# SCHEDULE RC-R -- REGULATORY CAPITAL

## General Instructions

The extent to which banks must complete this Schedule RC-R depends on their size and, for smaller banks, their capital level.

All banks that reported total assets of less than $1 billion in their Reports of Condition for June 30 of the previous year must complete item 1 of this schedule each quarter. Item 1 consists of a "YES" or "NO" question which asks whether a simplified risk-based capital calculation performed by the reporting bank resulted in a ratio greater than or equal to eight percent. Banks with assets of less than $1 billion must complete the remainder of Schedule RC-R in each quarter when their response to item 1 is a "NO." Banks whose response to item 1 is a "YES" must complete only items 2 and 3 of Schedule RC-R for that quarter. A "NO" response to item 1 does not necessarily mean that the bank's actual risk-based capital ratio is less than eight percent or that the bank is not in compliance with the risk-based capital guidelines.

All banks that reported total assets of $1 billion or more in their Reports of Condition for June 30 of the previous year must complete this entire schedule (except for item 1) each quarter.

Under the banking agencies' risk-based capital guidelines, assets and credit equivalent amounts of off-balance sheet items are assigned to one of several broad risk categories according to the obligor, or, if relevant, the guarantor or the nature of the collateral. The aggregate dollar amount in each risk category is then multiplied by the risk weight associated with that category. The resulting weighted values from each of the risk categories are added together, and generally this sum is the bank's total risk weighted assets which comprises the denominator of the risk-based capital ratio.

Risk weights for all off-balance sheet items are determined by a two-step process. First, the "credit equivalent amount" of an off-balance sheet item is determined, in most cases by multiplying the **face value or notional amount of the** off-balance sheet item by a credit conversion factor. Second, the credit equivalent amount is treated like a balance sheet asset and generally is assigned to the appropriate risk category according to the obligor or, if relevant, the guarantor or the nature of the collateral. A summary of the credit conversion factors for off-balance sheet items is presented below.

In general, if a particular asset or off-balance sheet item has features that could place it in more than one risk category, it is assigned to the category that has the lowest risk weight. For example, a holding of a U.S. municipal revenue bond that is fully guaranteed by a U.S. bank would be assigned the 20 percent risk weight appropriate to claims guaranteed by U.S. banks, rather than the 50 percent risk weight appropriate to U.S. municipal revenue bonds.

At each bank's option, assets and the credit equivalent amounts of off-balance sheet items that are assigned to a risk weight category of less than 100 percent may be included in the amount reported for a higher risk weight category than the risk weight category to which the asset or credit equivalent amount of the off-balance sheet item would otherwise be assigned.

For risk-based capital purposes, the term "claim" refers to loans to, securities issued by, balances due from, accrued interest receivable from, and all other claims against the various entities with which the reporting bank conducts its business.

Several of the risk weight categories refer to claims against obligors in OECD countries or in non-OECD countries. The following countries are members of the Organization for Economic Cooperation and Development (OECD):

General Instructions (cont.)

Australia, Austria, Belgium, Canada, the Czech Republic, Denmark, the Federal Republic of Germany, Finland, France, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Poland, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States.

In addition, for purposes of risk-based capital, Saudi Arabia should be treated as an OECD country since it has concluded special lending arrangements with the International Monetary Fund associated with the Fund's General Arrangements to Borrow. All other countries should be treated as non-OECD countries.

If a reporting bank has conveyed risk participations in bankers acceptances, standby letters of credit, and commitments, it may segregate the amounts conveyed from the total outstanding amount. The bank may then risk weight the amounts conveyed according to the guarantors (i.e., the parties that have acquired the conveyances) separately from the amounts retained if this results in a lower risk weight for the amounts conveyed.

When assets have been transferred with recourse, the amount of risk-based capital required to be maintained to support this exposure may not exceed the maximum amount of recourse for which the transferring institution is contractually liable under the recourse agreement. This rule applies to recourse transactions in which a bank contractually limits its recourse exposure to less than the full effective minimum risk-based capital requirement for the assets transferred -- generally, four percent for first lien residential mortgage loans and eight percent for most other assets. These types of asset transfers are referred to as low level recourse transactions. The reporting of such transactions in Schedule RC-R is discussed below in the section on "Treatment of Low Level Recourse Transactions."

The sum of items 4, 5, 6, and 7, after each has been multiplied by the appropriate risk weight percentage, will not necessarily correspond to the reporting bank's actual risk weighted assets. This is because this sum has not been adjusted for the portion of the allowance for loan and lease losses in excess of the amount permitted to be included in capital and for any allocated transfer risk reserve.

Credit Conversion Factors for Off-Balance Sheet Items -- A summary of the credit conversion factors follows. For further information on these factors, refer to the risk-based capital guidelines.

Off-balance sheet items subject to a 100 percent conversion factor:

(1) Direct credit substitutes, including general guarantees of indebtedness and guarantee-type instruments, such as financial standby letters of credit.
(2) Risk participations acquired in bankers acceptances and in direct credit substitutes such as financial standby letters of credit.
(3) Sale and repurchase agreements and assets sold with recourse, if not included on the balance sheet, except low level recourse transactions and small business obligations transferred with recourse under Section 208 of the Riegle Community Development and Regulatory Improvement Act of 1994, each of which is discussed below.
(4) Forward agreements/contingent obligations to purchase assets with drawdown certain.
(5) Securities lent, if the lending bank is exposed to risk of loss.

Off-balance sheet items subject to a 50 percent conversion factor:

(1) Transaction-related contingencies, including performance standby letters of credit, shipside guarantees, bid bonds, performance bonds, and warranties.
(2) Unused portions of commitments with an original maturity exceeding one year, including underwriting commitments and commercial credit lines.
(3) Revolving underwriting facilities (RUFs), note issuance facilities (NIFs), and other similar arrangements, regardless of maturity.

## General Instructions (cont.)

Off-balance sheet items subject to a 20 percent conversion factor:
(1) Short-term, self-liquidating, trade-related contingencies, including commercial letters of credit.

Off-balance sheet items subject to a zero percent conversion factor:
(1) Unused portions of commitments with an original maturity of one year or less.
(2) Unused portions of commitments (regardless of maturity) which are unconditionally cancellable at any time, provided a separate credit decision is made before each drawing.

For information on the treatment of credit derivatives for risk-based capital and supervisory purposes, banks should refer to the supervisory guidance issued by their primary federal bank regulatory agency.

Credit conversion process for off-balance sheet interest rate, foreign exchange, equity derivative, and commodity and other contracts -- In general, to calculate the credit equivalent amount for such contracts, a bank should, for each contract, add (1) the mark-to-market value (only if a positive value) of the contract (i.e., the contract's current credit exposure or replacement cost), and (2) an estimate of the potential future increase in credit exposure over the remaining life of the instrument. For risk-based capital purposes, potential future credit exposure of a contract is determined by multiplying the notional principal amount of the contract (even if the contract had a negative mark-to-market value) by the appropriate credit conversion factor from the chart presented below. However, under the banking agencies' risk-based capital standards and for purposes of Schedule RC-R, the existence of a legally enforceable bilateral netting agreement between the reporting bank and a counterparty may be taken into consideration when determining both the current credit exposure and the potential future exposure of off-balance sheet derivative contracts. For further information on the treatment of bilateral netting agreements covering off-balance sheet derivative contracts, refer to the risk-based capital standards issued by the reporting bank's primary federal supervisory authority.

| Remaining maturity | Interest rate contracts | Foreign exchange and gold contracts | Equity derivative contracts | Precious metals contracts (except gold) | Other commodity contracts |
|---|---|---|---|---|---|
| One year or less | 0.0% | 1.0% | 6.0% | 7.0% | 10.0% |
| More than one year through five years | 0.5% | 5.0% | 8.0% | 7.0% | 12.0% |
| More than five years | 1.5% | 7.5% | 10.0% | 8.0% | 15.0% |

The types of off-balance sheet derivative contracts that are excluded in whole or in part from the credit conversion process are discussed below in the section on "Treatment of Off-Balance Sheet Interest Rate, Foreign Exchange, Equity Derivative, and Commodity and Other Contracts."

Treatment of Commitments -- Under the risk-based capital guidelines, the unused portion of commitments (facilities) with an original maturity of one year or less or which are unconditionally cancellable (without cause) at any time by the bank, provided a separate credit decision is made before each drawing, have a zero percent conversion factor. The unused portion of such commitments should be excluded from items 4 through 7 of Schedule RC-R. "Original maturity" is defined as the length of time between the date a commitment is issued and the date of maturity, or the earliest date on which the bank (1) is scheduled to (and as a normal practice actually does) review the facility to determine whether or not it should be extended and (2) can unconditionally cancel the commitment.

## General Instructions (cont.)

For commitments providing for increases in the dollar amount of the commitment, the amount to be converted to an on-balance sheet credit equivalent amount and risk weighted is the maximum dollar amount that the bank is obligated to advance at anytime during the life of the commitment. This includes seasonal commitments where the dollar amount of the commitment increases during the customer's peak business period. In addition, this risk-based capital treatment applies to long-term commitments that contain short-term options which, for a fee, allow the customer to increase the dollar amount of the commitment. Until the short-term option has expired, the reporting bank must convert and risk weight the amount which it is obligated to lend if the option is exercised. After the expiration of a short-term option which has not been exercised, the unused portion of the original amount of the commitment is to be used in the credit conversion process.

In the case of consumer home equity or mortgage lines of credit secured by liens on 1-4 family residential properties, a bank is deemed able to unconditionally cancel the commitment if, at its option, it can prohibit additional extensions of credit, reduce the credit line, and terminate the commitment to the full extent permitted by relevant federal law. Retail credit cards and related plans are defined to be short-term commitments that should be converted at zero percent and excluded from items 4 through 7 of Schedule RC-R if the bank has the unconditional right to cancel the line of credit at any time, in accordance with applicable law.

<u>Treatment of Off-Balance Sheet Interest Rate, Foreign Exchange, Equity Derivative, and Commodity and Other Contracts</u> -- In general, only the credit equivalent amounts of those off-balance sheet interest rate, foreign exchange, equity derivative, and commodity and other contracts <u>covered</u> under the risk-based capital guidelines are to be reported in Schedule RC-R. The maximum risk weight to be applied to the credit equivalent amount of such contracts is 50 percent. The credit equivalent amounts calculated for interest rate, foreign exchange, equity derivative, and commodity and other swaps, forwards, purchased option contracts, when-issued securities, and forward deposits accepted as outlined in the risk-based capital guidelines, and any margin accounts associated with such contracts, are to be included in items 4 through 6 depending upon the risk weights accorded the transactions due to the counterparty, or, if relevant, the nature of any collateral or guarantees.

Purchased options held by the reporting bank that are traded on an exchange are to be included in the calculation of the risk-based capital ratio <u>unless</u> such options are subject to a daily variation margin. Variation margin is defined as the gain or loss on open positions, calculated by marking to market at the end of each trading day. Such gain or loss is credited or debited by the clearing house to each clearing member's account, and by members to their customers' accounts.

<u>Exclude</u> from the credit conversion process and from items 4 through 6 of Schedule RC-R: (1) interest rate, foreign exchange, equity derivative, and commodity and other contracts traded on exchanges that require daily payment of variation margin, (2) foreign exchange contracts with an original maturity of fourteen calendar days or less, and (3) all written option contracts except for those that are, in substance, financial guarantees. (However, see the instructions to Schedule RC-R, Memorandum item 1, concerning bilateral netting agreements.) In general, also <u>exclude</u> from items 4 through 6 the on-balance sheet asset values (or portions thereof) of all interest rate, foreign exchange, equity derivative, and commodity and other contracts subject to risk-based capital; these amounts are to be reported in item 8 of this schedule. For further information, see the instructions to Schedule RC-R, item 8.

If a written option contract acts as a financial guarantee, then it will be treated as a direct credit substitute for purposes of risk-based capital and Schedule RC-R. An example of such a contract occurs when the reporting bank writes a put option to a second bank which has a loan to a third

**General Instructions (cont.)**

party. The strike price would be the equivalent of the par value of the loan. If the credit quality of the loan deteriorates, thereby reducing the value of the loan to the second bank, the reporting bank would be required by the second bank to take the loan onto its books.

Treatment of Low Level Recourse Transactions -- The banking agencies' risk-based capital standards provide that the amount of risk-based capital that must be maintained for assets transferred with recourse should not exceed the maximum amount of recourse for which a bank is contractually liable under the recourse agreement. This rule, known as the low level recourse rule, applies to transactions accounted for as sales under generally accepted accounting principles (GAAP) in which a bank contractually limits its risk of loss or recourse exposure to less than the full effective minimum risk-based capital requirement for the assets transferred -- generally, four percent for qualifying first lien 1-to-4 family residential mortgages and eight percent for most other assets. Low level recourse transactions may arise when a bank sells or securitizes assets and:

- Uses contractual cash flows (e.g., interest-only strips receivable and so-called "spread accounts"), retained subordinated interests, retained securities (e.g., collateral invested amounts or cash collateral accounts), or other assets as credit enhancements. When a credit enhancement is carried as an asset on the bank's Call Report balance sheet in accordance with GAAP and the low level recourse rule applies, the on-balance sheet asset amount of the credit enhancement should be reported in Schedule RC-R, item 8. The "maximum contractual dollar amount of recourse exposure" for the transaction is this on-balance sheet asset amount on a net of tax basis, when appropriate.

OR

- Provides limited recourse to purchasers of the assets sold, but does not use on-balance sheet assets as credit enhancements. In this situation, the "maximum contractual dollar amount of recourse exposure" for a transaction is the maximum contractual amount of the bank's recourse exposure as of the report date, less the balance of any associated recourse liability account established in accordance with GAAP and reported in Schedule RC, item 20, "Other liabilities."

Banks that have entered into low level recourse transactions should report these transactions in Schedule RC-R using either the "direct reduction method" or the "gross-up method" in accordance with the following guidance. When using the "gross-up method," a bank includes an amount in its risk-weighted assets (the denominator of its risk-based capital ratios) for its "maximum contractual dollar amount of recourse exposure" that is calculated under the assumption that the bank's total risk-based capital ratio equals the 8 percent minimum requirement. In contrast, when using the "direct reduction method," a bank includes an institution-specific amount in its risk-weighted assets for its "maximum contractual dollar amount of recourse exposure" that is calculated using the actual amount of the bank's total risk-based capital. This institution-specific calculation produces the effect of directly reducing Tier 1 and total risk-based capital by the "maximum contractual dollar amount of recourse exposure" without lowering the bank's Tier 1 leverage capital ratio. For a bank whose risk-based capital ratios exceed the required minimums, it is normally preferable to use the "direct reduction method."

- If the bank chooses to use the "direct reduction method," the "maximum contractual dollar amount of recourse exposure," as defined above, should be reported in Schedule RC-R, item 3.e. In addition, the bank should report as a credit equivalent amount in Schedule RC-R, item 7.b, column B, an "institution-specific add-on factor" for its low level recourse exposure. The amount of this factor also should be included in the "net risk-weighted assets" that the bank reports in Schedule RC-R, item 3.d.(1). The "institution-specific add-on factor," which is independent of the risk weight category of the assets to which the recourse applies, is calculated as follows:

**General Instructions (cont.)**

$$F = \frac{C \times A}{C - R} - A$$

where F = institution-specific add-on factor;
C = total risk-based capital (as reported in Schedule RC-R, item 3.b);
A = net risk-weighted assets excluding low level recourse exposures; and
R = maximum contractual dollar amount of recourse exposure in low level recourse transactions (as reported in Schedule RC-R, item 3.e)

For purposes of calculating the amount of the bank's total risk-based capital to be used in the preceding formula (C in the formula) and to be reported in Schedule RC-R, item 3.b, the bank should determine the Tier 2 capital limit on the allowance for loan and lease losses by multiplying its "maximum contractual dollar amount of recourse exposure" (R in the preceding formula, as defined in these instructions) by 12.5 and adding this product to its gross risk-weighted assets excluding low level recourse exposures. This adjusted gross risk-weighted-assets figure multiplied by 1.25 percent is the bank's Tier 2 capital limit on the allowance for loan and lease losses. Once this limit on the allowance has been calculated, the limit is fixed at this amount. This limit should not be changed after the bank calculates the actual amount of its net risk-weighted assets excluding low level recourse exposures (A in the preceding formula) or its institution-specific add-on factor for low level recourse under the "direct reduction method" (F in the preceding formula). This means that a bank will measure its Tier 2 capital and its total risk-based capital prior to its application of the "direct reduction method" and will not recalculate these two amounts once the add-on factor is known.

- If the bank chooses to use the "gross-up method," the "maximum contractual dollar amount of recourse exposure" for a transaction, as defined above, should be multiplied by a factor of 12.5, 25, or 62.5 according to whether the assets sold would be assigned to the 100 percent, 50 percent, or 20 percent risk weight category, respectively. The resulting dollar amount should be reported as an off-balance sheet credit equivalent amount in column B of Schedule RC-R in the item (item 7.b, 6.b, or 5.b) appropriate to the risk weight category of the assets sold.

For example, a bank has sold $2 million in first lien residential mortgages subject to two percent recourse. The bank has removed the $2 million in mortgages from its Call Report balance sheet and, in accordance with GAAP, has also established a recourse liability account with a balance of $10,000. The maximum amount for which the bank is liable is $40,000. The mortgages qualify for a 50 percent risk weight and the bank's recourse exposure is less than the $80,000 minimum risk-based capital requirement for these assets sold with recourse. Thus, the low level recourse rule applies. The "maximum contractual dollar amount of recourse exposure" for this transaction is $30,000, the $40,000 maximum contractual amount of the bank's recourse exposure as of the report date, less the $10,000 balance of the recourse liability account for this transaction. The bank has gross risk-weighted assets excluding low level recourse exposures of $100 million, Tier 1 capital of $8 million, an allowance for loan and lease losses of $1.1 million, and other qualifying Tier 2 capital components of $1.4 million.

- If the bank chooses to use the "direct reduction method," the bank would report $30,000 -- its "maximum contractual dollar amount of recourse exposure" -- in Schedule RC-R, item 3.e, and would use this amount to calculate its institution-specific add-on factor using the formula provided above. To determine the Tier 2 capital limit for the bank's allowance for loan and lease losses, the bank would first add $375,000 ($30,000 -- its "maximum contractual recourse exposure" -- multiplied by 12.5) to its $100 million of gross risk-weighted assets excluding low level recourse exposures. Its Tier 2 capital limit for the allowance would be $1,254,688 ($100,375,000 -- its

## General Instructions (cont.)

adjusted gross risk-weighted assets -- multiplied by 1.25 percent -- the limit for the allowance). Since the bank's $1.1 million allowance is less than its Tier 2 capital limit for the allowance, the bank would report an "excess allowance for loan and lease losses" of $0 in Schedule RC-R, item 3.c. The bank's total risk-based capital is $10.5 million and its net risk-weighted assets excluding low level recourse exposures are $100 million. Based on the facts in the example, the bank calculates that its institution-specific add-on factor is $286,533. The bank would report the amount of this add-on factor as a credit equivalent amount in Schedule RC-R, item 7.b, column B, and also include this amount in the "net risk-weighted assets" that it reports in Schedule RC-R, item 3.d.(1).

- If the bank chooses to use the "gross-up method," the bank would report $750,000 as a credit equivalent amount in Schedule RC-R, item 6.b, column B ($30,000 -- its "maximum contractual dollar amount of recourse exposure" -- multiplied by 25 -- the factor for assets that qualify for a 50 percent risk weight). Because the $2 million in mortgages sold have been removed from the balance sheet, the difference between the $750,000 credit equivalent amount and the $2 million is not reported in Schedule RC-R. In addition, because the $750,000 credit equivalent amount is assigned to the 50 percent risk category, the bank would include $375,000 ($750,000 multiplied by 50 percent) in its gross risk-weighted assets for purposes of determining the Tier 2 capital limit for the allowance for loan and lease losses and in the "net risk-weighted assets" that it reports in Schedule RC-R, item 3.d.(1).

Treatment of Small Business Obligations Transferred with Recourse Under Section 208 of the Riegle Community Development and Regulatory Improvement Act of 1994 -- A "qualifying institution" that transfers small business loans and leases on personal property (small business obligations) with recourse in a transaction that qualifies as a sale under generally accepted accounting principles (GAAP) must maintain risk-based capital only against the amount of recourse retained, provided the institution establishes a recourse liability account that is sufficient under GAAP. Only loans and leases to businesses that meet the criteria for a small business concern established by the Small Business Administration under Section 3(c) of the Small Business Act (12 U.S.C. 631) are eligible for this favorable risk-based capital treatment.

In general, a "qualifying institution" is one that is well capitalized without regard to the Section 208 provisions. If a bank ceases to be a qualifying institution or exceeds the retained recourse limit set forth in banking agency regulations implementing Section 208, all new transfers of small business obligations with recourse would not be treated as sales. However, the reporting and risk-based capital treatment described above will continue to apply to any transfers of small business obligations with recourse that were consummated during the time the bank was a "qualifying institution" and did not exceed the limit.

When reporting eligible transfers with recourse in Schedule RC-R, only the amount of retained recourse should be reported as a credit equivalent amount in column B. This amount, which is reported in Schedule RC-L, item 9.c.(2), will normally be accorded a 100 percent risk weight and be included in Schedule RC-R, item 7.b.

Treatment of covered positions by banks that are subject to the market risk capital guidelines -- The banking agencies' risk-based capital standards require all banks with significant market risk to measure their market risk exposure and hold sufficient capital to mitigate this exposure. In general, a bank is subject to the market risk capital guidelines if its consolidated trading activity, defined as the sum of trading assets and liabilities as reported in its Call Report for the previous quarter, equals: (1) 10 percent or more of the bank's total assets as reported in its Call Report for the previous quarter, or (2) $1 billion or more. However, the primary federal supervisory authority may exempt or include a bank if necessary or appropriate for safe and sound banking practices.

**General Instructions (cont.)**

A bank that is subject to the market risk capital guidelines must hold capital to support its exposure to general market risk arising from fluctuations in interest rates, equity prices, foreign exchange rates, and commodity prices and its exposure to specific risk associated with certain debt and equity positions. Covered positions include all positions in a bank's trading account and foreign exchange and commodity positions, whether or not in the trading account. Covered positions generally should not be risk-weighted as part of the bank's gross risk-weighted assets. However, foreign exchange positions that are outside of the trading account and all over-the-counter (OTC) derivatives continue to have a counterparty credit risk capital charge. Those positions are included in both gross risk-weighted assets for credit risk and the bank's covered positions for market risk.

The value-at-risk (VAR) of the bank's covered positions should be used to determine the bank's measure for market risk. VAR is an estimate of the amount by which a bank's positions in a risk category could decline due to expected losses in the bank's portfolio due to market movements during a given period, measured with a specified confidence level. A bank's measure for market risk equals the sum of its VAR-based capital charge, the specific risk add-on (if any), and the capital charge for de minimus exposures (if any). A bank's market risk equivalent assets equal its measure for market risk multiplied by 12.5 (the reciprocal of the minimum 8.0 percent capital ratio). Banks subject to the market risk capital guidelines must maintain an overall minimum 8.0 percent ratio of total qualifying capital (the sum of Tier 1 capital (both allocated and excess), Tier 2 capital (both allocated and excess), and Tier 3 capital (allocated for market risk), net of all deductions) to risk-weighted assets and market risk equivalent assets. Banks should refer to the capital guidelines of their primary federal supervisory authority for specific instructions on the calculation of the measure for market risk.

## Item Instructions

**Item No. Caption and Instructions**

**1 Test for determining the extent to which Schedule RC-R must be completed.**

Item 1 is to be completed only by banks with total assets of less than $1 billion. Indicate in the appropriate box at the right whether the bank has total capital greater than or equal to eight percent of adjusted total assets.

If "total risk-based capital," as reported in item 3.b below, divided by "adjusted total assets" (on an unrounded basis) is greater than or equal to 8.00 percent and the bank has less than $1 billion in total assets, the reporting bank should place an "X" in the box marked "YES." If "total capital" divided by "adjusted total assets" (on an unrounded basis) is less than 8.00 percent, the reporting bank should place an "X" in the box marked "NO." If the box marked "YES" is checked, then the bank must complete only items 2 and 3 of this schedule. If the box marked "NO" is checked, then the bank must complete items 2 through 9 and Memorandum items 1 and 2. In addition, checking the box marked "NO" does not necessarily mean that the bank's actual risk-based capital ratio is less than eight percent or that the bank is not in compliance with the risk-based capital guidelines.

"Adjusted total assets" is defined as total assets (after adjusting available-for-sale securities from fair value to amortized cost) LESS cash, U.S. Treasury securities, U.S. Government agency obligations, and 80 percent of U.S. Government-sponsored agency obligations not held for trading PLUS the allowance for loan and lease losses and selected off-balance sheet items. "Adjusted total assets" should be measured by using amounts reported elsewhere in the Report of Condition according to the following formula:

| | |
|---|---|
| Total assets | Schedule RC, item 12 |
| Adjustment to Available-for-Sale Securities | - Schedule RC-B, item 7, column D, + Schedule RC-B, item 7, column C |
| LESS: | |
| Cash (currency and coin) | - Schedule RC-M, item 3.b, on the FFIEC 034;<br>- Schedule RC-A, item 1.b, on the FFIEC 031, 032, and 033 |
| U.S. Treasuries (not held for trading) | - Schedule RC-B, item 1, sum of columns A and C |
| U.S. Government agencies (not held for trading) | - Schedule RC-B, item 2.a, sum of columns A and C, plus item 4.a.(1), sum of columns A and C |
| 80% of U.S. Government-sponsored agencies (not held for trading) | - 0.8 x (Schedule RC-B, item 2.b, sum of columns A and C, plus item 4.a.(2), sum of columns A and C, plus item 4.b.(1), sum of columns A and C) |
| PLUS: | |
| Allowance for Loan and Lease Losses | + Schedule RC, item 4.b |

| Item No. | Caption and Instructions | |
|---|---|---|
| 1 (cont.) | Unused Commitments | + Schedule RC-L, sum of items 1.a through 1.e |
| | Financial Standby Letters of Credit, Net | + Schedule RC-L, item 2 minus item 2.a |
| | Performance Standby Letters of Credit, Net | + Schedule RC-L, item 3 minus item 3.a |
| | Commercial Letters of Credit | + Schedule RC-L, item 4 |
| | Participations Acquired in Acceptances | + Schedule RC-L, item 6 |
| | Securities Lent | + Schedule RC-L, item 8 |
| | Financial Assets Transferred with Recourse | + Schedule RC-L, sum of items 9.a.(1), 9.b.(1), and 9.c.(2) |
| | Credit Derivatives | + Schedule RC-L, sum of items 10.a and 10.b |
| | Forward Contracts | + Schedule RC-L, item 14.b, sum of columns A through D |
| | Exchange-Traded Purchased Options | + Schedule RC-L, item 14.c.(2), sum of columns A through D |
| | Over-the-Counter Purchased Options | + Schedule RC-L, item 14.d.(2), sum of columns A through D |
| | Swaps | + Schedule RC-L, item 14.e, sum of columns A through D |
| | Other Off-Balance Sheet Liabilities | + Schedule RC-L, item 12 |
| | EQUALS: | = Adjusted Total Assets |

**2** **Portion of qualifying limited-life capital instruments (original weighted average maturity of at least five years) that is includible in Tier 2 capital.** The portion of a bank's qualifying limited-life capital instruments that is includible in Tier 2 capital is the amount that remains after discounting those instruments, if any, with five years or less until maturity and then applying any applicable percentage of Tier 1 capital limit. For limited-life capital instruments with serial maturities or with sinking fund provisions, the amount associated with each maturity date is to be treated as a separate issue and discounted on an individual basis. If the holder of the reporting bank's subordinated debt or intermediate-term or long-term preferred stock has the right to require the bank to redeem, repay, or repurchase the instrument prior to the original stated maturity, then maturity would be defined as the earliest possible date on which the holder can put the instrument back to the issuing bank.

**2.a** **Subordinated debt and intermediate-term preferred stock.** Report the portion of the reporting bank's qualifying term subordinated debt and intermediate-term preferred stock (including any related surplus) that is includible in Tier 2 capital. These capital instruments must have an original weighted average maturity of at least five years. Include as

| Item No. | Caption and Instructions |
|---|---|
| **2.a** (cont.) | intermediate-term preferred stock those issues of preferred stock with an original maturity of less than 20 years. |

Mandatory convertible debt, i.e., equity contract notes, should be excluded from this item.

Qualifying term subordinated debt and intermediate-term preferred stock is the amount that remains after discounting any instruments with five years or less until maturity. The portion of this qualifying amount that is includible in Tier 2 capital is limited to 50 percent of Tier 1 capital. This portion is calculated as follows:

| | | |
|---|---|---|
| (1) | Amount of subordinated debt and intermediate-term preferred stock with a remaining maturity of more than five years | _____ x 100% = _____ |
| (2) | Amount of subordinated debt and intermediate-term preferred stock with a remaining maturity of more than four years, but less than five years | _____ x 80% = _____ |
| (3) | Amount of subordinated debt and intermediate-term preferred stock with a remaining maturity of more than three years, but less than four years | _____ x 60% = _____ |
| (4) | Amount of subordinated debt and intermediate-term preferred stock with a remaining maturity of more than two years, but less than three years | _____ x 40% = _____ |
| (5) | Amount of subordinated debt and intermediate-term preferred stock with a remaining maturity of more than one year, but less than two years | _____ x 20% = _____ |
| (6) | Amount of subordinated debt and intermediate-term preferred stock with a remaining maturity of one year or less | _____ x 0% = _____ |
| (7) | Qualifying subordinated debt and intermediate-term preferred stock (sum of discounted amounts of lines (1) through (6)) | _____ |
| (8) | Tier 1 capital (from Schedule RC-R, item 3.a) | _____ |
| (9) | Multiplied by 50 percent | x 50% |
| (10) | Limit for qualifying subordinated debt and intermediate-term preferred stock (line (8) multiplied by 50 percent) | _____ |
| (11) | Portion of qualifying subordinated debt and intermediate-term preferred stock includible in Tier 2 capital (lesser of lines (7) and (10)) | _____ |

Report the amount from line (11) in Schedule RC-R, item 2.a.

| | |
|---|---|
| **2.b** | **Other limited-life capital instruments.** Report the portion of the reporting bank's qualifying other limited-life capital instruments, such as long-term preferred stock with an original maturity of 20 years or more, that is includible in Tier 2 capital. |

Qualifying other limited-life capital instruments is the amount that remains after discounting any instruments with five years or less until maturity. The entire amount of this qualifying

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**2.b** (cont.) amount is the portion that is includible in Tier 2 capital. This portion is calculated as follows:

| | | |
|---|---|---|
| (1) | Amount of other limited-life capital instruments with a remaining maturity of more than five years | _____ x 100% = _____ |
| (2) | Amount of other limited-life capital instruments with a remaining maturity of more than four years, but less than five years | _____ x 80% = _____ |
| (3) | Amount of other limited-life capital instruments with a remaining maturity of more than three years, but less than four years | _____ x 60% = _____ |
| (4) | Amount of other limited-life capital instruments with a remaining maturity of more than two year, but less than three years | _____ x 40% = _____ |
| (5) | Amount of other limited-life capital instruments with a remaining maturity of more than one year, but less than two years | _____ x 20% = _____ |
| (6) | Amount of other limited-life capital instruments with a remaining maturity of one year or less | _____ x 0% = _____ |
| (7) | Portion of qualifying other limited-life capital instruments (sum of discounted amounts of lines (1) through (6)) | _____ |

Report the amount from line (7) in Schedule RC-R, item 2.b.

**3** **Amounts used in calculating regulatory capital ratios.** Report in the appropriate subitem the indicated amounts used in calculating the bank's risk-based and leverage capital ratios.[1] Some of these amounts are also used in calculating other regulatory limitations, such as limits on loans to insiders. The amounts to be reported in these subitems should be those determined by the bank for its own internal regulatory capital analyses consistent with applicable capital standards and these instructions and they are subject to examiner review.

**3.a.(1)** **Tier 1 capital.** Report the amount of the bank's Tier 1 capital. The amount reported in this item is the numerator of the bank's Tier 1 risk-based capital ratio and its Tier 1 leverage ratio.

Tier 1 (core) capital consists of:
(1) common stockholders' equity capital,
(2) noncumulative perpetual preferred stock and any related surplus, and
(3) minority interests in equity capital accounts of consolidated subsidiaries,
less goodwill, other disallowed intangible assets, and disallowed deferred tax assets, and any other amounts that are deducted in determining Tier 1 capital in accordance with the capital

[1] For purposes of Schedule RC-R, items 3.a.(1), 3.d.(1), and 3.f, insured state banks with real estate subsidiaries whose continued operations have been approved by the FDIC pursuant to Section 362.4 of the FDIC's Rules and Regulations should deduct from the parent bank's Tier 1 capital and assets, as appropriate: (a) any equity investment in the subsidiary, (b) any debt issued by the subsidiary that is held by the insured state bank or guarantees of any debt issued by the subsidiary by the insured state bank, and (c) any extensions of credit from the insured state bank to the subsidiary. Insured state banks with FDIC-approved phase-out plans for real estate subsidiaries need not make these deductions.

standards issued by the reporting bank's primary federal supervisory authority.

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**3.a.(1)** (cont.) NOTE: For regulatory capital purposes, common stockholders' equity capital includes any net unrealized holding losses on available-for-sale equity securities with readily determinable fair values (net of any applicable tax effect), but excludes other net unrealized holding gains (losses) on available-for-sale securities. Common stockholders' equity capital also excludes accumulated net gains (losses) on cash flow hedges.

For most banks, Tier 1 capital will equal common stockholders' equity capital (Schedule RC, the sum of items 24, 25, 26.a, and 27, less any net unrealized holding losses on available-for-sale equity securities with readily determinable fair values, net of any applicable tax effect) less goodwill and other disallowed intangible assets and less disallowed deferred tax assets. (Net unrealized holding losses on available-for-sale equity securities with readily determinable fair values can be determined from Schedule RC-B, item 6.a. In general, if item 6.a, column C, is greater than item 6.a, column D, the excess should be deducted from Tier 1 capital, net of any applicable tax effect. Intangible assets are reported in Schedule RC, item 10, and in Schedule RC-M, item 6. Disallowed deferred tax assets are reported in Schedule RC-F, Memorandum item 1.)

If the bank has any low level recourse transactions and chooses to use the "direct reduction method" for reporting these transactions in Schedule RC-R (as discussed in the General Instructions to Schedule RC-R), do *not* deduct any of the bank's "maximum contractual dollar amount of recourse exposure in low level recourse transactions," as reported in Schedule RC-R, item 3.e, from the amount of Tier 1 capital that the bank reports in this item.

**3.a.(2)** **Tier 2 capital.** Report the amount of the bank's Tier 2 capital. The amount reported in this item must be less than or equal to the amount reported in Schedule RC-R, item 3.a.(1), "Tier 1 capital."

Tier 2 (supplementary) capital is limited to 100 percent of Tier 1 capital and consists of:

(1) cumulative perpetual preferred stock and any related surplus,
(2) long-term preferred stock (original maturity of 20 years or more) and any related surplus (discounted for capital purposes as it approaches maturity),
(3) auction rate and similar preferred stock (both cumulative and noncumulative),
(4) hybrid capital instruments (including mandatory convertible debt securities),
(5) term subordinated debt and intermediate-term preferred stock (original weighted average maturity of five years or more) to the extent of 50 percent of Tier 1 capital (and discounted for capital purposes as they approach maturity),
(6) the allowance for credit losses, i.e., the allowance for loan and lease losses plus any portions of the allowance for credit losses related to off-balance sheet exposures (limited to the lesser of the balance of the allowance or 1.25 percent of gross risk-weighted assets), and
(7) up to 45 percent of pretax net unrealized holding gains on available-for-sale equity securities with readily determinable fair values.

For most banks, Tier 2 capital will equal the allowable portion of the allowance for loan and lease losses (Schedule RC, item 4.b) and is further limited to 100 percent of Tier 1 capital. Banks with other Tier 2 capital components (e.g., subordinated debt and preferred stock) should refer to the definition of Tier 2 capital set forth above and to the risk-based capital guidelines for the proper treatment of such components.

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**3.a.(3)** **Tier 3 capital.** (Item 3.a.(3) is to be completed only by banks that file the FFIEC 031 or 032 report forms.) Report the amount of the bank's Tier 3 capital allocated for market risk. This item is only applicable to banks that are subject to the market risk capital guidelines. The amount reported in this item may only be used to satisfy the bank's market risk capital requirement and may not be used to support credit risk. The sum of the amount reported in this item and the amount reported in Schedule RC-R, item 3.a.(2), "Tier 2 capital," must be less than or equal to the amount reported in Schedule RC-R, item 3.a.(1), "Tier 1 capital." In addition, Tier 3 capital allocated for market risk plus Tier 2 capital allocated for market risk are limited to 71.4 percent of a bank's measure for market risk.

**3.b** **Total risk-based capital.** Report the amount of the bank's total risk-based capital. The amount reported in this item is the numerator of the bank's total risk-based capital ratio.

Total risk-based capital is the sum of Tier 1 capital, Tier 2 capital, and Tier 3 capital allocated for market risk, net of all deductions. *Deductions* are made for investments in banking and finance subsidiaries that are not consolidated for regulatory capital purposes, intentional reciprocal cross-holdings of banking organizations' capital instruments, and other deductions as determined by the reporting bank's primary federal supervisory authority.

For most banks, total risk-based capital will equal the sum of Schedule RC-R, item 3.a.(1), "Tier 1 capital," and item 3.a.(2), "Tier 2 capital."

If the bank has any low level recourse transactions and chooses to use the "direct reduction method" for reporting these transactions in Schedule RC-R (as discussed in the General Instructions to Schedule RC-R), do *not* deduct the bank's "maximum contractual dollar amount of recourse exposure in low level recourse transactions," as reported in Schedule RC-R, item 3.e, from the amount of total risk-based capital that the bank reports in this item.

**3.c** **Excess allowance for loan and lease losses.** Report the amount, if any, by which the bank's allowance for credit losses exceeds 1.25 percent of the bank's *gross* risk-weighted assets. The allowance for credit losses is reported in Schedule RI-B, part II, item 6. On the FFIEC 034 in quarters when Schedule RI-B, part II, is not completed, the allowance for credit losses generally is the allowance for loan and lease losses as reported in Schedule RC, item 4.b. However, the allowance for credit losses also includes any portions of the allowance for credit losses related to off-balance sheet credit exposures reported elsewhere on the balance sheet (Schedule RC).

Gross risk-weighted assets is the amount of the bank's risk-weighted assets *before* deducting the amount of any excess allowance for loan and lease losses. (Note: The amount reported in Schedule RC-R, item 3.d.(1), is *net* risk-weighted assets. Do *not* multiply the amount reported in item 3.d.(1) by 1.25 percent to determine the amount of the bank's excess allowance for loan and lease losses.)

If the bank has any low level recourse transactions and chooses to use the "direct reduction method" for reporting these transactions in Schedule RC-R, refer to the discussion of this subject in the General Instructions to Schedule RC-R for guidance on determining the limit on the allowance for loan and lease losses for Tier 2 capital purposes.

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| **3.c** (cont.) | For banks that are subject to the market risk capital guidelines, report the amount, if any, by which the allowance for credit losses exceeds 1.25 percent of the sum of market risk equivalent assets (as reported in Schedule RC-R, item 3.d.(2)) plus gross risk-weighted assets. |
| **3.d.(1)** | **Net risk-weighted assets.** Report the amount of the bank's risk-weighted assets *net* of all deductions. The amount reported in this item is the denominator of the bank's total risk-based capital ratio and, thus, should include any amount reported in Schedule RC-R, item 3.d.(2), "Market risk equivalent assets."<br><br>When determining the amount of risk-weighted assets, on-balance sheet assets are assigned an appropriate risk weight (zero percent, 20 percent, 50 percent, or 100 percent) and off-balance sheet items are first converted to a credit equivalent amount and then assigned to one of the four risk weight categories. All covered positions that are subject to the market risk capital guidelines, except for foreign exchange positions that are outside of the trading account and all over-the-counter (OTC) derivatives, are excluded from the amounts used to determine risk-weighted assets. Foreign exchange positions outside of the trading account and all OTC derivatives have a counterparty credit risk capital charge and are included in net risk-weighted assets. The on-balance sheet assets and the credit equivalent amounts of off-balance sheet items are then multiplied by the appropriate risk weight percentages and the sum of these risk-weighted amounts, less certain deductions, is the bank's *gross* risk-weighted assets. These deductions are for goodwill, other disallowed intangible assets, disallowed deferred tax assets, investments in banking and finance subsidiaries that are not consolidated for regulatory capital purposes, intentional reciprocal cross-holdings of banking organizations' capital instruments, and other deductions as determined by the reporting bank's primary federal supervisory authority. Gross risk-weighted assets minus any excess allowance for loan and lease losses (reported in Schedule RC-R, item 3.c) and minus any allocated transfer risk reserve is the bank's *net* risk-weighted assets, which is the amount to be reported in this item.<br><br>If the bank has any low level recourse exposures, it should include in the net risk-weighted assets reported in this item the appropriate amount for these exposures as determined under the "direct reduction method" or the "gross-up method." These methods are discussed in the section of the General Instructions to Schedule RC-R on "Treatment of Low Level Recourse Transactions." |
| **3.d.(2)** | **Market risk equivalent assets.** (Item 3.d.(2) is to be completed only by banks that file the FFIEC 031 or 032 report forms.) Report the amount of the bank's market risk equivalent assets. This item is only applicable to banks that are subject to the market risk capital guidelines. Market risk equivalent assets equals the bank's measure for market risk multiplied by 12.5. Banks should refer to the capital guidelines of their primary federal supervisory authority for specific instructions on the calculation of the measure for market risk. |
| **3.e** | **Maximum contractual dollar amount of recourse exposure in low level recourse transactions.** If the bank has any low level recourse transactions and chooses to use the "direct reduction method" for reporting these transactions in Schedule RC-R, report the "maximum contractual dollar amount of recourse exposure" for these transactions in accordance with the guidance in the section of the General Instructions to Schedule RC-R on "Treatment of Low Level Recourse Transactions." |

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**3.e** (cont.) If the bank has no low level recourse transactions or if the bank chooses to use the "gross-up method" for reporting its low level recourse transactions in Schedule RC-R, report a zero in this item.

**3.f** **"Average total assets."** Report the amount of the bank's "average total assets," i.e., the denominator of the bank's Tier 1 leverage capital ratio.

"Average total assets" consists of the quarterly average for "total assets" as reported in the Call Report, less goodwill, other disallowed intangible assets, disallowed deferred tax assets, and any other assets that are deducted in determining Tier 1 capital in accordance with the capital standards issued by the reporting bank's primary federal supervisory authority. For FDIC-supervised banks, the quarterly average for "total assets" must be adjusted for any securities subsidiary subject to Section 337.4 of the FDIC's Rules and Regulations.

For most banks, "average total assets" will equal Schedule RC-K, item 7 on the FFIEC 034, item 9 on the FFIEC 031, 032, and 033, less goodwill and other disallowed intangible assets and less disallowed deferred tax assets. Intangible assets are reported in Schedule RC, item 10, and in Schedule RC-M, item 6. Disallowed deferred tax assets are reported in Schedule RC-F, Memorandum item 1.

**4** **Assets and credit equivalent amounts of off-balance sheet items assigned to the Zero percent risk category.** Report in the appropriate subitem:

(1) Currency and coin (domestic and foreign) held in the bank or in transit (from Schedule RC-A on the FFIEC 031, 032, and 033; from Schedule RC-M, item 3.b, on the FFIEC 034);

(2) Securities issued by and other direct claims (such as loans or leases) on the U.S. Government and other OECD central governments (including U.S. Treasury securities from Schedule RC-B, item 1);

(3) Portions of claims on other counterparties that are *unconditionally* guaranteed by the U.S. Government and its agencies and other OECD central governments (including GNMA and SBA securities and loans guaranteed by the Export-Import Bank);

(4) Local currency claims on, and the portions of local currency claims that are *unconditionally* guaranteed by, non-OECD central governments (including central banks) to the extent that the bank has liabilities booked in that currency; and

(5) Gold bullion held in the bank's vaults or in another's vaults on an allocated basis, to the extent offset by gold bullion liabilities.

For national and state member banks, this item includes those claims, or portions of claims, that (a) are collateralized by cash on deposit in the reporting bank or by securities issued by, or directly and unconditionally guaranteed by, the U.S. Government or its agencies or the central government of an OECD country and (b) qualify for a zero percent risk weight in accordance with the risk-based capital standards issued by the reporting bank's primary federal supervisory authority. The extent to which qualifying securities are recognized as collateral is determined by their current market value. If a claim is partially secured, that is, the market value of the pledged securities is less than the face amount of an asset or off-balance sheet item, only the portion that is covered by the market value of the collateral

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4 (cont.) is to be reported in this item. The face amount of a claim secured by two types of qualifying collateral is to be reported in the items appropriate to the collateral types, apportioned according to the market value of each of the two types of collateral.

Claims on OECD central governments includes balances due from the Federal Reserve Banks (including Federal Reserve Bank stock) and central banks in other OECD countries. If the reporting bank is the correspondent bank in a pass-through reserve balance relationship, report the amount of its own reserves as well as those reserve balances actually passed through to a Federal Reserve Bank on behalf of its respondent depository institutions.

If the reporting bank is the respondent bank in a pass-through reserve balance relationship, report in this item the amount of the bank's reserve balances due from its correspondent bank that its correspondent has actually passed through to a Federal Reserve Bank on the reporting bank's behalf, i.e., for purposes of this item, treat these balances as balances due from a Federal Reserve Bank. This treatment differs from that required in Schedule RC-A, item 2 (on the FFIEC 031, 032, and 033), "Balances due from depository institutions in the U.S.," which would treat balances held by a bank's correspondent as balances due from a depository institution as opposed to balances due from the Federal Reserve.

For banks that are subject to the market risk capital guidelines, exclude all covered positions except for foreign exchange positions that are outside of the trading account and over-the-counter (OTC) derivatives. The book value or credit equivalent amount, as appropriate, of foreign exchange positions that are outside of the trading account and all OTC derivatives assigned to the Zero percent risk category should continue to be included in this item. Covered positions include all positions in a bank's trading account, and all foreign exchange and commodity positions whether or not in the trading account.

**4.a** **Assets recorded on the balance sheet.** Report the book value (i.e., fair value for assets held for trading) of all assets recorded on the reporting bank's balance sheet which are assigned a Zero percent risk weight under the risk-based capital guidelines. However, for available-for-sale securities assigned to the Zero percent risk category, report the amortized cost of such securities rather than the fair value at which they are reported on the balance sheet.

**4.b** **Credit equivalent amount of off-balance sheet items.** Report the credit equivalent amount, as determined under the risk-based capital guidelines, for those off-balance sheet items that are to be risk weighted at Zero percent in accordance with the guidelines. Include the credit equivalent amount of those off-balance sheet direct claims on, or claims unconditionally guaranteed by the U.S. Government and other OECD central governments.

**5** **Assets and credit equivalent amounts of off-balance sheet items assigned to the 20 percent risk category.** Report in the appropriate subitem:

(1) Cash items in the process of collection (from Schedule RC-A on the FFIEC 031, 032, and 033; a portion of Schedule RC, item 1.a on the FFIEC 034);

(2) Claims on (including balances due from), and the portion of claims guaranteed by, U.S. depository institutions and other OECD banks (except as noted below);

(3) Short-term (one year or less) claims on, and the portions of short-term claims guaranteed by, non-OECD banks;

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**5** (cont.) (4) Portions of claims collateralized by securities issued, or guaranteed, by the U.S. Government and other OECD central governments that, under the risk-based capital standards issued by the reporting bank's primary federal supervisory authority, do not qualify for the zero percent risk weight category;

(5) Portions of securities, loans, and other claims *conditionally* guaranteed by the U.S. Government and its agencies and other OECD central governments (e.g., VA and FHA mortgage loans and student loans on which the U.S. Department of Education acts as a reinsurer);

(6) Portions of local currency claims that are *conditionally* guaranteed by the central governments of non-OECD countries, to the extent that the bank has liabilities booked in that country;

NOTE: A guarantee is conditional if its validity is dependent upon some affirmative action by the bank or a third party (e.g., servicing requirements).

(7) General obligation claims on, and the portion of claims that are guaranteed by the full faith and credit of local governments and political subdivisions in the U.S. and other OECD local governments;

(8) Portions of claims collateralized by cash on deposit in the reporting bank -- including standby letters of credit collateralized by cash -- that, under the risk-based capital standards issued by the reporting bank's primary federal supervisory authority, do not qualify for the zero percent risk weight category;

NOTE: Claims collateralized by deposits in other depository institutions (e.g., certificates of deposit issued by other banks) do *not* qualify for a 20 percent risk weight. Such collateralized claims are to be reported in Schedule RC-R, item 6 or item 7, as appropriate.

(9) Claims (including securities from Schedule RC-B) on or guaranteed by U.S. Government-sponsored agencies;

(10) Portions of claims collateralized by securities issued or guaranteed by U.S. Government-sponsored agencies (e.g., loans collateralized by FHLMC pass-through securities);

(11) Certain privately-issued mortgage-backed securities representing indirect ownership of U.S. Government agency or U.S. Government-sponsored agency mortgage-backed securities (e.g., GNMA, FNMA, and FHLMC pass-through securities); and

(12) Claims on, guaranteed by, or collateralized by securities of, official multilateral lending institutions or regional development banks, e.g., the World Bank including the International Finance Corporation.

<u>Include</u> as claims guaranteed by U.S. depository institutions and foreign banks all risk participations in bankers acceptances, standby letters of credit, and commitments that are conveyed to such institutions. Do *not* include in this item the portion of loans insured under the FHA Title I insurance program, claims on bank holding companies, or holdings of bank-issued securities that qualify as capital of the issuing bank for risk-based capital

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**5** (cont.) purposes (report in item 7). In addition, claims on foreign official institutions that are not multilateral lending institutions or regional development banks (e.g., agencies of the United Nations other than the World Bank and the International Finance Corporation) are *not* to be reported in this item (report in item 7).

The extent to which qualifying securities are recognized as collateral is determined by their current market value. If a claim is partially secured, that is, the market value of the pledged securities is less than the face amount of an asset or off-balance sheet item, only the portion that is covered by the market value of the collateral is to be reported in this item. The face amount of a claim secured by two types of qualifying collateral is to be reported in the items appropriate to the collateral types, apportioned according to the market value of each of the two types of collateral.

If a claim is partially guaranteed or covered by two types of guarantees, then the aforementioned treatment of claims that are collateralized is applicable.

For banks that are subject to the market risk capital guidelines, exclude all covered positions except for foreign exchange positions that are outside of the trading account and over-the-counter (OTC) derivatives. The book value or credit equivalent amount, as appropriate, of foreign exchange positions that are outside of the trading account and all OTC derivatives assigned to the 20 percent risk category should continue to be included in this item. Covered positions include all positions in a bank's trading account, and all foreign exchange and commodity positions whether or not in the trading account.

**5.a** **Assets recorded on the balance sheet.** Report the book value (fair value for assets held for trading) of all assets recorded on the reporting bank's balance sheet which are assigned a 20 percent risk weight under the risk-based capital guidelines. However, for available-for-sale debt securities assigned to the 20 percent risk category, report the amortized cost of such securities rather than the fair value at which they are reported on the balance sheet. For available-for-sale equity securities, if total cost exceeds total fair value, report in this item the fair value of available-for-sale equity securities assigned to the 20 percent risk category rather than their cost; if total fair value exceeds total cost, report in this item the cost of available-for-sale equity securities assigned to the 20 percent risk category rather than the fair value at which they are reported on the balance sheet.

**5.b** **Credit equivalent amount of off-balance sheet items.** Report the credit equivalent amount, as determined under the risk-based capital guidelines, for those off-balance sheet items that are risk weighted at 20 percent. Include the credit equivalent amount of off-balance sheet claims collateralized by cash on deposit (e.g., standby letters of credit collateralized by cash) that, under the risk-based capital standards issued by the reporting bank's primary federal supervisory authority, do not qualify for the zero percent risk weight category.

**6** **Assets and credit equivalent amounts of off-balance sheet items assigned to the 50 percent risk category.** Report the book value (fair value for assets held for trading) of all assets recorded on the reporting bank's balance sheet and the credit equivalent amount of all off-balance sheet items which are assigned a 50 percent risk weight under the risk-based capital guidelines. However, for available-for-sale debt securities assigned to the 50 percent risk category, report the amortized cost of such securities rather than the fair value at which they are reported on the balance sheet. For available-for-sale equity securities, if total cost exceeds total fair value, report in this item the fair value of available-for-sale equity securities assigned to the 50 percent risk category rather than their cost; if total fair

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**6** (cont.) value exceeds total cost, report in this item the cost of available-for-sale equity securities assigned to the 50 percent risk category rather than the fair value at which they are reported on the balance sheet. In addition, the 50 percent risk weight is the maximum risk weight to be applied to the credit equivalent amounts of those interest rate, foreign exchange, equity derivative, and commodity and other derivative contracts covered under the risk-based capital guidelines.

For banks that are subject to the market risk capital guidelines, exclude all covered positions except for foreign exchange positions that are outside of the trading account and over-the-counter (OTC) derivatives. The book value or credit equivalent amount, as appropriate, of foreign exchange positions that are outside of the trading account and all OTC derivatives assigned to the 50 percent risk category should continue to be included in this item. Covered positions include all positions in a bank's trading account, and all foreign exchange and commodity positions whether or not in the trading account.

**6.a** **Assets recorded on the balance sheet.** Report in this item loans that are fully secured by first liens on 1-to-4 family residential properties (including certain presold residential construction loans) that were made in accordance with prudent underwriting standards (including an appropriate loan-to-value ratio), that are performing in accordance with their original terms, and that are not 90 days or more past due or in nonaccrual status.

If a bank holds the first and junior lien(s) on a residential property and no other party holds an intervening lien, the loans will be viewed as a single extension of credit secured by a first lien on the underlying property for purposes of determining the loan-to-value ratio and assigning a risk weight. The combined loan amount will be assigned to either the 50 percent or 100 percent risk category, depending on whether the credit satisfies the criteria for a 50 percent risk weighting. To qualify for the 50 percent risk category, the combined loan must be made in accordance with prudent underwriting standards (including an appropriate loan-to-value ratio) and none of the combined loans may be 90 days or more past due or in nonaccrual status. If the combined loan does not meet all of these criteria, the combined loans must be assigned in their entirety to the 100 percent risk category and reported in Schedule RC-R, item 7.a below.

Also report in this item loans fully secured by first liens on multifamily residential properties that have been prudently underwritten and meet the requirements specified in the risk-based capital standards for loan-to-value ratios, level of annual net operating income to required debt service, maximum amortization period, minimum original maturity, and demonstrated timely repayment performance.

Also include certain privately-issued mortgage-backed securities representing direct and indirect ownership of the aforementioned mortgage loans if the criteria for privately-issued mortgage-backed securities outlined in the risk-based capital guidelines (and listed below) are met. For example, a homebuilder issues a pass-through security that is backed by a pool of first mortgages on 1-to-4 family residential mortgages that are prudently underwritten and are not restructured, past due, or in nonaccrual status. The criteria outlined in the risk-based capital guidelines allowing these securities to be risk-weighted on the basis of the pool of mortgage collateral rather than on the issuer require that:

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| **6.a** (cont.) | (1) the underlying assets are held by an independent trustee and the trustee has a first priority, perfected security interest in the underlying assets on behalf of the holders of the security;<br><br>(2) either (a) the holder of the security has an undivided *pro rata* ownership interest in the underlying mortgage assets or (b) the trust or single purpose entity that issues the security has no liabilities unrelated to the issued securities;<br><br>(3) the security is structured such that the cash flow from the underlying assets in all cases fully meets the cash flow requirements of the security without undue reliance on any reinvestment income; and<br><br>(4) there is no material reinvestment risk associated with any funds awaiting distribution to the holders of the security.<br><br>In addition, include revenue bonds or similar claims that are obligations of U.S. state or local governments, or other OECD local governments, for which the government is committed to repay the debt only out of revenues from the facilities financed.<br><br><u>Exclude</u> from this item loans collateralized by mortgage notes that the reporting bank has indirectly financed, e.g., mortgage warehousing lines. |
| **6.b** | **<u>Credit equivalent amount of off-balance sheet items.</u>** Report the credit equivalent amount, as determined under the risk-based capital guidelines, for those off-balance sheet items that are to be risk weighted at 50 percent in accordance with the guidelines. Include in this item the credit equivalent amounts of interest rate and foreign exchange rate contracts that are not accorded a lower risk weight as a result of the counterparty, collateral, or a guarantee. |
| **7** | **<u>Assets and credit equivalent amounts of off-balance sheet items assigned to the 100 percent risk category.</u>** Report the book value (fair value for assets held for trading) of all assets recorded on the reporting bank's balance sheet and the credit equivalent amount of all off-balance sheet items which are assigned a 100 percent risk weight under the risk-based capital guidelines. For available-for-sale debt securities assigned to the 100 percent risk category, report the amortized cost of such securities rather than the fair value at which they are reported on the balance sheet. For available-for-sale equity securities, if total cost exceeds total fair value, report in this item the fair value of available-for-sale equity securities assigned to the 100 percent risk category rather than their cost; if total fair value exceeds total cost, report in this item the cost of available-for-sale equity securities assigned to the 100 percent risk category (rather than the fair value at which they are reported on the balance sheet) plus the portion of the pretax net unrealized holding gains (up to 45 percent) the bank has included in Tier 2 capital.<br><br>For banks that are subject to the market risk capital guidelines, exclude all covered positions except for foreign exchange positions that are outside of the trading account and over-the-counter (OTC) derivatives. The book value or credit equivalent amount, as appropriate, of foreign exchange positions that are outside of the trading account and all OTC derivatives assigned to the 100 percent risk category should continue to be included in this item. Covered positions include all positions in a bank's trading account, and all foreign exchange and commodity positions whether or not in the trading account. |

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**7.a** **Assets recorded on the balance sheet.** Report all assets that are not reportable in items 4 through 6 above or in item 8 below. Include:

(1) Stripped mortgage-backed securities (e.g., interest-only and principal-only strips);
(2) Residual and subordinated interests in asset-backed securities;
(3) Mortgage servicing assets, purchased credit card relationships, and nonmortgage servicing assets (excluding any portion that is disallowed for regulatory capital purposes);
(4) Premises and fixed assets;
(5) Industrial development bonds;
(6) Loans, debt securities, and other claims where the counterparty is a private obligor;
(7) Margin accounts on futures contracts;
(8) Other real estate owned;
(9) Net deferred tax assets (excluding any portion that is disallowed for regulatory capital purposes); and
(10) All other assets not already reported above (excluding those reportable in Schedule RC-R, item 8 below).

For purposes of this schedule, the amount to be reported in this item should be *reduced* by the amount of any valuation allowances the reporting bank maintains against assets other than loans and available-for-sale securities (e.g., valuation allowances for other real estate owned).

**7.b** **Credit equivalent amounts of off-balance sheet items.** Report the credit equivalent amount, as determined under the risk-based capital guidelines, for those off-balance sheet items that are risk weighted at 100 percent in accordance with the guidelines. Include those off-balance sheet items where the counterparty is a private obligor and which are not accorded a lower risk weight as a result of collateral or a guarantee.

**8** **On-balance sheet asset values excluded from and deducted in the calculation of the risk-based capital ratio.** Report in this item the difference between the fair value and the amortized cost of the reporting bank's available-for-sale debt securities (and report the amortized cost of these debt securities in Schedule RC-R, items 4 through 7 above). Furthermore, to the extent that the amount of net deferred tax assets carried on the balance sheet (Schedule RC) and reported in Schedule RC-F, item 2, includes the deferred tax effects of any unrealized holding gains and losses on available-for-sale debt securities, these deferred tax effects *may* be excluded from the net deferred tax asset amount reported as a 100 percent risk weight asset in Schedule RC-R, item 7.a. If these deferred tax assets are excluded, they should be reported in this item and this reporting treatment must be followed consistently over time. For available-for-sale equity securities, if total cost exceeds total fair value, report the fair value of these equity securities in items 5 through 7 above and include no amount in this item. However, if total fair value exceeds total cost, the bank may include up to 45 percent of the pretax net unrealized holding gains as a component of Tier 2 capital. In this situation, report the cost of these equity securities in items 5 through 7 above, report the portion of the pretax net unrealized holding gains (up to 45 percent) included in Tier 2 capital in item 7.a above, and include the remainder of the pretax net unrealized holding gains (55 percent or more) in this item.

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**8** (cont.) Include in this item any portion of the bank's mortgage servicing assets, purchased credit card relationships, nonmortgage servicing assets, and net deferred tax assets that is disallowed for regulatory capital purposes as well as all other intangible assets and other assets that are required to be deducted from regulatory capital in accordance with the capital standards issued by the bank's primary federal regulatory agency.

If the bank has low level recourse transactions that use contractual cash flows (e.g., interest-only strips receivable and so-called "spread accounts"), retained subordinated interests, retained securities (e.g., collateral invested amounts or cash collateral accounts) or other assets as credit enhancements, the on-balance sheet asset amount of the credit enhancements should be included in this item. The "maximum contractual dollar amount of recourse exposure" for low level recourse transactions should be converted into off-balance sheet credit equivalent amounts and reported in accordance with the section of the General Instructions to Schedule RC-R on "Treatment of Low Level Recourse Transactions."

Also report in this item the on-balance sheet asset values (or portions thereof) of off-balance sheet interest rate, foreign exchange, equity derivative, and commodity and other contracts that are treated for risk-based capital purposes as off-balance sheet items even though they may have on-balance sheet amounts included on Schedule RC. In addition, include in this item the on-balance sheet asset values related to (1) foreign exchange contracts with an original maturity of fourteen calendar days or less, (2) instruments traded on organized exchanges that require daily payment and receipt of variation margin (e.g., futures contracts), and (3) other interest rate, foreign exchange, equity derivative, and commodity and other contracts not covered under the risk-based capital guidelines such as over-the-counter written options. These on-balance sheet asset values may have been reported on Schedule RC on a net basis in accordance with the FASB Interpretation No. 39, as described in the Glossary entry for "Offsetting." (Purchased options that are traded on an organized exchange are to be included in the calculation of the risk-based capital ratio because such option contracts are not subject to a daily variation margin.) For banks that are subject to the market risk capital guidelines, to the extent that their on-balance sheet amounts have not already been included in this item in accordance with the preceding instructions, also report in this item the on-balance sheet asset values of all positions in the trading account and commodity positions.

For those off-balance sheet interest rate, foreign exchange, equity derivative, and commodity and other contracts subject to risk-based capital, banks should report the on-balance sheet asset values (or portions thereof) in this item to avoid a capital charge against the on-balance sheet amounts in addition to the capital charge against the credit equivalent amounts calculated under the risk-based capital guidelines. The amount to be reported in this item for each off-balance sheet interest rate, foreign exchange, equity derivative, and commodity and other contract should equal the lower of the contract's positive on-balance sheet asset amount included in Schedule RC or its positive market value included in computing the credit equivalent amount of the transaction. (For purposes of this comparison, if the amount of any accrued receivable is included in the calculation of the credit equivalent amount of an off-balance sheet derivative contract, this amount should be treated as part of the contract's positive on-balance sheet asset amount.) If either amount is zero or negative, then report for that contract in this item the amount, if any, which has been included in the on-balance sheet asset amount reported for such contract on Schedule RC. For example, a forward contract that is marked to market for reporting purposes will have its on-balance sheet market value, if positive, reported in this item and,

| Item No. | Caption and Instructions |
| --- | --- |
| **8** (cont.) | as a result, this on-balance sheet asset amount will be excluded from the risk-based capital ratio computation. The positive market value, however, will be included in the credit equivalent amount of this off-balance sheet item for risk-based capital purposes.<br><br>If the on-balance sheet asset value of a purchased option exceeds the market value of the purchased option, then the excess is not to be included in this item; rather, the excess is to be included in the appropriate risk weight category in Schedule RC-R, items 4 through 6 above. However, if the market value equals or exceeds the on-balance sheet asset value, the full on-balance sheet amount would be included in this item.<br><br>Exclude from this item any accrued receivables associated with off-balance sheet derivative contracts that are not included in the calculation of the credit equivalent amounts of these contracts and margin accounts related to derivative contracts. Margin accounts must be assigned to the 100 percent risk category while accrued receivables not reported in this item are to be included in the appropriate risk-weight category. |
| **9** | **Total assets recorded on the balance sheet.** Report in column A the sum of items 4.a, 5.a, 6.a, 7.a, and 8, column A. This amount must equal Schedule RC, item 12 plus items 4.b and 4.c. |

## Memoranda

**Item No.** **Caption and Instructions**

**1** **Current credit exposure across all off-balance-sheet derivative contracts covered by the risk-based capital standards**. Report a single current credit exposure amount for off-balance-sheet derivative contracts covered by the risk-based capital standards after considering applicable legally enforceable bilateral netting agreements. For purposes of this item, include the current credit exposure for off-balance sheet interest rate, foreign exchange, equity derivative, and commodity and other contracts. For descriptions of these contracts, refer to the instructions for Schedule RC-L, item 14. For banks that are subject to the market risk capital guidelines, exclude all covered positions subject to these guidelines, except for foreign exchange derivatives that are outside of the trading account and all over-the-counter (OTC) derivatives. Foreign exchange derivatives that are outside of the trading account and all OTC derivatives continue to have a counterparty credit risk capital charge and, therefore, a current credit exposure amount.

Current credit exposure (sometimes referred to as the replacement cost) is the fair value of a contract when that fair value is positive. The current credit exposure is zero when the fair value is negative or zero. Current credit exposure should be derived as follows: Determine whether a legally enforceable bilateral netting agreement is in place between the reporting bank and a counterparty. If such an agreement is in place, the fair values of all applicable interest rate and foreign exchange contracts with that counterparty that are included in the netting agreement are netted to a single amount. Next, for all other contracts covered by the risk-based capital standards that have positive fair values, the total of the positive fair values is determined. Then, report in this item the sum of (i) the net positive fair values of applicable interest rate and foreign exchange contracts subject to legally enforceable bilateral netting agreements and (ii) the total positive fair values of all other contracts covered by the risk-based capital standards.

Consistent with the risk-based capital guidelines, if a bilateral netting agreement covers off-balance sheet derivative contracts that are normally not covered by the risk-based capital standards (e.g., foreign exchange contracts with an original maturity of 14 calendar days or less and contracts traded on exchanges that require daily payment of variation margin), the reporting bank may elect to consistently either include or exclude the fair values of all such derivative contracts when determining the net current credit exposure for that agreement.

The definition of a legally enforceable bilateral netting agreement for purposes of this item is the same as that set forth in the risk-based capital rules. These rules require a written bilateral netting contract that creates a single legal obligation covering all included individual contracts and that does not contain a walkaway clause. The bilateral netting agreement must be supported by a written and reasoned legal opinion representing that an organization's claim or obligation, in the event of a legal challenge, including one resulting from default, insolvency, bankruptcy, or similar circumstances, would be found by the court and administrative authorities of all relevant jurisdictions to be the net sum of all positive and negative fair values of contracts included in the bilateral netting contract.

**2** **Notional principal amounts of off-balance-sheet derivative contracts**. Report in the appropriate subitem and column below the notional amount or par value of off-balance-sheet contracts included in Schedule RC-L, item 14, that are subject to risk-based capital requirements. Such contracts include swaps, forwards, and purchased options. Report notional amounts and par values in the column corresponding to the contract's remaining

## Memoranda

**Item No.** **Caption and Instructions**

**2** (cont.) term to maturity from the report date. Remaining maturities are to be reported as (1) one year or less in column A, (2) over one year through five years in column B, or (3) over five years in column C.

Do not report the notional amount for single currency interest rate swaps in which payments are made based upon two floating rate indices, so-called floating/floating or basis swaps; foreign exchange contracts with an original maturity of 14 days or less; and futures contracts.

The notional amount or par value to be reported for an off-balance-sheet derivative contract with a multiplier component is the contract's effective notional amount or par value. (For example, a swap contract with a stated notional amount of $1,000,000 whose terms called for quarterly settlement of the difference between 5% and LIBOR multiplied by 10 has an effective notional amount of $10,000,000.)

The notional amount to be reported for an amortizing off-balance-sheet derivative contract is the contract's current (or, if appropriate, effective) notional amount. This notional amount should be reported in the column corresponding to the contract's remaining term to final maturity.

For descriptions of "interest rate contracts," "foreign exchange contracts," "commodity and other contracts," and "equity derivative contracts," refer to the instructions for Schedule RC-L, item 14.

**2.a** Interest rate contracts. Report the remaining maturities of interest rate contracts that are subject to risk-based capital requirements.

**2.b** Foreign exchange contracts. Report the remaining maturities of foreign exchange contracts that are subject to risk-based capital requirements.

**2.c** Gold contracts. Report the remaining maturities of gold contracts that are subject to risk-based capital requirements.

**2.d** Other precious metals contracts. Report the remaining maturities of other precious metals contracts that are subject to risk-based capital requirements. Report all silver, platinum, and palladium contracts.

**2.e** Other commodity contracts. Report the remaining maturities of other commodity contracts that are subject to risk-based capital requirements. For contracts with multiple exchanges of principal, notional amount is determined by multiplying the contractual amount by the number of remaining payments (i.e., exchanges of principal) in the derivative contract.

**2.f** Equity derivative contracts. Report the remaining maturities of equity derivative contracts that are subject to risk-based capital requirements.

# OPTIONAL NARRATIVE STATEMENT CONCERNING THE AMOUNTS REPORTED IN THE REPORTS OF CONDITION AND INCOME

The management of the reporting bank may, if it wishes, submit a brief narrative statement on the amounts reported in the Reports of Condition and Income. This optional statement will be made available to the public, along with the publicly available data in the Reports of Condition and Income, in response to any request for individual bank report data. However, the information reported in column A and in all of Memorandum item 1 of Schedule RC-N is regarded as confidential and will not be released to the public. BANKS CHOOSING TO SUBMIT THE NARRATIVE STATEMENT SHOULD ENSURE THAT THE STATEMENT DOES NOT CONTAIN THE NAMES OR OTHER IDENTIFICATIONS OF INDIVIDUAL BANK CUSTOMERS, REFERENCES TO THE AMOUNTS REPORTED IN THE CONFIDENTIAL ITEMS IN SCHEDULE RC-N, OR ANY OTHER INFORMATION THAT THEY ARE NOT WILLING TO HAVE MADE PUBLIC OR THAT WOULD COMPROMISE THE PRIVACY OF THEIR CUSTOMERS. Banks choosing not to make a statement may check the "No comment" box and should make no entries of any kind in the space provided for the narrative statement; i.e., DO NOT enter in this space such phrases as "No statement," "Not applicable," "N/A," "No comment," and "None."

The optional statement must be entered on the sheet provided by the agencies. The statement should not exceed 100 words. Further, regardless of the number of words, the statement must not exceed 750 characters, including punctuation, indentation, and standard spacing between words and sentences. If any submission should exceed 750 characters, as defined, it will be truncated at 750 characters with no notice to the submitting bank and the truncated statement will appear as the bank's statement both on agency computerized records and in computer-file releases to the public.

All information furnished by the bank in the narrative statement must be accurate and not misleading. Appropriate efforts shall be taken by the submitting bank to ensure the statement's accuracy. The statement must be signed, in the space provided, by a senior officer of the bank who thereby attests to its accuracy.

If, subsequent to the original submission, material changes are submitted for the data reported in the Reports of Condition and Income, the existing narrative statement will be deleted from the files, and from disclosure; the bank, at its option, may replace it with a statement, under signature, appropriate to the amended data.

The optional narrative statement will appear in agency records and in release to the public exactly as submitted (or amended as described in the preceding paragraph) by the management of the bank (except for the truncation of statements exceeding the 750-character limit described above). THE STATEMENT WILL NOT BE EDITED OR SCREENED IN ANY WAY BY THE SUPERVISORY AGENCIES FOR ACCURACY OR RELEVANCE. DISCLOSURE OF THE STATEMENT SHALL NOT SIGNIFY THAT ANY FEDERAL SUPERVISORY AGENCY HAS VERIFIED OR CONFIRMED THE ACCURACY OF THE INFORMATION CONTAINED THEREIN. A STATEMENT TO THIS EFFECT WILL APPEAR ON ANY PUBLIC RELEASE OF THE OPTIONAL STATEMENT SUBMITTED BY THE MANAGEMENT OF THE REPORTING BANK.