banking organization has three options under the capital rule to measure its gross long position in a capital instrument held indirectly through an investment fund.<sup>38</sup> The proposal would have amended section \_\_.22(h)(2)(iii) of the capital rule to provide the same three options to determine the gross long position in a covered debt instrument held through an investment fund. The agencies received no comments on this aspect of the proposal and the final rule adopts the changes as proposed.

The agencies’ capital rule sets qualifying criteria for recognizing short positions that can be netted against gross long positions; specifically, a short position must be in the “same instrument” as the gross long position and must meet minimum maturity requirements, among

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<sup>38</sup> See 12 CFR 3.22(h)(2)(iii) (OCC); 12 CFR 217.12(h)(2)(iii) (Board); and 12 CFR 324.22(h)(2)(iii) (FDIC).



other requirements.<sup>39</sup> The proposal would not have changed these operational criteria for recognizing short positions in the calculation of a net long position. Some commenters advocated for changes to the capital rule’s requirements for recognizing a short position under section \_\_.22(h)(3). These commenters argued that the capital rule should be modified to not require short positions to be in the “same instrument” as the gross long position when calculating the net long position. Instead, commenters recommended that the final rule allow recognized short positions to be in any instrument that is *pari passu* or subordinated to the gross long position’s instrument. These commenters recommended that this change should also apply to calculating the net long position of investments in covered debt instruments in the final rule.

The agencies have consistently maintained that recognition of short positions under the net long position calculation are required to be in the “same instrument” as a matter of prudent risk management and hedging practices. To recognize short positions in other than the “same instrument” would potentially undermine the effectiveness of risk mitigating hedges. Accordingly, the final rule adopts the calculation of the net long position as proposed.

Under the proposal, for purposes of any deduction required for an advanced approaches banking organization’s investment in the capital of an unconsolidated financial institution, the amount of a covered debt instrument would have included any contractual obligations the advanced approaches banking organization has to purchase such covered debt instruments. The

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<sup>39</sup> See 12 CFR 3.22(h)(3) (OCC); 12 CFR 217.12(h)(3) (Board); and 12 CFR 324.22(h)(3) (FDIC).

agencies received no comment on this aspect of the proposal, and the final rule adopts this change as proposed.

## **VI. *Technical Amendment and Other Comments***

The agencies proposed amending the definition of “investment in the capital of an unconsolidated financial institution” in section \_\_.2 of the capital rule to correct a drafting error in that definition. The agencies did not receive any comment with regard to the proposed technical amendment. However, in the period between the issuance of the proposal and this final rule, this technical amendment was implemented by the agencies’ final rule to simplify the capital rule.<sup>40</sup>

A few commenters suggested that the proposal should go further in limiting the exposure of advanced approaches banking organizations to GSIBs, given their size and the risk their failure could pose to the financial system. These commenters argued that the final rule should ensure that the cost of TLAC debt better reflect heightened risks of GSIBs and that the agencies should require U.S. GSIBs to hold more common equity tier 1 capital. Other commenters suggested that the agencies consider existing elements of the regulatory framework – such as the single counterparty credit limit and the GSIB surcharge - when finalizing the deduction framework.

Under the capital rule, each agency has the authority to require a banking organization to hold additional capital based on the banking organization’s risk profile.<sup>41</sup> Similarly, while other

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<sup>40</sup> See 84 FR 35234 (July 22, 2019).

<sup>41</sup> See 12 CFR 3.1(d)(1) (OCC); 12 CFR 217.1(d)(1) (Board); 12 CFR 324.1(d)(1) (FDIC).

elements of the regulatory framework address the systemic risk of large, internationally active banking organizations or concentrations of exposures to counterparties, no existing regulation specifically address the risks associated with investments in TLAC-eligible debt instruments. The agencies, therefore, are finalizing the proposal to establish a regulatory capital treatment for investments in covered debt instruments with certain modifications, as previously described.

The proposal did not contemplate providing a transition period for implementation of the final rule by advanced approaches banking organizations. Some commenters requested that the agencies provide banking organizations with a transition period to ease compliance burden. Specifically, commenters requested that the agencies provide 18 months before banking organizations must effectuate the deduction treatment. These commenters asserted that a transition period would give banking organizations more time to build out systems to track which instruments are covered debt instruments and therefore subject to the deduction framework. A commenter requested that the agencies not require deduction of any unsecured debt instrument issued by a GSIB until the information necessary to determine whether the instrument is a covered debt instrument is available.

The agencies maintain the supervisory expectation that large and internationally active banking organizations should be deeply knowledgeable of the securities exposures on their own balance sheets, if only for the purposes of prudent risk management. The final rule will become effective on April 1, 2021. The agencies believe this effective date provides sufficient time for advanced approaches banking organizations to evaluate investments in covered debt instruments and apply the final rule's deduction treatment.

In addition to the above, the agencies are making certain technical amendments to section \_\_.10 of the capital rule to more clearly differentiate between requirements applicable to advanced approaches banking organizations and those applicable to Category III banking organizations. In section \_\_.10 of the capital rule, as amended by the recent interagency tailoring rule,<sup>42</sup> paragraphs (c)(1)-(3) describe the capital ratio calculations applicable to advanced approaches banking organizations, whereas paragraph 10(c)(4) of the capital rule describes the supplementary leverage ratio calculations applicable to both advanced approaches banking organizations and Category III banking organizations. To avoid confusion, the agencies are amending section \_\_.10 of the capital rule such that paragraph (c) will provide only the supplementary leverage ratio requirements. The advanced approaches capital calculations will be moved to revised paragraph (d) of section \_\_.10 of the capital rule. Current paragraph (d), *Capital adequacy*, will be re-designated as paragraph (e) of section \_\_.10 of the capital rule. The agencies are also amending language in sections \_\_.2 and \_\_.121 of the capital rule to correct cross-references in light of the amendments described above. These technical amendments do not amend any substantive requirements applicable to banking organizations.

## **VII. *Amendments to the Board's TLAC Rule***

In 2018, the Board issued a notice of proposed rulemaking that, among other items, included minor proposed amendments to the Board's TLAC rule.<sup>43</sup> The proposal included revisions to ensure that the external TLAC risk-weighted buffer level, TLAC leverage buffer

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<sup>42</sup> 84 FR 59230 (November 1, 2019).

<sup>43</sup> 83 FR 17317, 17322 (April 19, 2018).

level, and the TLAC buffer level for covered IHCs would be amended to use the same haircuts applicable to LTD instruments that are currently used to calculate outstanding minimum required TLAC amounts, which do not include a 50 percent haircut on LTD instruments with a remaining maturity of between one and two years. Another proposed amendment was to ensure that the term “external TLAC risk-weighted buffer” is used consistently in the TLAC rule. The proposal also would have provided that a new covered IHC would always have three years to conform to most of the requirements of the TLAC rule, and to align the articulation of the methodology for calculating the covered IHC’s LTD instrument amount with the same methodology used for GSIBs.

The Board received minimal comments on these proposed revisions to the TLAC rule within the comments received on its proposal overall and the comments received were supportive of the specific proposed revisions. As a result, the Board is issuing these revisions in the final rule without change from the proposal.

## **VIII. *Changes to Regulatory Reporting***

### **A. Deductions from Tier 2 Capital Related to Investments in Covered Debt**

#### **Instruments and Excluded Covered Debt Instruments**

In the April 2019 rulemaking, the Board proposed to modify the instructions to the Consolidated Financial Statements for Holding Companies (FR Y-9C), Schedule HC-R, Part I and Part II, to effectuate the deductions from regulatory capital for Board-regulated advanced approaches banking organizations related to investments in covered debt instruments and excluded covered debt instruments as described in the proposal.

Specifically, the Board would have modified the instructions of the FR Y-9C for Schedule HC-R, Part I, item 33, “Tier 2 capital deductions.” On the FR Y-9C, a covered BHC would have been required to deduct from tier 2 capital the aggregate amount of its investments in covered debt instruments that, when combined with the banking organization’s other non-significant investments in the capital of unconsolidated financial institutions, exceed 10 percent of the common equity tier 1 capital of the banking organization. Also, if an excluded covered debt instrument were held by a covered BHC for more than 30 business days, or no longer held in connection with market making-related activities, the excluded covered debt instrument would have been deducted from tier 2 capital.

In addition, for purposes of the deduction requirements related to non-significant investments in the capital of unconsolidated financial institutions, Board-regulated advanced approaches banking organizations that are not covered BHCs would have been required to deduct from tier 2 capital those investments in covered debt instruments that exceed five percent of common equity tier 1 capital, and that also, when combined with the banking organization’s other non-significant investments in unconsolidated financial institutions, exceed 10 percent of the common equity tier 1 capital of the banking organization. The Board also would have modified the instructions for calculating other deduction-related and risk-weighted asset line items to incorporate investments in covered debt instruments and excluded covered debt instruments, as applicable, by Board-regulated advanced approaches banking organizations.

In October 2019, the Federal Financial Institutions Examination Council (FFIEC) separately proposed to modify the Consolidated Reports of Condition and Income for a Bank with Domestic and Foreign Offices (FFIEC 031), Consolidated Reports of Condition and Income

for a Bank with Domestic Offices Only (FFIEC 041) (collectively with the FFIEC 031, the Call Report<sup>44</sup>), and Regulatory Capital Reporting for Institutions Subject to the Advanced Capital Adequacy Framework (FFIEC 101) in a manner consistent with the changes described above to the FR Y-9C to effectuate the proposal's deduction approach for investments in covered debt instruments and excluded covered debt instruments, as applicable.<sup>45</sup>

In March 2020, the Board separately proposed conforming changes to the FR Y-14 to effectuate the proposed deduction framework for investments in covered debt instruments.<sup>46</sup>

With respect to the FR Y-9C proposed changes, one commenter requested clarification on the sequencing of reporting changes related to effectuating deductions for covered debt instruments and the effective date of the final rule. Specifically, this commenter requested that the effective date of the final rule should precede any requirement to begin effectuating deductions related to investments in covered debt instruments on regulatory reports. The agencies confirm that the effective date of the final rule will precede any reporting requirements related to implementing the deduction framework for covered debt instruments. The Board received no comments on the FR Y-14 proposed changes.

As described above, reporting changes to effectuate the deduction framework for investments in covered debt instruments described in the proposal were proposed separately for

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<sup>44</sup> The proposed modifications would not affect the Consolidated Reports of Condition and Income for a Bank with Domestic Offices Only and Total Assets Less than \$1 Billion (FFIEC 051) because banks and savings associations that are advanced approaches banking organizations are not eligible to file the FFIEC 051 report.

<sup>45</sup> See 84 FR 53227 (October 4, 2019).

<sup>46</sup> See 85 FR 15776 (March 19, 2020).

the (1) FR Y-9C, (2) FFIEC 101 and Call Report, and (3) FR Y-14. The Board is finalizing as proposed, changes to the FR Y-9C and FR Y-14, to effectuate the deduction framework for investments in covered debt instruments in this Federal Register notice. The agencies will address comments submitted in connection with the FFIEC's October 2019 proposal when those forms and instructions are finalized in a separate Federal Register notice, consistent with the final rule.

### **B. Public Disclosure of Long-term Debt and TLAC by Covered BHCs and Covered IHCs**

In the April 2019 rulemaking, the Board also proposed to modify Schedule HC-R, Part I of the FR Y-9C by adding new data items that would publicly disclose: (1) the long-term debt and TLAC for covered BHCs and covered IHCs; (2) these banking organizations' long-term debt and TLAC ratios to ensure compliance with the TLAC rule; (3) TLAC buffers; and (4) amendments to the instructions for the calculation of eligible retained income (item 47), institution-specific capital buffer (items 46.a and 46.b), and distributions and discretionary bonus payments (item 48) for covered BHCs and covered IHCs.<sup>47</sup> Commenters suggested that the Board clarify in the final rule when changes to FR Y-9C related to long-term debt and TLAC reporting disclosures will become effective. Reporting changes for deductions related to

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<sup>47</sup> See 84 FR 13823–13824 (April 8, 2019).



investments in covered debt instruments on the FR Y-9C will not go into effect until after the final rule's effective date.

In March 2020, the Board separately proposed conforming changes to the FR Y-14 to disclose new items related to long-term debt and TLAC, as described above.<sup>48</sup>

In response to the proposal, commenters requested that the Board clarify how U.S. GSIBs are to calculate the TLAC rule's leverage ratios on the FR Y-9C report. More specifically, commenters suggested the Board clarify that U.S. GSIBs should not be required to report long-term debt and TLAC leverage ratios based on total assets because U.S. GSIBs' applicable long-term debt and TLAC leverage requirement is based on the denominator for the supplementary leverage ratio. Commenters noted that only covered IHCs are required to report the long-term debt and TLAC leverage ratios based on total assets. The Board confirms that reporting of the long-term debt and TLAC leverage requirement for U.S. GSIBs will only be based upon the supplementary leverage ratio denominator, consistent with the TLAC rule's leverage requirement. The Board received no comments on the FR Y-14 proposed changes.

The Board is finalizing the proposed changes to the FR Y-9C and FR Y-14 to require covered BHCs and covered IHCs to report their long-term debt and TLAC resources, with modifications in response to comment as described above, in this Federal Register notice.

Some commenters suggested the Board develop a more robust disclosure regime related to TLAC so that the level of risk is appropriately priced into these instruments. They stated that

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<sup>48</sup> See 85 FR 15776 (March 19, 2020).

disclosures will incentivize GSIBs to meet their TLAC requirements with equity rather than debt instruments. Commenters offered suggestions for improving disclosures by noting that the agencies should collaborate with the Securities and Exchange Commission to require plain-language warnings regarding risk of bail-in to investors (1) when purchasing a TLAC instrument in their brokerage account and (2) in offering materials published by pension and mutual funds that invest in TLAC instruments. The Board does not have the authority to change disclosures required by the Securities and Exchange Commission related to securities issuances or sales to retail investors. The interagency statement on retail sales of nondeposit investments products should ensure certain disclosures for retail sales programs involving mutual funds, annuities and other nondeposit investment products.<sup>49</sup> Further, the Board does not have the authority to mandate disclosures by pension or mutual funds. The final rule does not incorporate these suggestions.

## **IX. *Regulatory Analyses***

### **A. Paperwork Reduction Act**

Certain provisions of the final rule contain “collection of information” within the meaning of the Paperwork Reduction Act of 1995 (PRA).<sup>50</sup> In accordance with the requirements of the PRA, the agencies may not conduct or sponsor, and the respondent is not required to

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<sup>49</sup> See “Interagency Statement on Retail Sales of Nondeposit Investment Products.” OCC Bulletin 1994-13 (OCC); SR 94-11 (FIS) (Board); and FIL-9-94 (FDIC).

<sup>50</sup> 44 U.S.C. 3501-3521.

respond to, an information collection unless it displays a currently-valid Office of Management and Budget (OMB) control number.

The final rule revises section \_\_.22(c), (f), and (h) of the capital rule to incorporate the proposed deduction approach for investments in covered debt instruments. Several new definitions are added to section \_\_.2 to effectuate these deductions.

Each agency has an information collection related to its regulatory capital rules. The OMB control number for the OCC is 1557-0318, Board is 7100-0313, and FDIC is 3064-0153. The final rule will not, however, result in changes to burden under these information collections and therefore no submissions will be made under section 3507(d) of the PRA (44 U.S.C. 3507(d)) and section 1320.11 of the OMB's implementing regulations (5 CFR 1320) for each of the agencies' regulatory capital rules.

In addition, the final rule requires changes to the Call Reports (OMB No. 1557-0081 (OCC), 7100-0036 (Board), and 3064-0052 (FDIC)), and the FFIEC 101 (OMB No. 1557-0239 (OCC), 7100-0319 (Board), and 3064-0159 (FDIC)), which will be addressed in one or more separate Federal Register notices.

The final rule requires changes to the Consolidated Financial Statements for Holding Companies (FR Y-9C; OMB No. 7100-0128) and the Capital Assessments and Stress Testing Reports (FR Y-14A/Q/M; OMB No. 7100-0341). The Board reviewed the final rule under the authority delegated to the Board by OMB.

*Revised Collection (Board only)*

*Title of Information Collection:* Consolidated Financial Statements for Holding Companies.

*Agency form number:* FR Y-9C, FR Y-9LP, FR Y-9SP, FR Y-9ES, and FR Y-9CS.

*OMB control number:* 7100-0128.

*Effective date:* June 30, 2021

*Frequency:* Quarterly, semiannually, and annually.

*Affected Public:* Businesses or other for-profit.

*Respondents:* Bank holding companies (BHCs), savings and loan holding companies (SLHCs), securities holding companies (SHCs), and U.S. Intermediate Holding Companies (IHCs) (collectively, holding companies (HCs)).

*Estimated number of respondents:*

FR Y-9C (non-advanced approaches (AA) HCs community bank leverage ratio (CBLR)) with less than \$5 billion in total assets – 71,

FR Y-9C (non AA HCs CBLR) with \$5 billion or more in total assets – 35,

FR Y-9C (non AA HCs non-CBLR) with less than \$5 billion in total assets – 84,

FR Y-9C (non AA HCs non-CBLR) with \$5 billion or more in total assets – 154,

FR Y-9C (AA HCs) – 19,

FR Y-9LP – 434,

FR Y-9SP – 3,960,

FR Y-9ES – 83,

FR Y-9CS – 236.

*Estimated average hours per response:*

## **Reporting**

FR Y-9C (non AA HCs CBLR) with less than \$5 billion in total assets – 29.17,  
FR Y-9C (non AA HCs CBLR) with \$5 billion or more in total assets – 35.14,  
FR Y-9C (non AA HCs non-CBLR) with less than \$5 billion in total assets – 41.01,  
FR Y-9C (non AA HCs non-CBLR) with \$5 billion or more in total assets – 46.98,  
FR Y-9C (AA HCs) – 49.30,  
FR Y-9LP – 5.27,  
FR Y-9SP – 5.40,  
FR Y-9ES – 0.50,  
FR Y-9CS – 0.50.

### **Recordkeeping**

FR Y-9C (non-advanced approaches HCs with less than \$5 billion in total assets), FR Y-9C (non-advanced approaches HCs with \$5 billion or more in total assets), FR Y-9C (advanced approaches HCs), and FR Y-9LP: 1.00 hour; FR Y-9SP, FR Y-9ES, and FR Y-9CS: 0.50 hours.

*Estimated annual burden hours:*

### **Reporting**

FR Y-9C (non AA HCs CBLR) with less than \$5 billion in total assets – 8,284,  
FR Y-9C (non AA HCs CBLR) with \$5 billion or more in total assets – 4,920,  
FR Y-9C (non AA HCs non-CBLR) with less than \$5 billion in total assets – 13,779,  
FR Y-9C (non AA HCs non-CBLR) with \$5 billion or more in total assets – 28,940,  
FR Y-9C (AA HCs) – 3,747,  
FR Y-9LP – 9,149,  
FR Y-9SP – 42,768,

FR Y-9ES – 42,  
FR Y-9CS – 472.

### **Recordkeeping**

FR Y-9C – 1,452,  
FR Y-9LP – 1,736,  
FR Y-9SP – 3,960,  
FR Y-9ES – 42,  
FR Y-9CS – 472.

*General description of report:* The FR Y-9 family of reporting forms continues to be the primary source of financial data on holding companies (HCs) on which examiners rely between on-site inspections. Financial data from these reporting forms is used to detect emerging financial problems, review performance, conduct pre-inspection analysis, monitor and evaluate capital adequacy, evaluate HC mergers and acquisitions, and analyze an HC's overall financial condition to ensure the safety and soundness of its operations. The FR Y-9C serves as the standardized financial statements for certain consolidated holding companies. The Board requires HCs to provide standardized financial statements to fulfill the Board's statutory obligation to supervise these organizations. HCs file the FR Y-9C on a quarterly basis.

*Legal authorization and confidentiality:* The reporting and recordkeeping requirements associated with the FR Y-9 series of reports are authorized for BHCs pursuant to section 5 of the Bank Holding Company Act ("BHC Act"); for SLHCs pursuant to section 10(b)(2) and (3) of the Home Owners' Loan Act, 12 U.S.C. 1467a(b)(2) and (3), as amended by sections 369(8) and 604(h)(2) of the Dodd-Frank Wall Street and Consumer Protection Act ("Dodd-Frank Act"); for

IHCs pursuant to section 5 of the BHC Act, as well as pursuant to sections 102(a)(1) and 165 of the Dodd-Frank Act; and for securities holding companies pursuant to section 618 of the Dodd-Frank Act. Except for the FR Y-9CS report, which is expected to be collected on a voluntary basis, the obligation to submit the remaining reports in the FR Y-9 series of reports and to comply with the recordkeeping requirements set forth in the respective instructions to each of the other reports, is mandatory.

With respect to the FR Y-9C report, Schedule HI's Memoranda item 7(g) "FDIC deposit insurance assessments," Schedule HC-P's item 7(a) "Representation and warranty reserves for 1-4 family residential mortgage loans sold to U.S. government agencies and government sponsored agencies," and Schedule HC-P's item 7(b) "Representation and warranty reserves for 1-4 family residential mortgage loans sold to other parties" are considered confidential commercial and financial information. Such treatment is appropriate under exemption 4 of the Freedom of Information Act ("FOIA"), because these data items reflect commercial and financial information that is both customarily and actually treated as private by the submitter, and which the Board has previously assured submitters will be treated as confidential. It also appears that disclosing these data items may reveal confidential examination and supervisory information, and in such instances, the information also would be withheld pursuant to exemption 8 of the FOIA, which protects information related to the supervision or examination of a regulated financial institution.

In addition, for both the FR Y-9C report and the FR Y-9SP report, Schedule HC's Memoranda item 2.b., the name and email address of the external auditing firm's engagement partner, is considered confidential commercial information and protected by exemption 4 of the

FOIA, if the identity of the engagement partner is treated as private information by HCs. The Board has assured respondents that this information will be treated as confidential since the collection of this data item was proposed in 2004.

Additionally, items on the FR Y-9C, Schedule HC-C for loans modified under Section 4013, data items Memorandum items 16.a, “Number of Section 4013 loans outstanding”; and Memorandum items 16.b, “Outstanding balance of Section 4013 loans” are considered confidential. While the Board generally makes institution-level FR Y-9C report data publicly available, the Board is collecting Section 4013 loan information as part of condition reports for the impacted HCs and the Board considers disclosure of these items at the HC level would not be in the public interest. Such information is permitted to be collected on a confidential basis, consistent with 5 U.S.C. 552(b)(8). In addition, holding companies may be reluctant to offer modifications under Section 4013 if information on these modifications made by each holding company is publicly available, as analysts, investors, and other users of public FR Y-9C report information may penalize an institution for using the relief provided by the CARES Act. The Board may disclose Section 4013 loan data on an aggregated basis, consistent with confidentiality or as otherwise required by law.

Aside from the data items described above, the remaining data items collected on the FR Y-9C report and the FR Y-9SP report are generally not accorded confidential treatment. The data items collected on FR Y-9LP, FR Y-9ES, and FR Y-9CS reports, are also generally not accorded confidential treatment. As provided in the Board’s Rules Regarding Availability of Information, however, a respondent may request confidential treatment for any data items the respondent believes should be withheld pursuant to a FOIA exemption. The Board will review



any such request to determine if confidential treatment is appropriate, and will inform the respondent if the request for confidential treatment has been granted or denied.

To the extent the instructions to the FR Y-9C, FR Y-9LP, FR Y-9SP, and FR Y-9ES reports each respectively direct the financial institution to retain the workpapers and related materials used in preparation of each report, such material would only be obtained by the Board as part of the examination or supervision of the financial institution. Accordingly, such information is considered confidential pursuant to exemption 8 of the FOIA. In addition, the workpapers and related materials may also be protected by exemption 4 of the FOIA, to the extent such financial information is treated as confidential by the respondent.

*Current Actions:* As discussed in detail in section VIII above, several comments were received on the proposed changes to the FR Y-9C. Commenters requested that the effective date of the final rule precede proposed changes to regulatory reports. The agencies confirmed that the final rule will be effective before changes are implemented to regulatory reports. The final rule is effective April 1, 2021, and the changes to the FR Y-9C are effective June 30, 2021. Also, commenters requested that the Board clarify that U.S. GSIBs will report long-term debt and TLAC leverage requirements based upon the supplementary leverage ratio denominator. The Board agreed and clarified this requirement. Finally, some commenters suggested that the Board develop a more robust disclosure regime related to TLAC, including collaborating with the SEC. The Board did not accept this comment for the reasons noted above. Some of the item numbers below have changed since the proposed rule due to other FR Y-9C reporting changes to Schedule HC-R that have been implemented since that time.

To implement the reporting requirements of the final rule, the Board revises the FR Y-9C, Schedule HC-R, Part I, Regulatory Capital Components and Ratios, to amend instructions for line items 11, 17, 24, and 43 to effectuate the deductions from regulatory capital for advanced approaches holding companies related to investments in covered debt instruments and excluded covered debt instruments as described above. Further, the Board proposes to revise the FR Y-9C, Schedule HC-R, Part II, Risk-Weighted Assets, to amend instructions for line items 2(a), 2(b), 7, and 8 to incorporate investments in covered debt instruments and excluded debt instruments, as applicable, by advanced approaches holding companies in their calculation of risk-weighted assets.

In addition, the Board revises the FR Y-9C, Schedule HC-R, Part I, Regulatory Capital Components and Ratios, to create new line items and instructions to allow the BHCs of U.S. GSIBs and the IHCs of foreign GSIBs to publicly report their long-term debt (LTD) and total loss absorbing capacity (TLAC) in accordance, respectively, with 12 CFR 252, Subpart G and 12 CFR 252, Subpart P. Specifically, new line items are created to report, as applicable, BHCs of U.S. GSIBs' and IHCs of foreign GSIBs' (1.) outstanding eligible LTD (item 50); (2.) TLAC (item 51); (3.) LTD standardized risk-weighted asset ratio (item 52, column A); (4.) TLAC standardized risk-weighted asset ratio (item 52, column B); (5.) LTD advanced approaches risk-weighted asset ratio (item 53, column A); (6.) TLAC advanced approaches risk-weighted asset ratio (item 53, column B); (7.) *IHCs of foreign GSIBs only*: LTD leverage ratio (item 54, column A); (8.) *IHCs of foreign GSIBs only*: TLAC leverage ratio (item 54, column B); (9.) LTD supplementary leverage ratio (item 55, column A); (10.) TLAC supplementary leverage ratio (item 55, column B); (11.) institution-specific TLAC risk-weighted asset buffer necessary to avoid limitations on distributions and discretionary bonus payments (item 57(a)); and (12.)

TLAC leverage buffer necessary to avoid limitations on distributions and discretionary bonus payments (item 57(b)). Existing line items 50(a), 50(b), 51, 52, and 53 are re-numbered to 56(a), 56(b), 58, 59, and 60, respectively, and instructions' references updated, to account for the proposed inclusion of the new data collection items described above. Finally, the instructions for re-numbered line item 59, "Distributions and discretionary bonus payments during the quarter," are amended for the BHCs of U.S. GSIBs and the IHCs of foreign GSIBs to reflect maximum payout amounts that take into account a firm's TLAC risk-weighted and leverage buffers reported in line items 57(a) and 57(b), respectively. The final reporting forms and instructions will become available in the near future on the Board's public website at <https://www.federalreserve.gov/apps/reportforms/review.aspx>.

*Revised Collection (Board only)*

*Title of Information Collection:* Capital Assessments and Stress Testing Reports.

*Agency form number:* FR Y-14A/Q/M.

*OMB control number:* 7100-0341.

*Effective date:* June 30, 2021.

*Frequency:* Annually, quarterly, and monthly.

*Respondents:* These collections of information are applicable to bank holding companies (BHCs), U.S. intermediate holding companies (IHCs), and savings and loan holding companies

(SLHCs)<sup>51</sup> with \$100 billion or more in total consolidated assets, as based on: (i) The average of the firm's total consolidated assets in the four most recent quarters as reported quarterly on the firm's Consolidated Financial Statements for Holding Companies (FR Y-9C; OMB No. 7100-0128); or (ii) if the firm has not filed an FR Y-9C for each of the most recent four quarters, then the average of the firm's total consolidated assets in the most recent consecutive quarters as reported quarterly on the firm's FR Y-9Cs. Reporting is required as of the first day of the quarter immediately following the quarter in which the respondent meets this asset threshold, unless otherwise directed by the Board.

*Estimated number of respondents:* FR Y-14A/Q: 36; FR Y-14M: 34.<sup>52</sup>

*Estimated average hours per response:* FR Y-14A: 929 hours; FR Y-14Q: 2,201 hours; FR Y-14M: 1,072 hours

*On-going Automation Revisions:* 480 hours; FR Y-14 Attestation On-going Attestation: 2,560 hours.

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<sup>51</sup> SLHCs with \$100 billion or more in total consolidated assets became members of the FR Y-14Q and FR Y-14M panels effective June 30, 2020, and will join the FR Y-14A panel effective December 31, 2020. *See* 84 FR 59032 (November 1, 2019).

<sup>52</sup> The estimated number of respondents for the FR Y-14M is lower than for the FR Y-14Q and FR Y-14A because, in recent years, certain respondents to the FR Y-14A and FR Y-14Q have not met the materiality thresholds to report the FR Y-14M due to their lack of mortgage and credit activities. The Board expects this situation to continue for the foreseeable future.

*Estimated annual burden hours:* FR Y–14A: 33,444 hours; FR Y–14Q: 316,944 hours; FR Y–14M: 437,376 hours; FR Y–14 On-going Automation Revisions: 17,280 hours; FR Y–14 Attestation On-going Attestation: 33,280 hours.

*General description of report:* This family of information collections is composed of the following three reports:

- The FR Y–14A collects quantitative projections of balance sheet, income, losses, and capital across a range of macroeconomic scenarios and qualitative information on methodologies used to develop internal projections of capital across scenarios.<sup>53</sup>
- The quarterly FR Y–14Q collects granular data on various asset classes, including loans, securities, trading assets, and PPNR for the reporting period.
- The monthly FR Y–14M is comprised of three retail portfolio- and loan-level schedules, and one detailed address-matching schedule to supplement two of the portfolio and loan-level schedules.

The data collected through the FR Y– 14A/Q/M reports provide the Board with the information needed to help ensure that large firms have strong, firm-wide risk measurement and

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<sup>53</sup> On October 10, 2019, the Board issued a final rule that eliminated the requirement for firms subject to Category IV standards to conduct and publicly disclose the results of a company-run stress test. *See* 84 FR 59032 (Nov. 1, 2019). That final rule maintained the existing FR Y–14 substantive reporting requirements for these firms in order to provide the Board with the data it needs to conduct supervisory stress testing and inform the Board’s ongoing monitoring and supervision of its supervised firms. However, as noted in the final rule, the Board intends to provide greater flexibility to banking organizations subject to Category IV standards in developing their annual capital plans and consider further change to the FR Y–14 forms as part of a separate proposal. *See* 84 FR 59032, 59063.

management processes supporting their internal assessments of capital adequacy and that their capital resources are sufficient given their business focus, activities, and resulting risk exposures. The reports are used to support the Board’s annual Comprehensive Capital Analysis and Review (CCAR) and Dodd Frank Act Stress Test (DFAST) exercises, which complement other Board supervisory efforts aimed at enhancing the continued viability of large firms, including continuous monitoring of firms’ planning and management of liquidity and funding resources, as well as regular assessments of credit, market and operational risks, and associated risk management practices. Information gathered in this data collection is also used in the supervision and regulation of respondent financial institutions. Respondent firms are currently required to complete and submit up to 17 filings each year: one annual FR Y–14A filing, four quarterly FR Y–14Q filings, and 12 monthly FR Y–14M filings. Compliance with the information collection is mandatory.

*Current actions:* On March 19, 2020, the Board proposed to revise the FR Y-14 reports to collect TLAC and LTD information.<sup>54</sup> The Board did not receive any comments on the proposed TLAC and LTD revisions. The Board has modified the Capital Assessments and Stress Testing (FR Y-14A and Q; OMB No. 7100-0341) in a manner consistent with the changes described above to the FR Y-9C. In addition, the Board has renumbered items in the FR Y-14A, Schedule A.1.d (Capital) instructions to correspond with related items on the FR Y-9C. The Board has adopted, as proposed, the following revisions to FR Y-14A, Schedule A.1.d, and FR Y-14Q, Schedule D, effective for the June 30, 2021, as of date:

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<sup>54</sup> See 85 FR 15776 (March 19, 2020).

*FR Y-14A, Schedule A.1.d (Capital)*

In order to align Schedule A.1.d with the FR Y-9C, the Board has added the following items to Schedule A.1.d:

- “Outstanding eligible long-term debt”;
- “Total loss-absorbing capacity”;
- “LTD and TLAC total risk-weighted assets ratios”;
- “*IHCs of foreign GSIBs only*: LTD and TLAC leverage ratios”;
- “LTD and TLAC supplementary leverage ratios”;
- “Institution-specific TLAC buffer necessary to avoid limitations on distributions discretionary bonus payments”;
- “TLAC risk-weighted buffer”; and
- “TLAC leverage buffer.”

*FR Y-14Q, Schedule D (Regulatory Capital)*

The Board has revised the instructions for item 1 (“Aggregate amount of non-significant investments in the capital of unconsolidated financial institutions”) to require banking organizations subject to Category I and II standards to include covered debt instruments.

**B. Regulatory Flexibility Act Analysis**

*OCC*: The Regulatory Flexibility Act, 5 U.S.C. 601 *et seq.*, (RFA), requires an agency either to provide a final regulatory flexibility analysis with a final rule for which a general notice of proposed rulemaking is required or to certify that the final rule will not have a significant, economic impact on a substantial number of small entities. The Small Business Administration

(SBA) establishes size standards that define which entities are small businesses for purposes of the RFA to include commercial banks and savings institutions with total assets of \$600 million or less and trust companies with total assets of \$41.5 million or less) or to certify that the final rule would not have a significant economic impact on a substantial number of small entities.

As of December 31, 2019, the OCC supervises 745 small entities.<sup>55</sup>

As part of the OCC's analysis, we consider whether the final rule will have a significant economic impact on a substantial number of small entities, pursuant to the RFA. Because the final rule only applies to advanced approaches banking organizations it will not impact any OCC-supervised small entities. Therefore, the final rule will not have a significant economic impact on a substantial number of small entities.

Therefore, the OCC certifies that the final rule will not have a significant economic impact on a substantial number of OCC-supervised small entities.

*Board:* The Regulatory Flexibility Act (RFA) generally requires that, in connection with a final rulemaking, an agency prepare and make available for public comment a final regulatory flexibility analysis describing the impact of the proposed rule on small entities. However, a final regulatory flexibility analysis is not required if the agency certifies that the final rule will not

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<sup>55</sup> The OCC calculated the number of small entities using the SBA's size thresholds for commercial banks and savings institutions, and trust companies, which are \$600 million and \$41.5 million, respectively. Consistent with the General Principles of Affiliation, 13 CFR 121.103(a), the OCC counted the assets of affiliated financial institutions when determining whether to classify a national bank or Federal savings association as a small entity.



have a significant economic impact on a substantial number of small entities. The Small Business Administration (SBA) has defined “small entities” to include banking organizations with total assets of less than or equal to \$600 million that are independently owned and operated or owned by a holding company with less than or equal to \$600 million in total assets.<sup>56</sup> For the reasons described below and under section 605(b) of the RFA, the Board certifies that the final rule will not have a significant economic impact on a substantial number of small entities.<sup>57</sup> As of December 31, 2019, there were 2,799 bank holding companies, 171 savings and loan holding companies, and 497 state member banks that would fit the SBA's current definition of “small entity” for purposes of the RFA.

The Board has considered the potential impact of the final rule on small entities in accordance with the RFA. Based on its analysis and for the reasons stated below, the Board believes that this final rule will not have a significant economic impact on a substantial number of small entities.

As discussed in detail above, the final rule amends the capital rule to require advanced approaches banking organizations to deduct exposures to covered debt instruments issued by covered BHCs, covered IHCs, and foreign GSIBs and their subsidiaries. These deductions are subject to regulatory thresholds, as described above. Deductions related to investments in and

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<sup>56</sup> See 13 CFR 121.201. Effective August 19, 2019, the SBA revised the size standards for banking organizations to \$600 million in assets from \$550 million in assets. 84 FR 34261 (July 18, 2019).

<sup>57</sup> 5 U.S.C. 605(b).

exposures to covered debt instruments are effectuated by deduction from tier 2 capital according to the corresponding deduction approach, subject to applicable deduction thresholds. However, the assets of institutions subject to this final rule substantially exceed the \$600 million asset threshold under which a banking organization is considered a “small entity” under SBA regulations.<sup>58</sup> Because the final rule is not likely to apply to any depository institution or company with assets of \$600 million or less, it is not expected to apply to any small entity for purposes of the RFA. In light of the foregoing, the Board certifies that the final rule will not have a significant economic impact on a substantial number of small entities supervised.

*FDIC:* The Regulatory Flexibility Act (RFA), 5 U.S.C. 601 et seq., generally requires an agency, in connection with a final rule, to prepare and make available for public comment a final regulatory flexibility analysis that describes the impact of a final rule on small entities.<sup>59</sup> However, a regulatory flexibility analysis is not required if the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities. The Small Business Administration (SBA) has defined “small entities” to include banking organizations with total assets of less than or equal to \$600 million who are independently owned and operated or owned by a holding company with less than \$600 million in total assets.<sup>60</sup> Generally, the

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<sup>58</sup> With respect to the revisions to the Board’s total loss-absorbing capacity rule, the scope of impacted institutions is different—Covered BHCs and Covered IHCs—but also only applies to institutions significantly above the threshold to be considered a “small entity.”

<sup>59</sup> 5 U.S.C. 601 et seq.

<sup>60</sup> The SBA defines a small banking organization as having \$600 million or less in assets, where “a financial institution’s assets are determined by averaging the assets reported on its four

FDIC considers a significant effect to be a quantified effect in excess of 5 percent of total annual salaries and benefits per institution, or 2.5 percent of total noninterest expenses. The FDIC believes that effects in excess of these thresholds typically represent significant effects for FDIC-supervised institutions. For the reasons described below and under section 605(b) of the RFA, the FDIC certifies that the final rule will not have a significant economic impact on a substantial number of small entities.

The FDIC supervises 3,270 institutions,<sup>61</sup> of which 2,492 are considered small entities for the purposes of RFA.<sup>62</sup>

This final rule will affect all institutions subject to the Category I and Category II capital standards, and their subsidiaries. The FDIC supervises one institution that is a subsidiary of an institution that is subject to the Category I capital standards, and no FDIC-supervised institutions are subsidiaries of institutions that are subject to the Category II capital standards.<sup>63</sup> The one FDIC-supervised institution that would be subject to this final rule is not considered a small entity for the purposes of the RFA since it is owned by a holding company with over \$600

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quarterly financial statements for the preceding year.” *See* 13 CFR 121.201 (as amended, effective August 19, 2019). “SBA counts the receipts, employees, or other measure of size of the concern whose size is at issue and all of its domestic and foreign affiliates.” *See* 13 CFR 121.103. Following these regulations, the FDIC uses a covered entity’s affiliated and acquired assets, averaged over the preceding four quarters, to determine whether the covered entity is “small” for the purposes of RFA.

<sup>61</sup> FDIC-supervised institutions are set forth in 12 U.S.C. 1813(q)(2).

<sup>62</sup> Call Report data, June 30, 2020.

<sup>63</sup> Call Report data, June 30, 2020.

million in total assets. Since this final rule does not affect any FDIC-supervised institutions that are defined as small entities for the purposes of the RFA, the FDIC certifies that the final rule will not have a significant economic impact on a substantial number of small entities.

### **C. Plain Language**

Section 722 of the Gramm-Leach-Bliley Act<sup>64</sup> requires the Federal banking agencies to use plain language in all proposed and final rules published after January 1, 2000. The agencies have sought to present the final rule in a simple and straightforward manner and did not receive any comments on the use of plain language in the proposed rule.

### **D. OCC Unfunded Mandates Reform Act of 1995 Determination**

The OCC analyzed the proposed rule under the factors set forth in the Unfunded Mandates Reform Act of 1995 (UMRA).<sup>65</sup> Under this analysis, the OCC considered whether the final rule includes a Federal mandate that may result in the expenditure by State, local, and Tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year (adjusted for inflation). Because the rule does not specifically require banks to modify their policies and procedures, the OCC has determined that there are no expenditures for the purposes

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<sup>64</sup> Pub. L. 106-102, section 722, 113 Stat. 1338, 1471 (1999).

<sup>65</sup> 2 U.S.C. 1532.

of UMRA. Therefore, the OCC concludes that this final rule will not result in expenditures of \$100 million or more annually by State, local, and Tribal governments, or by the private sector.<sup>66</sup>

#### **E. Riegle Community Development and Regulatory Improvement Act of 1994**

Pursuant to section 302(a) of the Riegle Community Development and Regulatory Improvement Act (RCDRIA),<sup>67</sup> in determining the effective date and administrative compliance requirements for new regulations that impose additional reporting, disclosure, or other requirements on insured depository institutions (IDIs), each Federal banking agency must consider, consistent with principles of safety and soundness and the public interest, any administrative burdens that such regulations would place on depository institutions, including small depository institutions, and customers of depository institutions, as well as the benefits of such regulations. In addition, section 302(b) of RCDRIA requires new regulations and amendments to regulations that impose additional reporting, disclosures, or other new requirements on IDIs generally to take effect on the first day of a calendar quarter that begins on or after the date on which the regulations are published in final form.<sup>68</sup>

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<sup>66</sup> Based on available supervisory information, the OCC determined that no OCC-supervised advanced approaches institutions currently hold TLAC instruments. Thus, there would no cost of capital associated with the implementation of this proposal. The OCC estimates that, if implemented, non-mandated, but anticipated compliance costs associated with activities such as modifying procedures and internal audit would be less than \$1 million.

<sup>67</sup> 12 U.S.C. 4802(a).

<sup>68</sup> 12 U.S.C. 4802.

The Federal banking agencies considered the administrative burdens and benefits of the final rule and its elective framework in determining its effective date and administrative compliance requirements. As such, the final rule will be effective on April 1, 2021.

#### **F. Congressional Review Act**

For purposes of Congressional Review Act, the OMB makes a determination as to whether a final rule constitutes a “major” rule.<sup>69</sup> If a rule is deemed a “major rule” by the Office of Management and Budget (OMB), the Congressional Review Act generally provides that the rule may not take effect until at least 60 days following its publication.<sup>70</sup>

The Congressional Review Act defines a “major rule” as any rule that the Administrator of the Office of Information and Regulatory Affairs of the OMB finds has resulted in or is likely to result in (A) an annual effect on the economy of \$100,000,000 or more; (B) a major increase in costs or prices for consumers, individual industries, Federal, State, or local government agencies or geographic regions, or (C) significant adverse effects on competition, employment, investment, productivity, innovation, or on the ability of United States-based enterprises to compete with foreign-based enterprises in domestic and export markets.<sup>71</sup> As required by the Congressional Review Act, the agencies will submit the final rule and other appropriate reports to Congress and the Government Accountability Office for review.

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<sup>69</sup> 5 U.S.C. 801 et seq.

<sup>70</sup> 5 U.S.C. 801(a)(3).

<sup>71</sup> 5 U.S.C. 804(2).

## **List of Subjects**

### **12 CFR Part 3**

Administrative practice and procedure, Capital, National banks, Risk.

### **12 CFR Part 217**

Administrative practice and procedure, Banks, Banking, Capital, Federal Reserve System, Holding companies.

### **12 CFR Part 252**

Administrative practice and procedure, Banks, banking, Credit, Federal Reserve System, Holding companies, Investments, Qualified financial contracts, Reporting and recordkeeping requirements, Securities.

### **12 CFR Part 324**

Administrative practice and procedure, Banks, Banking, Capital adequacy, Savings associations, State non-member banks.

## **Office of the Comptroller of the Currency**

For the reasons set out in the joint preamble, the OCC amends 12 CFR part 3 as follows.

### **PART 3 – CAPITAL ADEQUACY STANDARDS**

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

AUTHORITY: 12 U.S.C. 93a, 161, 1462, 1462a, 1463, 1464, 1818, 1828(n), 1828 note, 1831n note, 1835, 3907, 3909, 5412(b)(2)(B), and Pub. L. 116-136, 134 Stat. 281.

2. In § 3.2:

- a. Add the definitions of “Covered debt instrument”, “Excluded covered debt instrument”, and “Investment in a covered debt instrument”, in alphabetical order;
- b. Revise the definitions of “Indirect exposure” and “Synthetic exposure”;
- c. Remove “§3.10(c)(4)(ii)(J)” and add “§3.10(c)(2)(x)” in its place in the definition of “Fiduciary or custodial and safekeeping accounts”; and
- d. Remove “§3.10(c)(4)(ii)” and add “§3.10(c)(2)” in its place in the definition of “Total leverage exposure”.

The additions and revisions read as follows:

**§ 3.2 Definitions.**

\* \* \* \* \*

*Covered debt instrument* means an unsecured debt instrument that is:

(1) Issued by a global systemically important BHC, as defined in 12 CFR 217.2, and that is an eligible debt security, as defined in 12 CFR 252.61, or that is *pari passu* or subordinated to any eligible debt security issued by the global systemically important BHC; or

(2) Issued by a Covered IHC, as defined in 12 CFR 252.161, and that is an eligible Covered IHC debt security, as defined in 12 CFR 252.161, or that is *pari passu* or subordinated to any eligible Covered IHC debt security issued by the Covered IHC; or

(3) Issued by a global systemically important banking organization, as defined in 12 CFR 252.2 other than a global systemically important BHC, as defined in 12 CFR 217.2; or issued by a subsidiary of a global systemically important banking organization that is not a global



systemically important BHC, other than a Covered IHC, as defined in 12 CFR 252.161; and where

(i) The instrument is eligible for use to comply with an applicable law or regulation requiring the issuance of a minimum amount of instruments to absorb losses or recapitalize the issuer or any of its subsidiaries in connection with a resolution, receivership, insolvency, or similar proceeding of the issuer or any of its subsidiaries; or

(ii) The instrument is *pari passu* or subordinated to any instrument described in paragraph (3)(i) of this definition; for purposes of this paragraph (3)(ii) of this definition, if the issuer may be subject to a special resolution regime, in its jurisdiction of incorporation or organization, that addresses the failure or potential failure of a financial company and any instrument described in paragraph (3)(i) of this definition is eligible under that special resolution regime to be written down or converted into equity or any other capital instrument, then an instrument is *pari passu* or subordinated to any instrument described in paragraph (3)(i) of this definition if that instrument is eligible under that special resolution regime to be written down or converted into equity or any other capital instrument ahead of or proportionally with any instrument described in paragraph (3)(i) of this definition; and

(4) Provided that, for purposes of this definition, *covered debt instrument* does not include a debt instrument that qualifies as tier 2 capital pursuant to 12 CFR 217.20(d) or that is otherwise treated as regulatory capital by the primary supervisor of the issuer.

\* \* \* \* \*

*Excluded covered debt instrument* means an investment in a covered debt instrument held by a national bank or Federal savings association that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, that:

(1) Is held in connection with market making-related activities permitted under 12 CFR 44.4, provided that a direct exposure or an indirect exposure to a covered debt instrument is held for 30 business days or less; and

(2) Has been designated as an excluded covered debt instrument by the national bank or Federal savings association that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, pursuant to 12 CFR 3.22(c)(5)(iv)(A).

\* \* \* \* \*

*Indirect exposure* means an exposure that arises from the national bank's or Federal savings association's investment in an investment fund which holds an investment in the national bank's or Federal savings association's own capital instrument, or an investment in the capital of an unconsolidated financial institution. For an advanced approaches national bank or Federal savings association, indirect exposure also includes an investment in an investment fund that holds a covered debt instrument.

\* \* \* \* \*

*Investment in a covered debt instrument* means a national bank's or Federal savings association's net long position calculated in accordance with § 3.22(h) in a covered debt instrument, including direct, indirect, and synthetic exposures to the debt instrument, excluding any underwriting positions held by the national bank or Federal savings association for five or fewer business days.

\* \* \* \* \*

*Synthetic exposure* means an exposure whose value is linked to the value of an investment in the national bank or Federal savings association's own capital instrument or to the value of an investment in the capital of an unconsolidated financial institution. For an advanced approaches national bank or Federal savings association, synthetic exposure includes an exposure whose value is linked to the value of an investment in a covered debt instrument.

\* \* \* \* \*

3. Section 3.10 is amended as follows:

a. Redesignate paragraph (d) as (e);

b. Redesignate paragraph (c) introductory text and paragraphs (c)(1) through (3) as paragraph (d) introductory text and paragraphs (d)(1) through (3), respectively;

c. Redesignate paragraph (c)(4) as paragraph (c) as follows:

Old Paragraph	New Paragraph
(c)(4)(i)-(ii)	(c)(1)-(2)
(c)(4)(i)(A)-(B)	(c)(1)(i)-(ii)
(c)(4)(ii)(A)-(B)	(c)(2)(i)-(ii)
(c)(4)(ii)(B)(1)-(2)	(c)(2)(ii)(A)-(B)
(c)(4)(ii)(B)(1)(i)-(ii)	(c)(2)(ii)(A)(1)-(2)
(c)(4)(ii)(C)	(c)(2)(iii)
(c)(4)(ii)(C)(1)-(7)	(c)(2)(iii)(A)-(G)
(c)(4)(ii)(C)(1)(i)-(iii)	(c)(2)(iii)(A)(1)-(3)
(c)(4)(ii)(C)(2)(i)-(iii)	(c)(2)(iii)(B)(1)-(3)

(c)(4)(ii)(D)	(c)(2)(iv)
(c)(4)(ii)(D)(I)-(2)	(c)(2)(iv)(A)-(B)
(c)(4)(ii)(D)(2)(i)-(iv)	(c)(2)(iv)(B)(I)-(4)
(c)(4)(ii)(E)	(c)(2)(v)
(c)(4)(ii)(E)(I)-(3)	(c)(2)(v)(A)-(C)
(c)(4)(ii)(F)	(c)(2)(vi)
(c)(4)(ii)(F)(I)-(2)	(c)(2)(vi)(A)-(B)
(c)(4)(ii)(G)-(I)	(c)(2)(vii)-(ix)
(c)(4)(ii)(I)(I)-(5)	(c)(2)(ix)(A)-(E)
(c)(4)(ii)(J)(I)-(2)	(c)(2)(x)(A)-(B)

d. Redesignate paragraph (c)(5) as paragraph (d)(4).

e. In newly redesignated paragraph (c):

i. Remove “paragraphs (c)(4)(ii)(A) through (H)” and add “paragraphs (c)(2)(i) through (viii)” in paragraph (c)(2);

ii. Remove “paragraph (c)(4)(ii)(I)” and add “paragraph (c)(2)(ix)” wherever it appears;

iii. Remove “paragraph (c)(4)(ii)(J)” and add “paragraph (c)(2)(x)” wherever it appears;

iv. Remove “paragraph (c)(4)(ii)(B)(I)” and add “paragraph (c)(2)(ii)(A)” in paragraph (c)(2)(ii)(A)(2);

v. Remove “paragraph (c)(4)(ii)(B)(2)(i)” and add “paragraph (c)(2)(ii)(B)(I)” in paragraph (c)(2)(ii)(B)(I);

vi. Remove “paragraph (c)(4)(ii)(B)(2)(ii)” and add “paragraph (c)(2)(ii)(B)(2)” in paragraph (c)(2)(ii)(B)(I);

vii. Remove “paragraphs (c)(4)(ii)(C)(3) through (7)” and add “paragraphs (c)(2)(iii)(C) through (G)” wherever it appears;

viii. Remove “paragraph (c)(4)(ii)(C)(I)(ii)” and add “paragraph (c)(2)(iii)(A)(2)”;

ix. Remove “paragraph (c)(4)(ii)(C)(2)(i)” and add “paragraph (c)(2)(iii)(B)(I)” wherever it appears;

x. Remove “paragraph (c)(4)(ii)(C)(6)” and add “paragraph (c)(2)(iii)(F)” in paragraph (c)(2)(iii)(F);

xi. Remove “paragraph (c)(4)(ii)(D)(I)” and add “paragraph (C)(2)(iv)(A)” in paragraph (c)(2)(iv)(B)(3);

xii. Remove “paragraph (c)(4)(ii)(A)” and add “paragraph (c)(2)(i)” in paragraph (c)(2)(v);

xiii. Remove “part (c)(4)(ii)(D)” and add “paragraph (c)(2)(iv)” in paragraph (c)(2)(ix); and

xiv. Remove “paragraphs (c)(4)(ii)(I)(I) through (3)” and add “paragraphs (c)(2)(ix)(A) through (C)”;

f. Revise redesignated paragraph (c)(1) in paragraph (c)(2)(ix)(E); and

g. Revise redesignated paragraph (d), introductory text.

The revisions read as follows:

### **§ 3.10 Minimum capital requirements.**

\* \* \* \* \*

(c) *Supplementary leverage ratio.* (1) A Category III national bank or Federal savings association or advanced approaches national bank or Federal savings association must determine its supplementary leverage ratio in accordance with this paragraph, beginning with the calendar

quarter immediately following the quarter in which the national bank or Federal savings association is identified as a Category III national bank or Federal savings association. An advanced approaches national bank's or Federal savings association's or a Category III national bank's or Federal savings association's supplementary leverage ratio is the ratio of its tier 1 capital to total leverage exposure, the latter which is calculated as the sum of:

\* \* \* \* \*

(d) *Advanced approaches capital ratio calculations.* An advanced approaches national bank or Federal savings association that has completed the parallel run process and received notification from the OCC pursuant to §3.121(d) must determine its regulatory capital ratios as described in paragraphs (d)(1) through (3) of this section.

\* \* \* \* \*

4. In § 3.22, revise paragraphs (c) and its footnotes, and paragraphs (f) and (h) to read as follows:

**§ 3.22 Regulatory capital adjustments and deductions.**

\* \* \* \* \*

(c) *Deductions from regulatory capital related to investments in capital instruments or covered debt instruments*<sup>23</sup>—(1) *Investment in the national bank's or Federal savings association's own capital instruments.* A national bank or Federal savings association must

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<sup>23</sup> The national bank or Federal savings association must calculate amounts deducted under paragraphs (c) through (f) of this section after it calculates the amount of ALLL or AACL, as applicable, includable in tier 2 capital under § 3.20(d)(3).

deduct an investment in the national bank's or Federal savings association's own capital instruments, as follows:

(i) A national bank or Federal savings association must deduct an investment in the national bank's or Federal savings association's own common stock instruments from its common equity tier 1 capital elements to the extent such instruments are not excluded from regulatory capital under § 3.20(b)(1);

(ii) A national bank or Federal savings association must deduct an investment in the national bank's or Federal savings association's own additional tier 1 capital instruments from its additional tier 1 capital elements; and

(iii) A national bank or Federal savings association must deduct an investment in the national bank's or Federal savings association's own tier 2 capital instruments from its tier 2 capital elements.

(2) *Corresponding deduction approach.* For purposes of subpart C of this part, the corresponding deduction approach is the methodology used for the deductions from regulatory capital related to reciprocal cross holdings (as described in paragraph (c)(3) of this section), investments in the capital of unconsolidated financial institutions for a national bank or Federal savings association that is not an advanced approaches national bank or Federal savings association (as described in paragraph (c)(4) of this section), non-significant investments in the capital of unconsolidated financial institutions for an advanced approaches national bank or Federal savings association (as described in paragraph (c)(5) of this section), and non-common stock significant investments in the capital of unconsolidated financial institutions for an advanced approaches national bank or Federal savings association (as described in paragraph

(c)(6) of this section). Under the corresponding deduction approach, a national bank or Federal savings association must make deductions from the component of capital for which the underlying instrument would qualify if it were issued by the national bank or Federal savings association itself, as described in paragraphs (c)(2)(i) through (iii) of this section. If the national bank or Federal savings association does not have a sufficient amount of a specific component of capital to effect the required deduction, the shortfall must be deducted according to paragraph (f) of this section.

(i) If an investment is in the form of an instrument issued by a financial institution that is not a regulated financial institution, the national bank or Federal savings association must treat the instrument as:

(A) A common equity tier 1 capital instrument if it is common stock or represents the most subordinated claim in a liquidation of the financial institution; and

(B) An additional tier 1 capital instrument if it is subordinated to all creditors of the financial institution and is senior in liquidation only to common shareholders.

(ii) If an investment is in the form of an instrument issued by a regulated financial institution and the instrument does not meet the criteria for common equity tier 1, additional tier 1 or tier 2 capital instruments under § 3.20, the national bank or Federal savings association must treat the instrument as:

(A) A common equity tier 1 capital instrument if it is common stock included in GAAP equity or represents the most subordinated claim in liquidation of the financial institution;



(B) An additional tier 1 capital instrument if it is included in GAAP equity, subordinated to all creditors of the financial institution, and senior in a receivership, insolvency, liquidation, or similar proceeding only to common shareholders;

(C) A tier 2 capital instrument if it is not included in GAAP equity but considered regulatory capital by the primary supervisor of the financial institution; and

(D) For an advanced approaches national bank or Federal savings association, a tier 2 capital instrument if it is a covered debt instrument.

(iii) If an investment is in the form of a non-qualifying capital instrument (as defined in § 3.300(c)), the national bank or Federal savings association must treat the instrument as:

(A) An additional tier 1 capital instrument if such instrument was included in the issuer's tier 1 capital prior to May 19, 2010; or

(B) A tier 2 capital instrument if such instrument was included in the issuer's tier 2 capital (but not includable in tier 1 capital) prior to May 19, 2010.

(3) *Reciprocal cross holdings in the capital of financial institutions.* (i) A national bank or Federal savings association must deduct an investment in the capital of other financial institutions that it holds reciprocally with another financial institution, where such reciprocal cross holdings result from a formal or informal arrangement to swap, exchange, or otherwise intend to hold each other's capital instruments, by applying the corresponding deduction approach in paragraph (c)(2) of this section.

(ii) An advanced approaches national bank or Federal savings association must deduct an investment in any covered debt instrument that the institution holds reciprocally with another

financial institution, where such reciprocal cross holdings result from a formal or informal arrangement to swap, exchange, or otherwise intend to hold each other's capital or covered debt instruments, by applying the corresponding deduction approach in paragraph (c)(2) of this section.

(4) *Investments in the capital of unconsolidated financial institutions.* A national bank or Federal savings association that is not an advanced approaches national bank or Federal savings association must deduct its investments in the capital of unconsolidated financial institutions (as defined in § 3.2) that exceed 25 percent of the sum of the national bank or Federal savings association's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>24</sup> The deductions described in this section are net of associated DTLs in accordance with paragraph (e) of this section. In addition, with the prior written approval of the OCC, a national bank or Federal savings association that underwrites a failed underwriting, for the period of time stipulated by the OCC, is not required to deduct an investment in the capital of an

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<sup>24</sup> With the prior written approval of the OCC, for the period of time stipulated by the OCC, a national bank or Federal savings association is not required to deduct a non-significant investment in the capital instrument of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph if the financial institution is in distress and if such investment is made for the purpose of providing financial support to the financial institution, as determined by the OCC.

unconsolidated financial institution pursuant to this paragraph (c) to the extent the investment is related to the failed underwriting.<sup>25</sup>

*(5) Non-significant investments in the capital of unconsolidated financial institutions. (i)*

An advanced approaches national bank or Federal savings association must deduct its non-significant investments in the capital of unconsolidated financial institutions (as defined in § 3.2) that, in the aggregate and together with any investment in a covered debt instrument (as defined in §3.2) issued by a financial institution in which the national bank or Federal savings association does not have a significant investment in the capital of the unconsolidated financial institution (as defined in §3.2), exceeds 10 percent of the sum of the advanced approaches national bank's or Federal savings association's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section (the 10 percent threshold for non-significant investments) by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>26</sup> The deductions described in this paragraph are net of associated DTLs in accordance with paragraph (e) of this

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<sup>25</sup> Any non-significant investments in the capital of an unconsolidated financial institution that is not required to be deducted under this paragraph (c)(4) or otherwise under this section must be assigned the appropriate risk weight under subparts D, E, or F of this part, as applicable.

<sup>26</sup> With the prior written approval of the OCC, for the period of time stipulated by the OCC, an advanced approaches a national bank or Federal savings association is not required to deduct a non-significant investment in the capital instrument of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph if the financial institution is in distress and if such investment is made for the purpose of providing financial support to the financial institution, as determined by the OCC.

section. In addition, with the prior written approval of the OCC, an advanced approaches national bank or Federal savings association that underwrites a failed underwriting, for the period of time stipulated by the OCC, is not required to deduct from capital a non-significant investment in the capital of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph (c)(5) to the extent the investment is related to the failed underwriting.<sup>27</sup> For any calculation under this paragraph (c)(5)(i), an advanced approaches national bank or Federal savings association may exclude the amount of an investment in a covered debt instrument under paragraphs (c)(5)(iii) or (c)(5)(iv) of this section, as applicable.

(ii) For an advanced approaches national bank or Federal savings association, the amount to be deducted under this paragraph (c)(5) from a specific capital component is equal to:

(A) The advanced approaches national bank's or Federal savings association's aggregate non-significant investments in the capital of an unconsolidated financial institution and, if applicable, any investments in a covered debt instrument subject to deduction under this paragraph (c)(5), exceeding the 10 percent threshold for non-significant investments, multiplied by

(B) The ratio of the advanced approaches national bank's or Federal savings association's aggregate non-significant investments in the capital of an unconsolidated financial institution (in the form of such capital component) to the national bank's or Federal savings association's total

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<sup>27</sup> Any non-significant investment in the capital of an unconsolidated financial institution or any investment in a covered debt instrument that is not required to be deducted under this paragraph (c)(4) or otherwise under this section must be assigned the appropriate risk weight under subparts D, E, or F of this part, as applicable.

non-significant investments in unconsolidated financial institutions, with an investment in a covered debt instrument being treated as tier 2 capital for this purpose.

(iii) For purposes of applying the deduction under paragraph (c)(5)(i) of this section, an advanced approaches national bank or Federal savings association that is not a subsidiary of a global systemically important banking organization, as defined in 12 CFR 252.2, may exclude from the deduction the amount of the national bank's or Federal savings association's gross long position, in accordance with § 3.22(h)(2), in investments in covered debt instruments issued by financial institutions in which the national bank or Federal savings association does not have a significant investment in the capital of the unconsolidated financial institutions up to an amount equal to 5 percent of the sum of the national bank's or Federal savings association's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section, net of associated DTLs in accordance with paragraph (e) of this section.

(iv) Prior to applying the deduction under paragraph (c)(5)(i) of this section:

(A) A national bank or Federal savings association that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, may designate any investment in a covered debt instrument as an excluded covered debt instrument, as defined in § 3.2.

(B) A national bank or Federal savings association that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, must deduct according to the corresponding deduction approach in paragraph (c)(2) of this section, its gross long position, calculated in accordance with paragraph (h)(2) of this section, in a covered debt instrument that

was originally designated as an excluded covered debt instrument, in accordance with paragraph (c)(5)(iv)(A) above, but no longer qualifies as an excluded covered debt instrument.

(C) A national bank or Federal savings association that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, must deduct according to the corresponding deduction approach in paragraph (c)(2) of this section the amount of its gross long position, calculated in accordance with paragraph (h)(2) of this section, in a direct or indirect investment in a covered debt instrument that was originally designated as an excluded covered debt instrument, in accordance with paragraph (c)(5)(iv)(A) above, and has been held for more than thirty business days.

(D) A national bank or Federal savings association that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, must deduct according to the corresponding deduction approach in paragraph (c)(2) of this section its gross long position, calculated in accordance with paragraph (h)(2) of this section, of its aggregate investment in excluded covered debt instruments that exceeds 5 percent of the sum of the national bank's or Federal savings association's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section, net of associated DTLs in accordance with paragraph (e) of this section.

(6) *Significant investments in the capital of unconsolidated financial institutions that are not in the form of common stock.* If an advanced approaches national bank or Federal savings association has a significant investment in the capital of an unconsolidated financial institution, the advanced approaches national bank or Federal savings association must deduct from capital any such investment issued by the unconsolidated financial institution that is held by the national bank or Federal savings association other than an investment in the form of common stock, as

well as any investment in a covered debt instrument issued by the unconsolidated financial institution, by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>28</sup> The deductions described in this section are net of associated DTLs in accordance with paragraph (e) of this section. In addition, with the prior written approval of the OCC, for the period of time stipulated by the OCC, an advanced approaches national bank or Federal savings association that underwrites a failed underwriting is not required to deduct the significant investment in the capital of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph (c)(6) if such investment is related to such failed underwriting.

\* \* \* \* \*

*(f) Insufficient amounts of a specific regulatory capital component to effect deductions.*

Under the corresponding deduction approach, if a national bank or Federal savings association does not have a sufficient amount of a specific component of capital to effect the full amount of any deduction from capital required under paragraph (d) of this section, the national bank or Federal savings association must deduct the shortfall amount from the next higher (that is, more subordinated) component of regulatory capital. Any investment by an advanced approaches national bank or Federal savings association in a covered debt instrument must be treated as an investment in the tier 2 capital for purposes of this paragraph. Notwithstanding any other

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<sup>28</sup> With prior written approval of the OCC, for the period of time stipulated by the OCC, an advanced approaches national bank or Federal savings association is not required to deduct an investment in a covered debt instrument under this paragraph (c)(5) or otherwise under this section if such investment is made for the purpose of providing financial support to the financial institution as determined by the OCC.

provision of this section, a qualifying community banking organization (as defined in § 3.12) that has elected to use the community bank leverage ratio framework pursuant to § 3.12 is not required to deduct any shortfall of tier 2 capital from its additional tier 1 capital or common equity tier 1 capital.

\* \* \* \* \*

(h) *Net long position.* (1) For purposes of calculating the amount of a national bank's or Federal savings association's investment in the national bank's or Federal savings association's own capital instrument, investment in the capital of an unconsolidated financial institution, and investment in a covered debt instrument under this section, the institution's net long position is the gross long position in the underlying instrument determined in accordance with paragraph (h)(2) of this section, as adjusted to recognize any short position by the national bank or Federal savings association in the same instrument subject to paragraph (h)(3) of this section.

(2) *Gross long position.* A gross long position is determined as follows:

(i) For an equity exposure that is held directly by the national bank or Federal savings association, the adjusted carrying value of the exposure as that term is defined in § 3.51(b);

(ii) For an exposure that is held directly and that is not an equity exposure or a securitization exposure, the exposure amount as that term is defined in § 3.2;

(iii) For each indirect exposure, the national bank's or Federal savings association's carrying value of its investment in an investment fund or, alternatively:

(A) A national bank or Federal savings association may, with the prior approval of the OCC, use a conservative estimate of the amount of its indirect investment in the national bank's



or Federal savings association's own capital instruments, its indirect investment in the capital of an unconsolidated financial institution, or its indirect investment in a covered debt instrument held through a position in an index, as applicable; or

(B) A national bank or Federal savings association may calculate the gross long position for an indirect exposure to the national bank's or Federal savings association's own capital the capital in an unconsolidated financial institution, or a covered debt instrument by multiplying the national bank's or Federal savings association's carrying value of its investment in the investment fund by either:

(1) The highest stated investment limit (in percent) for an investment in the national bank's or Federal savings association's own capital instruments, an investment in the capital of an unconsolidated financial institution, or an investment in a covered debt instrument, as applicable, as stated in the prospectus, partnership agreement, or similar contract defining permissible investments of the investment fund; or

(2) The investment fund's actual holdings (in percent) of the investment in the national bank's or Federal savings association's own capital instruments, investment in the capital of an unconsolidated financial institution, or investment in an covered debt instrument, as applicable; and

(iv) For a synthetic exposure, the amount of the national bank's or Federal savings association's loss on the exposure if the reference capital instrument or covered debt instrument were to have a value of zero.

(3) *Adjustments to reflect a short position.* In order to adjust the gross long position to recognize a short position in the same instrument under paragraph (h)(1) of this section, the following criteria must be met:

(i) The maturity of the short position must match the maturity of the long position, or the short position must have a residual maturity of at least one year (maturity requirement); or

(ii) For a position that is a trading asset or trading liability (whether on- or off-balance sheet) as reported on the national bank's or Federal savings association's Call Report, if the national bank or Federal savings association has a contractual right or obligation to sell the long position at a specific point in time and the counterparty to the contract has an obligation to purchase the long position if the national bank or Federal savings association exercises its right to sell, this point in time may be treated as the maturity of the long position such that the maturity of the long position and short position are deemed to match for purposes of the maturity requirement, even if the maturity of the short position is less than one year; and

(iii) For an investment in a national bank's or Federal savings association's own capital instrument under paragraph (c)(1) of this section, an investment in the capital of an unconsolidated financial institution under paragraphs (c)(4), (c)(5), (c)(6), and (d) of this section (as applicable), and an investment in a covered debt instrument under paragraphs (c)(1), (c)(5), and (c)(6) of this section:

(A) The national bank or Federal savings association may only net a short position against a long position in an investment in the national bank's or Federal savings association's own capital instrument under paragraph (c)(1) of this section if the short position involves no counterparty credit risk;

(B) A gross long position in an investment in the national bank’s or Federal savings association’s own capital instrument, an investment in the capital of an unconsolidated financial institution, or an investment in a covered debt instrument due to a position in an index may be netted against a short position in the same index;

(C) Long and short positions in the same index without maturity dates are considered to have matching maturities; and

(D) A short position in an index that is hedging a long cash or synthetic position in an investment in the national bank’s or Federal savings association’s own capital instrument, an investment in the capital instrument of an unconsolidated financial institution, or an investment in a covered debt instrument can be decomposed to provide recognition of the hedge. More specifically, the portion of the index that is composed of the same underlying instrument that is being hedged may be used to offset the long position if both the long position being hedged and the short position in the index are reported as a trading asset or trading liability (whether on- or off-balance sheet) on the national bank’s or Federal savings association’s Call Report, and the hedge is deemed effective by the national bank’s or Federal savings association’s internal control processes, which have not been found to be inadequate by the OCC.

\* \* \* \* \*

**§ 3.121 [Amended]**

5. Section 3.121 is amended by removing “§3.10(c)(1) through (3)” and adding “§3.10(d)(1) through (3)” in its place in paragraph (c).

\* \* \* \* \*

6. Section 3.132 is amended by removing “§3.10(c)(4)(ii)(B)(2)” and adding “§3.10(c)(2)(ii)(B)” wherever it appears.

\* \* \* \* \*

7. Section 3.304 is amended by:

a. Removing “§3.10(c)(4)” and adding in its place “§3.10(d)”; and

b. Removing “§3.10(c)(4)(ii)(J)(I)” and adding in its place “§3.10(c)(2)(x)(A).”

\* \* \* \* \*

### **Board of Governors of the Federal Reserve System**

For the reasons set forth in the joint preamble, the Board amends part 217 of chapter II of title 12 of the Code of Federal Regulations as follows:

### **PART 217—CAPITAL ADEQUACY OF BANK HOLDING COMPANIES, SAVINGS AND LOAN HOLDING COMPANIES, AND STATE MEMBER BANKS (REGULATION Q).**

8. The authority citation for part 217 continues to read as follows:

AUTHORITY: 12 U.S.C. 248(a), 321–338a, 481–486, 1462a, 1467a, 1818, 1828, 1831n, 1831o, 1831p–l, 1831w, 1835, 1844(b), 1851, 3904, 3906–3909, 4808, 5365, 5368, 5371, and 5371 note; Pub. L. 116–136, 134 Stat. 281.

7. In § 217.2:

- a. Add the definitions of “Covered debt instrument”, “Excluded covered debt instrument”, “Investment in a covered debt instrument”, in alphabetical order;
- b. Revise the definitions of “Indirect exposure” and “Synthetic exposure”;
- c. Remove “§217.10(c)(4)(ii)(J)” and add “§217.10(c)(2)(x)” in its place in the definition of “Fiduciary or custodial and safekeeping accounts”; and
- d. Remove “§217.10(c)(4)(ii)” and add “§217.10(c)(2)” in its place in the definition of “Total leverage exposure”.

The additions and revisions read as follows:

**§ 217.2        Definitions.**

\*        \*        \*        \*        \*

*Covered debt instrument* means an unsecured debt instrument that is:

- (1) Issued by a global systemically important BHC and that is an eligible debt security, as defined in 12 CFR 252.61, or that is *pari passu* or subordinated to any eligible debt security issued by the global systemically important BHC; or
- (2) Issued by a Covered IHC, as defined in 12 CFR 252.161, and that is an eligible Covered IHC debt security, as defined in 12 CFR 252.161, or that is *pari passu* or subordinated to any eligible Covered IHC debt security issued by the Covered IHC; or
- (3) Issued by a global systemically important banking organization, as defined in 12 CFR 252.2 other than a global systemically important BHC; or issued by a subsidiary of a global

systemically important banking organization that is not a global systemically important BHC, other than a Covered IHC, as defined in 12 CFR 252.161; and where,

(i) The instrument is eligible for use to comply with an applicable law or regulation requiring the issuance of a minimum amount of instruments to absorb losses or recapitalize the issuer or any of its subsidiaries in connection with a resolution, receivership, insolvency, or similar proceeding of the issuer or any of its subsidiaries; or

(ii) The instrument is *pari passu* or subordinated to any instrument described in paragraph (3)(i) of this definition; for purposes of this paragraph (3)(ii) of this definition, if the issuer may be subject to a special resolution regime, in its jurisdiction of incorporation or organization, that addresses the failure or potential failure of a financial company and any instrument described in paragraph (3)(i) of this definition is eligible under that special resolution regime to be written down or converted into equity or any other capital instrument, then an instrument is *pari passu* or subordinated to any instrument described in paragraph (3)(i) of this definition if that instrument is eligible under that special resolution regime to be written down or converted into equity or any other capital instrument ahead of or proportionally with any instrument described in paragraph (3)(i) of this definition; and

(4) Provided that, for purposes of this definition, *covered debt instrument* does not include a debt instrument that qualifies as tier 2 capital pursuant to 12 CFR 217.20(d) or that is otherwise treated as regulatory capital by the primary supervisor of the issuer.

\* \* \* \* \*

*Excluded covered debt instrument* means an investment in a covered debt instrument held by a global systemically important BHC or a Board-regulated institution that is a subsidiary of a global systemically important BHC that:

(1) Is held in connection with market making-related activities permitted under 12 CFR 248.4, provided that a direct exposure or an indirect exposure to a covered debt instrument is held for 30 business days or less; and

(2) Has been designated as an excluded covered debt instrument by the global systemically important BHC or the subsidiary of a global systemically important BHC pursuant to 12 CFR 217.22(c)(5)(iv)(A).

\* \* \* \* \*

*Indirect exposure* means an exposure that arises from the Board-regulated institution's investment in an investment fund which holds an investment in the Board-regulated institution's own capital instrument or an investment in the capital of an unconsolidated financial institution. For an advanced approaches Board-regulated institution, indirect exposure also includes an investment in an investment fund that holds a covered debt instrument.

\* \* \* \* \*

*Investment in a covered debt instrument* means a Board-regulated institution's net long position calculated in accordance with § 217.22(h) in a covered debt instrument, including direct, indirect, and synthetic exposures to the debt instrument, excluding any underwriting positions held by the Board-regulated institution for five or fewer business days.

\* \* \* \* \*

*Synthetic exposure* means an exposure whose value is linked to the value of an investment in the Board-regulated institution's own capital instrument or to the value of an investment in the capital of an unconsolidated financial institution. For an advanced approaches Board-regulated institution, synthetic exposure includes an exposure whose value is linked to the value of an investment in a covered debt instrument.

\* \* \* \* \*

10. Section 217.10 is amended as follows:

- a. Redesignate paragraph (d) as (e);
- b. Redesignate paragraph (c) introductory text and paragraphs (c)(1) through (3) as paragraph (d) introductory text and paragraphs (d)(1) through (3), respectively;
- c. Redesignate paragraph (c)(4) as paragraph (c) as follows:

Old Paragraph	New Paragraph
(c)(4)(i)-(ii)	(c)(1)-(2)
(c)(4)(i)(A)-(B)	(c)(1)(i)-(ii)
(c)(4)(ii)(A)-(B)	(c)(2)(i)-(ii)
(c)(4)(ii)(B)(1)-(2)	(c)(2)(ii)(A)-(B)
(c)(4)(ii)(B)(1)(i)-(ii)	(c)(2)(ii)(A)(1)-(2)
(c)(4)(ii)(C)	(c)(2)(iii)
(c)(4)(ii)(C)(1)-(7)	(c)(2)(iii)(A)-(G)
(c)(4)(ii)(C)(1)(i)-(iii)	(c)(2)(iii)(A)(1)-(3)
(c)(4)(ii)(C)(2)(i)-(iii)	(c)(2)(iii)(B)(1)-(3)
(c)(4)(ii)(D)	(c)(2)(iv)



(c)(4)(ii)(D)(I)-(2)	(c)(2)(iv)(A)-(B)
(c)(4)(ii)(D)(2)(i)-(iv)	(c)(2)(iv)(B)(I)-(4)
(c)(4)(ii)(E)	(c)(2)(v)
(c)(4)(ii)(E)(I)-(3)	(c)(2)(v)(A)-(C)
(c)(4)(ii)(F)	(c)(2)(vi)
(c)(4)(ii)(F)(I)-(2)	(c)(2)(vi)(A)-(B)
(c)(4)(ii)(G)-(I)	(c)(2)(vii)-(ix)
(c)(4)(ii)(I)(I)-(5)	(c)(2)(ix)(A)-(E)
(c)(4)(ii)(J)(I)-(2)	(c)(2)(x)(A)-(B)

d. Redesignate paragraph (c)(5) as paragraph (d)(4).

e. In newly redesignated paragraph (c), remove “paragraphs (c)(4)(ii)(A) through (H)” and add “paragraphs (c)(2)(i) through (viii)”;

remove “paragraph (c)(4)(ii)(I)” and add “paragraph (c)(2)(ix)” wherever it appears; remove “paragraph (c)(4)(ii)(J)” and add “paragraph (c)(2)(x)” wherever it appears; remove “paragraph (c)(4)(ii)(B)(I)” and add “paragraph (c)(2)(ii)(A)”;

remove “paragraph (c)(4)(ii)(B)(2)(i)” and add “paragraph (c)(2)(ii)(B)(I)”;

remove paragraphs “(c)(4)(ii)(C)(3) through (7)” and add “paragraphs (c)(2)(iii)(C) through (G)” wherever it appears; remove “paragraph (c)(4)(ii)(C)(I)(ii)” and add “paragraph (c)(2)(iii)(A)(2)”;

remove “paragraph (c)(4)(ii)(C)(2)(i)” and add “paragraph (c)(2)(iii)(B)(I)” wherever it appears; remove “paragraph (c)(4)(ii)(C)(6)” and add “paragraph (c)(2)(iii)(F)”;

remove “paragraph (c)(4)(ii)(D)(I)” and add “paragraph (C)(2)(iv)(A)”;

remove “paragraph (c)(4)(ii)(A)” and add “paragraph (c)(2)(i)”;

remove “part (c)(4)(ii)(D)” and add “paragraph (c)(2)(iv)”;

and remove “paragraphs (c)(4)(ii)(I)(I) through (3)” and add “paragraphs (c)(2)(ix)(A) through (C)”.

f. In newly redesignated paragraph (c), new paragraph (c) and new paragraph (c)(1) are amended to read as follows:

**§ 217.10 Minimum capital requirements.**

\* \* \* \* \*

(c) *Supplementary leverage ratio.* (1) A Category III Board-regulated institution or advanced approaches Board-regulated institution must determine its supplementary leverage ratio in accordance with this paragraph, beginning with the calendar quarter immediately following the quarter in which the Board-regulated institution is identified as a Category III Board-regulated institution. An advanced approaches Board-regulated institution's or a Category III Board-regulated institution's supplementary leverage ratio is the ratio of its tier 1 capital to total leverage exposure, the latter which is calculated as the sum of:

\* \* \* \* \*

g. In newly redesignated paragraph (d), new introductory paragraph (d) is amended to read as follows:

**§ 217.10 Minimum capital requirements.**

\* \* \* \* \*

(d) *Advanced approaches capital ratio calculations.* An advanced approaches Board-regulated institution that has completed the parallel run process and received notification from the Board pursuant to §217.121(d) must determine its regulatory capital ratios as described in paragraphs (d)(1) through (3) of this section.

\* \* \* \* \*

11. In § 217.22, revise paragraph (c) and its footnotes, paragraphs (f), and (h) and renumber footnote 28 as footnote 30 in paragraph (d)(2), to read as follows:

**§ 217.22 Regulatory capital adjustments and deductions.**

\* \* \* \* \*

(c) *Deductions from regulatory capital related to investments in capital instruments or covered debt instruments*<sup>23</sup>—(1) *Investment in the Board-regulated institution's own capital or covered debt instruments.* A Board-regulated institution must deduct an investment in the Board-regulated institution's own capital instruments, and an advanced approaches Board-regulated institution also must deduct an investment in the Board-regulated institution's own covered debt instruments, as follows:

<sup>23</sup> The Board-regulated institution must calculate amounts deducted under paragraphs (c) through (f) of this section after it calculates the amount of ALLL or AACL, as applicable, includable in tier 2 capital under § 217.20(d)(3).

(i) A Board-regulated institution must deduct an investment in the Board-regulated institution's own common stock instruments from its common equity tier 1 capital elements to the extent such instruments are not excluded from regulatory capital under § 217.20(b)(1);

(ii) A Board-regulated institution must deduct an investment in the Board-regulated institution's own additional tier 1 capital instruments from its additional tier 1 capital elements;

(iii) A Board-regulated institution must deduct an investment in the Board-regulated institution's own tier 2 capital instruments from its tier 2 capital elements; and

(iv) An advanced approaches Board-regulated institution must deduct an investment in the institution's own covered debt instruments from its tier 2 capital elements, as applicable. If the advanced approaches Board-regulated institution does not have a sufficient amount of tier 2 capital to effect this deduction, the institution must deduct the shortfall amount from the next higher (that is, more subordinated) component of regulatory capital.

(2) *Corresponding deduction approach.* For purposes of subpart C of this part, the corresponding deduction approach is the methodology used for the deductions from regulatory capital related to reciprocal cross holdings (as described in paragraph (c)(3) of this section), investments in the capital of unconsolidated financial institutions for a Board-regulated institution that is not an advanced approaches Board-regulated institution (as described in paragraph (c)(4) of this section), non-significant investments in the capital of unconsolidated financial institutions for an advanced approaches Board-regulated institution (as described in paragraph (c)(5) of this section), and non-common stock significant investments in the capital of unconsolidated financial institutions for an advanced approaches Board-regulated institution (as described in paragraph (c)(6) of this section). Under the corresponding deduction approach, a Board-regulated institution must make deductions from the component of capital for which the underlying instrument would qualify if it were issued by the Board-regulated institution itself, as described in paragraphs (c)(2)(i) through (iii) of this section. If the Board-regulated institution does not have a sufficient amount of a specific component of capital to effect the required deduction, the shortfall must be deducted according to paragraph (f) of this section.

(i) If an investment is in the form of an instrument issued by a financial institution that is not a regulated financial institution, the Board-regulated institution must treat the instrument as:

(A) A common equity tier 1 capital instrument if it is common stock or represents the most subordinated claim in a liquidation of the financial institution; and

(B) An additional tier 1 capital instrument if it is subordinated to all creditors of the financial institution and is senior in liquidation only to common shareholders.

(ii) If an investment is in the form of an instrument issued by a regulated financial institution and the instrument does not meet the criteria for common equity tier 1, additional tier 1 or tier 2 capital instruments under § 217.20, the Board-regulated institution must treat the instrument as:

(A) A common equity tier 1 capital instrument if it is common stock included in GAAP equity or represents the most subordinated claim in liquidation of the financial institution;

(B) An additional tier 1 capital instrument if it is included in GAAP equity, subordinated to all creditors of the financial institution, and senior in a receivership, insolvency, liquidation, or similar proceeding only to common shareholders;

(C) A tier 2 capital instrument if it is not included in GAAP equity but considered regulatory capital by the primary supervisor of the financial institution; and

(D) For an advanced approaches Board-regulated institution, a tier 2 capital instrument if it is a covered debt instrument.

(iii) If an investment is in the form of a non-qualifying capital instrument (as defined in § 217.300(c)), the Board-regulated institution must treat the instrument as:

(A) An additional tier 1 capital instrument if such instrument was included in the issuer's tier 1 capital prior to May 19, 2010; or

(B) A tier 2 capital instrument if such instrument was included in the issuer's tier 2 capital (but not includable in tier 1 capital) prior to May 19, 2010.

(3) *Reciprocal cross holdings in the capital of financial institutions.* (i) A Board-regulated institution must deduct an investment in the capital of other financial institutions that it holds

reciprocally, where such reciprocal cross holdings result from a formal or informal arrangement to swap, exchange, or otherwise intend to hold each other's capital instruments, by applying the corresponding deduction approach in paragraph (c)(2) of this section.

(ii) An advanced approaches Board-regulated institution must deduct an investment in any covered debt instrument that the institution holds reciprocally with another financial institution, where such reciprocal cross holdings result from a formal or informal arrangement to swap, exchange, or otherwise intend to hold each other's capital or covered debt instruments, by applying the corresponding deduction approach in paragraph (c)(2) of this section.

(4) *Investments in the capital of unconsolidated financial institutions.* A Board-regulated institution that is not an advanced approaches Board-regulated institution must deduct its investments in the capital of unconsolidated financial institutions (as defined in § 217.2) that exceed 25 percent of the sum of the Board-regulated institution's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>24</sup> The deductions described in this section are net of associated DTLs in accordance with paragraph (e) of this section. In addition, with the prior written approval of the Board, a Board-regulated institution that underwrites a failed underwriting, for the period of time stipulated by the Board, is not required to deduct an investment in the capital of an unconsolidated financial institution pursuant to this paragraph (c) to the extent the investment is related to the failed underwriting.<sup>25</sup>

<sup>24</sup> With the prior written approval of the Board, for the period of time stipulated by the Board, a Board-regulated institution that is not an advanced approaches Board-regulated institution is not required to deduct an investment in the capital of an unconsolidated financial institution pursuant to this paragraph if the financial institution is in distress and if such investment is made for the purpose of providing financial support to the financial institution, as determined by the Board.

<sup>25</sup> Any investments in the capital of unconsolidated financial institutions that do not exceed the 25 percent threshold for investments in the capital of unconsolidated financial institutions under this section must be assigned the appropriate risk weight under subparts D or F of this part, as applicable.

*(5) Non-significant investments in the capital of unconsolidated financial institutions. (i)*

An advanced approaches Board-regulated institution must deduct its non-significant investments in the capital of unconsolidated financial institutions (as defined in § 217.2) that, in the aggregate and together with any investment in a covered debt instrument (as defined in §217.2) issued by a financial institution in which the Board-regulated institution does not have a significant investment in the capital of the unconsolidated financial institution (as defined in §217.2), exceeds 10 percent of the sum of the advanced approaches Board-regulated institution's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section (the 10 percent threshold for non-significant investments) by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>26</sup> The deductions described in this paragraph are net of associated DTLs in accordance with paragraph (e) of this section. In addition, with the prior written approval of the Board, an advanced approaches Board-regulated institution that underwrites a failed underwriting, for the period of time stipulated by the Board, is not required to deduct from capital a non-significant investment in the capital of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph (c)(5) to the extent the investment is related to the failed underwriting.<sup>27</sup> For any calculation under this paragraph (c)(5)(i), an advanced approaches Board-regulated institution may exclude the amount of an investment in a covered debt instrument under paragraphs (c)(5)(iii) or (c)(5)(iv) of this section, as applicable.

<sup>26</sup> With the prior written approval of the Board, for the period of time stipulated by the Board, an advanced approaches Board-regulated institution is not required to deduct a non-significant investment in the capital of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph if the financial institution is in distress and if such investment is made for the purpose of providing financial support to the financial institution, as determined by the Board.

<sup>27</sup> Any non-significant investment in the capital of an unconsolidated financial institution or any investment in a covered debt instrument that is not required to be deducted under this paragraph (c)(5) or otherwise under this section must be assigned the appropriate risk weight under subparts D, E, or F of this part, as applicable.

(ii) For an advanced approaches Board-regulated institution, the amount to be deducted under this paragraph (c)(5) from a specific capital component is equal to:

(A) The advanced approaches Board-regulated institution's aggregate non-significant investments in the capital of an unconsolidated financial institution and, if applicable, any investments in a covered debt instrument subject to deduction under this paragraph (c)(5), exceeding the 10 percent threshold for non-significant investments, multiplied by

(B) The ratio of the advanced approaches Board-regulated institution's aggregate non-significant investments in the capital of an unconsolidated financial institution (in the form of such capital component) to the advanced approaches Board-regulated institution's total non-significant investments in unconsolidated financial institutions, with an investment in a covered debt instrument being treated as tier 2 capital for this purpose.

(iii) For purposes of applying the deduction under paragraph (c)(5)(i) of this section, an advanced approaches Board-regulated institution that is not a global systemically important BHC or a subsidiary of a global systemically important banking organization, as defined in 12 CFR 252.2, may exclude from the deduction the amount of the Board-regulated institution's gross long position, in accordance with § 217.22(h)(2), in investments in covered debt instruments issued by financial institutions in which the Board-regulated institution does not have a



significant investment in the capital of the unconsolidated financial institutions up to an amount equal to 5 percent of the sum of the Board-regulated institution's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section, net of associated DTLs in accordance with paragraph (e) of this section.

(iv) Prior to applying the deduction under paragraph (c)(5)(i) of this section:

(A) A global systemically important BHC or a Board-regulated institution that is a subsidiary of a global systemically important BHC may designate any investment in a covered debt instrument as an excluded covered debt instrument, as defined in § 217.2.

(B) A global systemically important BHC or a Board-regulated institution that is a subsidiary of a global systemically important BHC must deduct, according to the corresponding deduction approach in paragraph (c)(2) of this section, its gross long position, calculated in accordance with paragraph (h)(2) of this section, in a covered debt instrument that was originally designated as an excluded covered debt instrument, in accordance with paragraph (c)(5)(iv)(A) above, but no longer qualifies as an excluded covered debt instrument.

(C) A global systemically important BHC or a Board-regulated institution that is a subsidiary of a global systemically important BHC must deduct according to the corresponding deduction approach in paragraph (c)(2) of this section the amount of its gross long position, calculated in accordance with paragraph (h)(2) of this section, in a direct or indirect investment in a covered debt instrument that was originally designated as an excluded covered debt instrument, in accordance with paragraph (c)(5)(iv)(A) above, and has been held for more than thirty business days.

(D) A global systemically important BHC or a Board-regulated institution that is a subsidiary of a global systemically important BHC must deduct according to the corresponding deduction approach in paragraph (c)(2) of this section its gross long position, calculated in accordance with paragraph (h)(2) of this section, of its aggregate position in excluded covered debt instruments that exceeds 5 percent of the sum of the Board-regulated institution's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section, net of associated DTLs in accordance with paragraph (e) of this section.

(6) *Significant investments in the capital of unconsolidated financial institutions that are not in the form of common stock.* If an advanced approaches Board-regulated institution has a significant investment in the capital of an unconsolidated financial institution, the advanced approaches Board-regulated institution must deduct from capital any such investment issued by the unconsolidated financial institution that is held by the Board-regulated institution other than an investment in the form of common stock, as well as any investment in a covered debt instrument issued by the unconsolidated financial institution, by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>28</sup> The deductions described in this section are net of associated DTLs in accordance with paragraph (e) of this section. In addition, with the prior written approval of the Board, for the period of time stipulated by the Board, an advanced approaches Board-regulated institution that underwrites a failed underwriting is not required to deduct the significant investment in the capital of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph (c)(6) if such investment is related to such failed underwriting.

<sup>28</sup> With prior written approval of the Board, for the period of time stipulated by the Board, an advanced approaches Board-regulated institution is not required to deduct a significant investment in the capital of an unconsolidated financial institution, including an investment in a covered debt instrument, under this paragraph (c)(6) or otherwise under this section if such investment is made for the purpose of providing financial support to the financial institution as determined by the Board.

\* \* \* \* \*

*(f) Insufficient amounts of a specific regulatory capital component to effect deductions.*

Under the corresponding deduction approach, if a Board-regulated institution does not have a sufficient amount of a specific component of capital to effect the full amount of any deduction from capital required under paragraph (d) of this section, the Board-regulated institution must deduct the shortfall amount from the next higher (that is, more subordinated) component of regulatory capital. Any investment by an advanced approaches Board-regulated institution in a covered debt instrument must be treated as an investment in the tier 2 capital for purposes of this paragraph (f). Notwithstanding any other provision of this section, a qualifying community banking organization (as defined in § 217.12) that has elected to use the community bank leverage ratio framework pursuant to § 217.12 is not required to deduct any shortfall of tier 2 capital from its additional tier 1 capital or common equity tier 1 capital.

\* \* \* \* \*

*(h) Net long position.* (1) For purposes of calculating the amount of a Board-regulated institution's investment in the Board regulated institution's own capital instrument, investment in the capital of an unconsolidated financial institution, and investment in a covered debt instrument under this section, the institution's net long position is the gross long position in the underlying instrument determined in accordance with paragraph (h)(2) of this section, as adjusted to recognize any short position by the Board-regulated institution in the same instrument subject to paragraph (h)(3) of this section.

(2) *Gross long position.* A gross long position is determined as follows:

(i) For an equity exposure that is held directly by the Board-regulated institution, the adjusted carrying value of the exposure as that term is defined in § 217.51(b);

(ii) For an exposure that is held directly and that is not an equity exposure or a securitization exposure, the exposure amount as that term is defined in § 217.2;

(iii) For each indirect exposure, the Board-regulated institution's carrying value of its investment in an investment fund or, alternatively:

(A) A Board-regulated institution may, with the prior approval of the Board, use a conservative estimate of the amount of its indirect investment in the Board-regulated institution's own capital instruments, its indirect investment in the capital of an unconsolidated financial institution, or its indirect investment in a covered debt instrument held through a position in an index, as applicable; or

(B) A Board-regulated institution may calculate the gross long position for an indirect exposure to the Board-regulated institution's own capital instruments, the capital of an unconsolidated financial institution, or a covered debt instrument by multiplying the Board-regulated institution's carrying value of its investment in the investment fund by either:

(1) The highest stated investment limit (in percent) for an investment in the Board-regulated institution's own capital instruments, an investment in the capital of an unconsolidated financial institution, or an investment in a covered debt instrument, as applicable, as stated in the prospectus, partnership agreement, or similar contract defining permissible investments of the investment fund; or

(2) The investment fund's actual holdings (in percent) of the investment in the Board-regulated institution's own capital instruments, investment in the capital of an unconsolidated financial institution, or investment in an covered debt instrument, as applicable; and

(iv) For a synthetic exposure, the amount of the Board-regulated institution's loss on the exposure if the reference capital or covered debt instrument were to have a value of zero.

(3) *Adjustments to reflect a short position.* In order to adjust the gross long position to recognize a short position in the same instrument under paragraph (h)(1) of this section, the following criteria must be met:

(i) The maturity of the short position must match the maturity of the long position, or the short position must have a residual maturity of at least one year (maturity requirement); or

(ii) For a position that is a trading asset or trading liability (whether on- or off-balance sheet) as reported on the Board-regulated institution's Call Report, for a state member bank, or FR Y-9C, for a bank holding company, savings and loan holding company, or intermediate holding company, as applicable, if the Board-regulated institution has a contractual right or obligation to sell the long position at a specific point in time and the counterparty to the contract has an obligation to purchase the long position if the Board-regulated institution exercises its right to sell, this point in time may be treated as the maturity of the long position such that the maturity of the long position and short position are deemed to match for purposes of the maturity requirement, even if the maturity of the short position is less than one year; and

(iii) For an investment in a Board-regulated institution's own capital instrument under paragraph (c)(1) of this section, an investment in the capital of an unconsolidated financial institution under paragraphs (c)(4), (c)(5), (c)(6), and (d) of this section (as applicable), and an

investment in a covered debt instrument under paragraphs (c)(1), (c)(5), and (c)(6) of this section:

(A) The Board-regulated institution may only net a short position against a long position in an investment in the Board-regulated institution's own capital instrument or own covered debt instrument under paragraph (c)(1) of this section if the short position involves no counterparty credit risk;

(B) A gross long position in an investment in the Board-regulated institution's own capital instrument, an investment in the capital of an unconsolidated financial institution, or an investment in a covered debt instrument due to a position in an index may be netted against a short position in the same index;

(C) Long and short positions in the same index without maturity dates are considered to have matching maturities; and

(D) A short position in an index that is hedging a long cash or synthetic position in an investment in the Board-regulated institution's own capital instrument, an investment in the capital instrument of an unconsolidated financial institution, or an investment in a covered debt instrument can be decomposed to provide recognition of the hedge. More specifically, the portion of the index that is composed of the same underlying instrument that is being hedged may be used to offset the long position if both the long position being hedged and the short position in the index are reported as a trading asset or trading liability (whether on- or off-balance sheet) on the Board-regulated institution's Call Report, for a state member bank, or FR Y-9C, for a bank holding company, savings and loan holding company, or intermediate holding

company, as applicable, and the hedge is deemed effective by the Board-regulated institution's internal control processes, which have not been found to be inadequate by the Board.

\* \* \* \* \*

12. Section 217.121 is amended by removing “§217.10(c)(1) through (3)” and adding “§217.10(d)(1) through (3)” wherever it appears.

\* \* \* \* \*

13. Section 217.132 is amended by removing “§217.10(c)(4)(ii)(B)(2)” and adding “§217.10(c)(2)(ii)(B)” wherever it appears.

\* \* \* \* \*

14. Section 217.303 is amended by:

- a. Removing “§217.10(c)(4)” and adding in its place “§217.10(c)”; and
- b. Removing “§217.10(c)(4)(ii)(J)(I)” and adding in its place “§217.10(c)(2)(x)(A).”

\* \* \* \* \*

## **PART 252—ENHANCED PRUDENTIAL STANDARDS (REGULATION YY)**

15. The authority citation for part 252 continues to read as follows:

Authority: 12 U.S.C. 321–338a, 481–486, 1467a, 1818, 1828, 1831n, 1831o, 1831p–l, 1831w, 1835, 1844(b), 1844(c), 3101 et seq., 3101 note, 3904, 3906–3909, 4808, 5361, 5362, 5365, 5366, 5367, 5368, 5371.

**Subpart G—External Long-term Debt Requirement, External Total Loss-absorbing Capacity Requirement and Buffer, and Restrictions on Corporate Practices for U.S. Global Systemically Important Banking Organizations**

16. In § 252.61:

a. Remove the definition of “External TLAC buffer”;

b. Add the definition of “External TLAC risk-weighted buffer” in alphabetical order to read as follows:

**§ 252.61 Definitions.**

\* \* \* \* \*

*External TLAC risk-weighted buffer* means, with respect to a global systemically important BHC, the sum of 2.5 percent, any applicable countercyclical capital buffer under 12 CFR 217.11(b) (expressed as a percentage), and the global systemically important BHC’s method 1 capital surcharge.

\* \* \* \* \*

17. In § 252.63, revise paragraphs (c)(3)(i)(C) and (c)(5)(iii)(A)(2) to read as follows:

**§ 252.63 External total loss-absorbing capacity requirement and buffer.**

\* \* \* \* \*

(c) \* \* \*

(3) \* \* \*

(i) \* \* \*



(C) The ratio (expressed as a percentage) of the global systemically important BHC's outstanding eligible external long-term debt amount plus 50 percent of the amount of unpaid principal of outstanding eligible debt securities issued by the global systemically important BHC due to be paid in, as calculated in § 252.62(b)(2), greater than or equal to 365 days (one year) but less than 730 days (two years) to total risk-weighted assets.

\* \* \* \* \*

(5) \* \* \*

(iii) \* \* \*

(A) \* \* \*

(2) The ratio (expressed as a percentage) of the global systemically important BHC's outstanding eligible external long-term debt amount plus 50 percent of the amount of unpaid principal of outstanding eligible debt securities issued by the global systemically important BHC due to be paid in in, as calculated in § 252.62(b)(2), greater than or equal to 365 days (one year) but less than 730 days (two years) to total leverage exposure.

\* \* \* \* \*

**Subpart P—Covered IHC Long-Term Debt Requirement, Covered IHC Total Loss absorbing Capacity Requirement and Buffer, and Restrictions on Corporate Practices for Intermediate Holding Companies of Global Systemically Important Foreign Banking Organizations**

18. In § 252.160, revise paragraph (b)(2) to read as follows:

**§ 252.160 Applicability.**

\* \* \* \* \*

(b) \* \* \*

(2) 1095 days (three years) after the later of the date on which:

(i) The U.S. non-branch assets of the global systemically important foreign banking organization that controls the Covered IHC equaled or exceeded \$50 billion; and

(ii) The foreign banking organization that controls the Covered IHC became a global systemically important foreign banking organization.

\* \* \* \* \*

19. In § 252.162, revise paragraph (b)(1) to read as follows:

**§ 252.162 Covered IHC long-term debt requirement.**

\* \* \* \* \*

(b) \* \* \*

(1) A Covered IHC's outstanding eligible Covered IHC long-term debt amount is the sum of:

(i) One hundred (100) percent of the amount due to be paid of unpaid principal of the outstanding eligible Covered IHC debt securities issued by the Covered IHC in greater than or equal to 730 days (two years); and

(ii) Fifty (50) percent of the amount due to be paid of unpaid principal of the outstanding eligible Covered IHC debt securities issued by the Covered IHC in greater than or equal to 365 days (one year) and less than 730 days (two years); and

(iii) Zero (0) percent of the amount due to be paid of unpaid principal of the outstanding eligible Covered IHC debt securities issued by the Covered IHC in less than 365 days (one year).

\* \* \* \* \*

20. In § 252.165, revise paragraph (d)(3)(i)(C) to read as follows:

**§ 252.165 Covered IHC total loss-absorbing capacity requirement and buffer.**

\* \* \* \* \*

(d) \* \* \*

(3) \* \* \*

(i) \* \* \*

(C) The ratio (expressed as a percentage) of the Covered IHC's outstanding eligible Covered IHC long-term debt amount plus 50 percent of the amount of unpaid principal of outstanding eligible Covered IHC debt securities issued by the Covered IHC due to be paid in, as calculated in § 252.162(b)(2), greater than or equal to 365 days (one year) but less than 730 days (two years) to total risk-weighted assets.

\* \* \* \* \*

## **Federal Deposit Insurance Corporation**

For the reasons set out in the joint preamble, the FDIC amends 12 CFR part 324 as follows.

### **PART 324 – CAPITAL ADEQUACY OF FDIC-SUPERVISED INSTITUTIONS**

\* \* \* \* \*

#### **12 CFR Part 324 Authority and Issuance**

For the reasons set out in the joint preamble, the FDIC amends 12 CFR part 324 as follows:

### **PART 324 – CAPITAL ADEQUACY OF FDIC-SUPERVISED INSTITUTIONS**

21. The authority citation for part 324 continues to read as follows:

Authority: 12 U.S.C. 1815(a), 1815(b), 1816, 1818(a), 1818(b), 1818(c), 1818(t), 1819(Tenth), 1828(c), 1828(d), 1828(i), 1828(n), 1828(o), 1831o, 1835, 3907, 3909, 4808; 5371; 5412; Pub. L. 102–233, 105 Stat. 1761, 1789, 1790 (12 U.S.C. 1831n note); Pub. L. 102–242, 105 Stat. 2236, 2355, as amended by Pub. L. 103–325, 108 Stat. 2160, 2233 (12 U.S.C. 1828 note); Pub. L. 102–242, 105 Stat. 2236, 2386, as amended by Pub. L. 102–550, 106 Stat. 3672, 4089 (12 U.S.C. 1828 note); Pub. L. 111–203, 124 Stat. 1376, 1887 (15 U.S.C. 78o–7 note), Pub. L. 115-174; section 4014, Pub. L. 116-136, 134 Stat. 281 (15 U.S.C. 9052).

22. In § 324.2:

- a. Add the definitions of “Covered debt instrument”, “Excluded covered debt instrument”, “Investment in a covered debt instrument”, in alphabetical order;
- b. Revise the definitions of “Indirect exposure” and “Synthetic exposure”;
- c. Remove “§324.10(c)(4)(ii)(J)” and add “§324.10(c)(2)(x)” in its place in the definition of “Fiduciary or custodial and safekeeping accounts”; and
- d. Remove “§324.10(c)(4)(ii)” and add “§324.10(c)(2)” in its place in the definition of “Total leverage exposure”.

The additions and revisions read as follows:

**§ 324.2        Definitions.**

\*        \*        \*        \*        \*

*Covered debt instrument* means an unsecured debt instrument that is:

(1) Issued by a global systemically important BHC, as defined in 12 CFR 217.2, and that is an eligible debt security, as defined in 12 CFR 252.61, or that is *pari passu* or subordinated to any eligible debt security issued by the global systemically important BHC; or

(2) Issued by a Covered IHC, as defined in 12 CFR 252.161, and that is an eligible Covered IHC debt security, as defined in 12 CFR 252.161, or that is *pari passu* or subordinated to any eligible Covered IHC debt security issued by the Covered IHC; or

(3) Issued by a global systemically important banking organization, as defined in 12 CFR 252.2 other than a global systemically important BHC, as defined in 12 CFR 217.2; or issued by a subsidiary of a global systemically important banking organization that is not a global systemically important BHC, other than a Covered IHC, as defined in 12 CFR 252.161; and

where,

(i) The instrument is eligible for use to comply with an applicable law or regulation requiring the issuance of a minimum amount of instruments to absorb losses or recapitalize the issuer or any of its subsidiaries in connection with a resolution, receivership, insolvency, or similar proceeding of the issuer or any of its subsidiaries; or

(ii) The instrument is *pari passu* or subordinated to any instrument described in paragraph (3)(i) of this definition; for purposes of this paragraph (3)(ii) of this definition, if the issuer may be subject to a special resolution regime, in its jurisdiction of incorporation or organization, that addresses the failure or potential failure of a financial company and any instrument described in paragraph (3)(i) of this definition is eligible under that special resolution regime to be written down or converted into equity or any other capital instrument, then an instrument is *pari passu* or subordinated to any instrument described in paragraph (3)(i) of this definition if that instrument is eligible under that special resolution regime to be written down or converted into equity or any other capital instrument ahead of or proportionally with any instrument described in paragraph (3)(i) of this definition; and

(4) Provided that, for purposes of this definition, *covered debt instrument* does not include a debt instrument that qualifies as tier 2 capital pursuant to 12 CFR 324.20(d) or that is otherwise treated as regulatory capital by the primary supervisor of the issuer.

\* \* \* \* \*

*Excluded covered debt instrument* means an investment in a covered debt instrument held by an FDIC-supervised institution that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, that:

(1) Is held in connection with market making-related activities permitted under 12 CFR 351.4, provided that a direct exposure or an indirect exposure to a covered debt instrument is held for 30 business days or less; and

(2) Has been designated as an excluded covered debt instrument by the FDIC-supervised institution that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, pursuant to 12 CFR 324.22(c)(5)(iv)(A).

\* \* \* \* \*

*Indirect exposure* means an exposure that arises from the FDIC-supervised institution's investment in an investment fund which holds an investment in the FDIC-supervised institution's own capital instrument or an investment in the capital of an unconsolidated financial institution. For an advanced approaches FDIC-supervised institution, indirect exposure also includes an investment in an investment fund that holds a covered debt instrument.

\* \* \* \* \*

*Investment in a covered debt instrument* means an FDIC-supervised institution's net long position calculated in accordance with § 324.22(h) in a covered debt instrument, including direct, indirect, and synthetic exposures to the debt instrument, excluding any underwriting positions held by the FDIC-supervised institution for five or fewer business days.

\* \* \* \* \*

*Synthetic exposure* means an exposure whose value is linked to the value of an investment in the FDIC-supervised institution's own capital instrument or to the value of an investment in the capital of an unconsolidated financial institution. For an advanced approaches FDIC-supervised

institution, synthetic exposure includes an exposure whose value is linked to the value of an investment in a covered debt instrument.

\* \* \* \* \*

23. Section 324.10 is amended as follows:

a. Redesignate paragraph (d) as (e);

b. Redesignate paragraph (c) introductory text and paragraphs (c)(1) through (3) as paragraph (d) introductory text and paragraphs (d)(1) through (3), respectively;

c. Redesignate paragraph (c)(4) as paragraph (c) as follows:

Old Paragraph	New Paragraph
(c)(4)(i)-(ii)	(c)(1)-(2)
(c)(4)(i)(A)-(B)	(c)(1)(i)-(ii)
(c)(4)(ii)(A)-(B)	(c)(2)(i)-(ii)
(c)(4)(ii)(B)(1)-(2)	(c)(2)(ii)(A)-(B)
(c)(4)(ii)(B)(1)(i)-(ii)	(c)(2)(ii)(A)(1)-(2)
(c)(4)(ii)(C)	(c)(2)(iii)
(c)(4)(ii)(C)(1)-(7)	(c)(2)(iii)(A)-(G)
(c)(4)(ii)(C)(1)(i)-(iii)	(c)(2)(iii)(A)(1)-(3)
(c)(4)(ii)(C)(2)(i)-(iii)	(c)(2)(iii)(B)(1)-(3)
(c)(4)(ii)(D)	(c)(2)(iv)
(c)(4)(ii)(D)(1)-(2)	(c)(2)(iv)(A)-(B)
(c)(4)(ii)(D)(2)(i)-(iv)	(c)(2)(iv)(B)(1)-(4)
(c)(4)(ii)(E)	(c)(2)(v)
(c)(4)(ii)(E)(1)-(3)	(c)(2)(v)(A)-(C)



(c)(4)(ii)(F)

(c)(2)(vi)

(c)(4)(ii)(F)(I)-(2)

(c)(2)(vi)(A)-(B)

(c)(4)(ii)(G)-(I)

(c)(2)(vii)-(ix)

(c)(4)(ii)(I)(I)-(5)

(c)(2)(ix)(A)-(E)

(c)(4)(ii)(J)(I)-(2)

(c)(2)(x)(A)-(B)

d. Redesignate paragraph (c)(5) as paragraph (d)(4).

e. In newly redesignated paragraph (c), remove “paragraphs (c)(4)(ii)(A) through (H)” and add “paragraphs (c)(2)(i) through (viii)”; remove “paragraph (c)(4)(ii)(I)” and add “paragraph (c)(2)(ix)” wherever it appears; remove “paragraph (c)(4)(ii)(J)” and add “paragraph (c)(2)(x)” wherever it appears; remove “paragraph (c)(4)(ii)(B)(I)” and add “paragraph (c)(2)(ii)(A)”; remove “paragraph (c)(4)(ii)(B)(2)(i)” and add “paragraph (c)(2)(ii)(B)(I)”; remove paragraphs “(c)(4)(ii)(C)(3) through (7)” and add “paragraphs (c)(2)(iii)(C) through (G)” wherever it appears; remove “paragraph (c)(4)(ii)(C)(I)(ii)” and add “paragraph (c)(2)(iii)(A)(2)”; remove “paragraph (c)(4)(ii)(C)(2)(i)” and add “paragraph (c)(2)(iii)(B)(I)” wherever it appears; remove “paragraph (c)(4)(ii)(C)(6)” and add “paragraph (c)(2)(iii)(F)”; remove “paragraph (c)(4)(ii)(D)(I)” and add “paragraph (C)(2)(iv)(A)”; remove “paragraph (c)(4)(ii)(A)” and add “paragraph (c)(2)(i)”; remove “part (c)(4)(ii)(D)” and add “paragraph (c)(2)(iv)”; and remove “paragraphs (c)(4)(ii)(I)(I) through (3)” and add “paragraphs (c)(2)(ix)(A) through (C)”.

f. In newly redesignated paragraph (c), new paragraph (c) and new paragraph (c)(1) are amended to read as follows:

**§ 324.10 Minimum capital requirements.**

\* \* \* \* \*

(c) *Supplementary leverage ratio.* (1) A Category III FDIC-supervised institution or advanced approaches FDIC-supervised institution must determine its supplementary leverage ratio in accordance with this paragraph, beginning with the calendar quarter immediately following the quarter in which the FDIC-supervised institution is identified as a Category III FDIC-supervised institution. An advanced approaches FDIC-supervised institution's or a Category III FDIC-supervised institution's supplementary leverage ratio is the ratio of its tier 1 capital to total leverage exposure, the latter which is calculated as the sum of:

\* \* \* \* \*

g. In newly redesignated paragraph (d), new introductory paragraph (d) is amended to read as follows:

**§ 324.10 Minimum capital requirements.**

\* \* \* \* \*

(d) *Advanced approaches capital ratio calculations.* An advanced approaches FDIC-supervised institution that has completed the parallel run process and received notification from the FDIC pursuant to §324.121(d) must determine its regulatory capital ratios as described in paragraphs (d)(1) through (3) of this section.

\* \* \* \* \*

24. In § 324.22, revise paragraph (c) and its footnotes, and paragraphs (f), and (h) to read as follows:

**§ 324.22 Regulatory capital adjustments and deductions.**

\* \* \* \* \*

(c) *Deductions from regulatory capital related to investments in capital instruments or covered debt instruments*<sup>23</sup>—(1) *Investment in the FDIC-supervised institution's own capital instruments.* An FDIC-supervised institution must deduct an investment in its own capital instruments, as follows:

(i) An FDIC-supervised institution must deduct an investment in the FDIC-supervised institution's own common stock instruments from its common equity tier 1 capital elements to the extent such instruments are not excluded from regulatory capital under § 324.20(b)(1);

(ii) An FDIC-supervised institution must deduct an investment in the FDIC-supervised institution's own additional tier 1 capital instruments from its additional tier 1 capital elements; and

(iii) An FDIC-supervised institution must deduct an investment in the FDIC-supervised institution's own tier 2 capital instruments from its tier 2 capital elements.

(2) *Corresponding deduction approach.* For purposes of subpart C of this part, the corresponding deduction approach is the methodology used for the deductions from regulatory capital related to reciprocal cross holdings (as described in paragraph (c)(3) of this section), investments in the capital of unconsolidated financial institutions for an FDIC-supervised institution that is not an advanced approaches FDIC-supervised institution (as described in paragraph (c)(4) of this section), non-significant investments in the capital of unconsolidated financial institutions for an advanced approaches FDIC-supervised institution (as described in

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<sup>23</sup> The FDIC-supervised institution must calculate amounts deducted under paragraphs (c) through (f) of this section after it calculates the amount of ALLL or ACL, as applicable, includable in tier 2 capital under § 324.20(d)(3).

paragraph (c)(5) of this section), and non-common stock significant investments in the capital of unconsolidated financial institutions for an advanced approaches FDIC-supervised institution (as described in paragraph (c)(6) of this section). Under the corresponding deduction approach, an FDIC-supervised institution must make deductions from the component of capital for which the underlying instrument would qualify if it were issued by the FDIC-supervised institution itself, as described in paragraphs (c)(2)(i) through (iii) of this section. If the FDIC-supervised institution does not have a sufficient amount of a specific component of capital to effect the required deduction, the shortfall must be deducted according to paragraph (f) of this section.

(i) If an investment is in the form of an instrument issued by a financial institution that is not a regulated financial institution, the FDIC-supervised institution must treat the instrument as:

(A) A common equity tier 1 capital instrument if it is common stock or represents the most subordinated claim in a liquidation of the financial institution; and

(B) An additional tier 1 capital instrument if it is subordinated to all creditors of the financial institution and is senior in liquidation only to common shareholders.

(ii) If an investment is in the form of an instrument issued by a regulated financial institution and the instrument does not meet the criteria for common equity tier 1, additional tier 1 or tier 2 capital instruments under § 324.20, the FDIC-supervised institution must treat the instrument as:

(A) A common equity tier 1 capital instrument if it is common stock included in GAAP equity or represents the most subordinated claim in liquidation of the financial institution;

(B) An additional tier 1 capital instrument if it is included in GAAP equity, subordinated to all creditors of the financial institution, and senior in a receivership, insolvency, liquidation, or similar proceeding only to common shareholders;

(C) A tier 2 capital instrument if it is not included in GAAP equity but considered regulatory capital by the primary supervisor of the financial institution; and

(D) For an advanced approaches FDIC-supervised institution, a tier 2 capital instrument if it is a covered debt instrument.

(iii) If an investment is in the form of a non-qualifying capital instrument (as defined in § 324.300(c)), the FDIC-supervised institution must treat the instrument as:

(A) An additional tier 1 capital instrument if such instrument was included in the issuer's tier 1 capital prior to May 19, 2010; or

(B) A tier 2 capital instrument if such instrument was included in the issuer's tier 2 capital (but not includable in tier 1 capital) prior to May 19, 2010.

(3) *Reciprocal cross holdings in the capital of financial institutions.* (i) An FDIC-supervised institution must deduct an investment in the capital of other financial institutions that it holds reciprocally, where such reciprocal cross holdings result from a formal or informal arrangement to swap, exchange, or otherwise intend to hold each other's capital instruments, by applying the corresponding deduction approach in paragraph (c)(2) of this section.

(ii) An advanced approaches FDIC-supervised institution must deduct an investment in any covered debt instrument that the institution holds reciprocally with another financial institution, where such reciprocal cross holdings result from a formal or informal arrangement to swap, exchange, or otherwise intend to hold each other's capital or covered debt instruments, by applying the corresponding deduction approach in paragraph (c)(2) of this section.

(4) *Investments in the capital of unconsolidated financial institutions.* An FDIC-supervised institution that is not an advanced approaches FDIC-supervised institution must deduct its investments in the capital of unconsolidated financial institutions (as defined in § 324.2) that

exceed 25 percent of the sum of the FDIC-supervised institution's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>24</sup> The deductions described in this section are net of associated DTLs in accordance with paragraph (e) of this section. In addition, with the prior written approval of the FDIC, an FDIC-supervised institution that underwrites a failed underwriting, for the period of time stipulated by the FDIC, is not required to deduct an investment in the capital of an unconsolidated financial institution pursuant to this paragraph (c) to the extent the investment is related to the failed underwriting.<sup>25</sup>

*(5) Non-significant investments in the capital of unconsolidated financial institutions. (i)*

An advanced approaches FDIC-supervised institution must deduct its non-significant investments in the capital of unconsolidated financial institutions (as defined in § 324.2) that, in the aggregate and together with any investment in a covered debt instrument (as defined in § 324.2) issued by a financial institution in which the FDIC-supervised institution does not have a significant investment in the capital of the unconsolidated financial institution (as defined in § 324.2), exceeds 10 percent of the sum of the advanced approaches FDIC-supervised institution's

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<sup>24</sup> With the prior written approval of the FDIC, for the period of time stipulated by the FDIC, an FDIC-supervised institution that is not an advanced approaches FDIC-supervised institution, is not required to deduct an investment in the capital of an unconsolidated financial institution pursuant to this paragraph if the financial institution is in distress and if such investment is made for the purpose of providing financial support to the financial institution, as determined by the FDIC.

<sup>25</sup> Any investments in the capital of an unconsolidated financial institution that do not exceed the 25 percent threshold for investments in the capital of unconsolidated financial institutions under this section must be assigned the appropriate risk weight under subparts D or F of this part, as applicable.

common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section (the 10 percent threshold for non-significant investments) by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>26</sup> The deductions described in this paragraph are net of associated DTLs in accordance with paragraph (e) of this section. In addition, with the prior written approval of the FDIC, an advanced approaches FDIC-supervised institution that underwrites a failed underwriting, for the period of time stipulated by the FDIC, is not required to deduct from capital a non-significant investment in the capital of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph (c)(5) to the extent the investment is related to the failed underwriting.<sup>27</sup> For any calculation under this paragraph (c)(5)(i), an advanced approaches FDIC-supervised institution may exclude the amount of an investment in a covered debt instrument under paragraphs (c)(5)(iii) or (c)(5)(iv) of this section, as applicable.

(ii) For an advanced approaches FDIC-supervised institution, the amount to be deducted under this paragraph (c)(5) from a specific capital component is equal to:

(A) The advanced approaches FDIC-supervised institution's aggregate non-significant investments in the capital of an unconsolidated financial institution and, if applicable, any

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<sup>26</sup> With the prior written approval of the FDIC, for the period of time stipulated by the FDIC, an advanced approaches FDIC-supervised institution is not required to deduct a non-significant investment in the capital of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph if the financial institution is in distress and if such investment is made for the purpose of providing financial support to the financial institution, as determined by the FDIC.

<sup>27</sup> Any non-significant investment in the capital of an unconsolidated financial institution or any investment in a covered debt instrument that is not required to be deducted under this paragraph (c)(5) or otherwise under this section must be assigned the appropriate risk weight under subparts D, E, or F of this part, as applicable.

investments in a covered debt instrument subject to deduction under this paragraph (c)(5), exceeding the 10 percent threshold for non-significant investments, multiplied by

(B) The ratio of the advanced approaches FDIC-supervised institution's aggregate non-significant investments in the capital of an unconsolidated financial institution (in the form of such capital component) to the advanced approaches FDIC-supervised institution's total non-significant investments in unconsolidated financial institutions, with an investment in a covered debt instrument being treated as tier 2 capital for this purpose.

(iii) For purposes of applying the deduction under paragraph (c)(5)(i) of this section, an advanced approaches FDIC-supervised institution that is not a subsidiary of a global systemically important banking organization, as defined in 12 CFR 252.2, may exclude from the deduction the amount of the FDIC-supervised institution's gross long position, in accordance with § 324.22(h)(2), in investments in covered debt instruments issued by financial institutions in which the FDIC-supervised institution does not have a significant investment in the capital of the unconsolidated financial institutions up to an amount equal to 5 percent of the sum of the FDIC-supervised institution's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section, net of associated DTLs in accordance with paragraph (e) of this section.

(iv) Prior to applying the deduction under paragraph (c)(5)(i) of this section:

(A) An FDIC-supervised institution that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, may designate any investment in a covered debt instrument as an excluded covered debt instrument, as defined in § 324.2.



(B) An FDIC-supervised institution that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, must deduct, according to the corresponding deduction approach in paragraph (c)(2) of this section, its gross long position, calculated in accordance with paragraph (h)(2) of this section, in a covered debt instrument that was originally designated as an excluded covered debt instrument, in accordance with paragraph (c)(5)(iv)(A) above, but no longer qualifies as an excluded covered debt instrument.

(C) An FDIC-supervised institution that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, must deduct according to the corresponding deduction approach in paragraph (c)(2) of this section the amount of its gross long position, calculated in accordance with paragraph (h)(2) of this section, in a direct or indirect investment in a covered debt instrument that was originally designated as an excluded covered debt instrument, in accordance with paragraph (c)(5)(iv)(A) above, and has been held for more than thirty business days.

(D) An FDIC-supervised institution that is a subsidiary of a global systemically important BHC, as defined in 12 CFR 252.2, must deduct according to the corresponding deduction approach in paragraph (c)(2) of this section its gross long position, calculated in accordance with paragraph (h)(2) of this section, of its aggregate position in excluded covered debt instruments that exceeds 5 percent of the sum of the FDIC-supervised institution's common equity tier 1 capital elements minus all deductions from and adjustments to common equity tier 1 capital elements required under paragraphs (a) through (c)(3) of this section, net of associated DTLs in accordance with paragraph (e) of this section.

(6) *Significant investments in the capital of unconsolidated financial institutions that are not in the form of common stock.* If an advanced approaches FDIC-supervised institution has a

significant investment in the capital of an unconsolidated financial institution, the advanced approaches FDIC-supervised institution must deduct from capital any such investment issued by the unconsolidated financial institution that is held by the FDIC-supervised institution other than an investment in the form of common stock, as well as any investment in a covered debt instrument issued by the unconsolidated financial institution, by applying the corresponding deduction approach in paragraph (c)(2) of this section.<sup>28</sup> The deductions described in this section are net of associated DTLs in accordance with paragraph (e) of this section. In addition, with the prior written approval of the FDIC, for the period of time stipulated by the FDIC, an advanced approaches FDIC-supervised institution that underwrites a failed underwriting is not required to deduct the significant investment in the capital of an unconsolidated financial institution or an investment in a covered debt instrument pursuant to this paragraph (c)(6) if such investment is related to such failed underwriting.

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*(f) Insufficient amounts of a specific regulatory capital component to effect deductions.*

Under the corresponding deduction approach, if an FDIC-supervised institution does not have a sufficient amount of a specific component of capital to effect the full amount of any deduction from capital required under paragraph (d) of this section, the FDIC-supervised institution must deduct the shortfall amount from the next higher (that is, more subordinated) component of regulatory capital. Any investment by an advanced approaches FDIC-supervised institution in a

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<sup>28</sup> With prior written approval of the FDIC, for the period of time stipulated by the FDIC, an advanced approaches FDIC-supervised institution is not required to deduct a significant investment in the capital of an unconsolidated financial institution, including an investment in a covered debt instrument, under this paragraph (c)(6) or otherwise under this section if such investment is made for the purpose of providing financial support to the financial institution as determined by the FDIC.

covered debt instrument must be treated as an investment in the tier 2 capital for purposes of this paragraph (f). Notwithstanding any other provision of this section, a qualifying community banking organization (as defined in § 324.12) that has elected to use the community bank leverage ratio framework pursuant to § 324.12 is not required to deduct any shortfall of tier 2 capital from its additional tier 1 capital or common equity tier 1 capital.

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(h) *Net long position.* (1) For purposes of calculating the amount of an FDIC-supervised institution's investment in the FDIC-supervised institution's own capital instrument, investment in the capital of an unconsolidated financial institution, and investment in a covered debt instrument under this section, the institution's net long position is the gross long position in the underlying instrument determined in accordance with paragraph (h)(2) of this section, as adjusted to recognize any short position by the FDIC-supervised institution in the same instrument subject to paragraph (h)(3) of this section.

(2) *Gross long position.* A gross long position is determined as follows:

(i) For an equity exposure that is held directly by the FDIC-supervised institution, the adjusted carrying value of the exposure as that term is defined in § 324.51(b);

(ii) For an exposure that is held directly and that is not an equity exposure or a securitization exposure, the exposure amount as that term is defined in § 324.2;

(iii) For each indirect exposure, the FDIC-supervised institution's carrying value of its investment in an investment fund or, alternatively:

(A) An FDIC-supervised institution may, with the prior approval of the FDIC, use a conservative estimate of the amount of its indirect investment in the FDIC-supervised institution's own capital instruments, its indirect investment in the capital of an unconsolidated

financial institution, or its indirect investment in a covered debt instrument held through a position in an index, as applicable; or

(B) An FDIC-supervised institution may calculate the gross long position for an indirect exposure to the FDIC-supervised institution's own capital instruments, the capital of an unconsolidated financial institution, or a covered debt instrument by multiplying the FDIC-supervised institution's carrying value of its investment in the investment fund by either:

(1) The highest stated investment limit (in percent) for an investment in the FDIC-supervised institution's own capital instruments, an investment in the capital of an unconsolidated financial institution, or an investment in a covered debt instrument, as applicable, as stated in the prospectus, partnership agreement, or similar contract defining permissible investments of the investment fund; or

(2) The investment fund's actual holdings (in percent) of the investment in the FDIC-supervised institution's own capital instruments, investment in the capital of an unconsolidated financial institution, or investment in an covered debt instrument, as applicable; and

(iv) For a synthetic exposure, the amount of the FDIC-supervised institution's loss on the exposure if the reference capital or covered debt instrument were to have a value of zero.

(3) *Adjustments to reflect a short position.* In order to adjust the gross long position to recognize a short position in the same instrument under paragraph (h)(1) of this section, the following criteria must be met:

(i) The maturity of the short position must match the maturity of the long position, or the short position must have a residual maturity of at least one year (maturity requirement); or

(ii) For a position that is a trading asset or trading liability (whether on- or off-balance sheet) as reported on the FDIC-supervised institution's Call Report, if the FDIC-supervised

institution has a contractual right or obligation to sell the long position at a specific point in time and the counterparty to the contract has an obligation to purchase the long position if the FDIC-supervised institution exercises its right to sell, this point in time may be treated as the maturity of the long position such that the maturity of the long position and short position are deemed to match for purposes of the maturity requirement, even if the maturity of the short position is less than one year; and

(iii) For an investment in an FDIC-supervised institution's own capital instrument under paragraph (c)(1) of this section, an investment in the capital of an unconsolidated financial institution under paragraphs (c)(4), (c)(5), (c)(6), and (d) of this section (as applicable), and an investment in a covered debt instrument under paragraphs (c)(1), (c)(5), and (c)(6) of this section:

(A) The FDIC-supervised institution may only net a short position against a long position in an investment in the FDIC-supervised institution's own capital instrument under paragraph (c)(1) of this section if the short position involves no counterparty credit risk;

(B) A gross long position in an investment in the FDIC-supervised institution's own capital instrument, an investment in the capital of an unconsolidated financial institution, or an investment in a covered debt instrument due to a position in an index may be netted against a short position in the same index;

(C) Long and short positions in the same index without maturity dates are considered to have matching maturities; and

(D) A short position in an index that is hedging a long cash or synthetic position in an investment in the FDIC-supervised institution's own capital instrument, an investment in the capital instrument of an unconsolidated financial institution, or an investment in a covered debt

instrument can be decomposed to provide recognition of the hedge. More specifically, the portion of the index that is composed of the same underlying instrument that is being hedged may be used to offset the long position if both the long position being hedged and the short position in the index are reported as a trading asset or trading liability (whether on- or off-balance sheet) on the FDIC-supervised institution's Call Report, and the hedge is deemed effective by the FDIC-supervised institution's internal control processes, which have not been found to be inadequate by the FDIC.

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25. Section 324.121 is amended by removing “§324.10(c)(1) through (3)” and adding “§324.10(d)(1) through (3)” wherever it appears.

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26. Section 324.132 is amended by removing “§324.10(c)(4)(ii)(B)(2)” and adding “§324.10(c)(2)(ii)(B)” wherever it appears.

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27. Section 324.304 is amended by:

- a. Removing “§324.10(c)(4)” and adding in its place “§324.10(c)”; and
- b. Removing “§324.10(c)(4)(ii)(J)(I)” and adding in its place “§324.10(c)(2)(x)(A).”

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*Brian P. Brooks*  
*Acting Comptroller of the Currency*

By order of the Board of Governors of the Federal Reserve System, [October XX, 2020].

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**Ann E. Misback,**  
*Secretary of the Board.*



Dated at Washington, DC on or about [October, XX, 2020].

By order of the Board of Directors.  
Federal Deposit Insurance Corporation.

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**James P. Sheesley,**  
*Assistant Executive Secretary.*