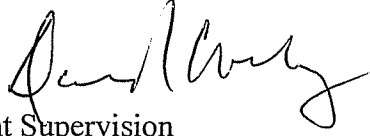


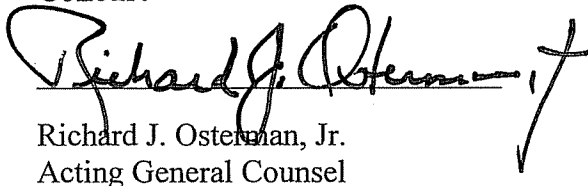
July 15, 2014

MEMORANDUM TO: Board of Directors
FROM: Doreen R. Eberley, Director 
Division of Risk Management Supervision
SUBJECT: *Final Rule: Advanced Approaches Risk-Based Capital Rule: Revisions to the Definition of Eligible Guarantee*

Summary: On July 9, 2013, the FDIC Board of Directors (Board) adopted an interim final rule that comprehensively revised the general risk-based and leverage capital rules for state nonmember banks and state savings associations (FDIC-supervised institutions). The interim final rule adopted a definition of eligible guarantee that requires all eligible guarantees to be provided by an eligible guarantor. This definition, however, inadvertently limited the recognition of eligible guarantees for wholesale credit exposures under the advanced approaches risk-based capital rule as incorporated into part 324, subpart E of the 2013 capital rule (advanced approaches). To address this situation, on April 8, 2014, the Board approved publication of a joint notice of proposed rulemaking (NPR) that proposed to remove the requirement that an eligible guarantee be made by an eligible guarantor for purposes of calculating the risk-weighted assets of an exposure (other than a securitization exposure) under the advanced approaches. The FDIC received two comments and after careful consideration, staff recommends adoption of the NPR without change as a final rule (Final Rule).

Recommendation: That the Board issue the attached Final Rule and authorize its publication in the *Federal Register*.

Concur:


Richard J. Osterman, Jr.
Acting General Counsel

Discussion:

In 2013, the FDIC, Office of the Comptroller of the Currency (OCC), and Board of Governors of the Federal Reserve System (Federal Reserve) (collectively, the agencies) comprehensively revised and strengthened their respective regulatory capital frameworks (2013 revised capital rule).¹ Among other provisions, the 2013 revised capital rule included a definition of eligible guarantee for purposes of both Subpart D (standardized approach) and the advanced approaches.² The definition of “eligible guarantee” requires that an “eligible guarantor” must provide the eligible guarantee.

An eligible guarantor under the 2013 capital rule includes a sovereign, the Bank for International Settlements, the International Monetary Fund, the European Central Bank, the European Commission, a Federal Home Loan Bank, Federal Agricultural Mortgage Corporation, a multilateral development bank, a depository institution, a bank holding company, a savings and loan holding company, a credit union, a foreign bank, or a qualifying central counterparty. It may also include an entity (other than a special purpose entity) that at the time the guarantee or anytime thereafter, has issued and outstanding an unsecured debt security that is investment grade; whose creditworthiness is not positively correlated with the credit risk of the exposures for which it has provided guarantees; and that is not an insurance company engaged predominately in the business of providing credit protection (such as a monoline bond insurer or re-insurer).

Prior to the promulgation of the 2013 capital rules, the agencies’ advanced approaches rules (for example, the FDIC’s capital rules in Appendix D of Part 325) did not require that

¹ The Board and the OCC issued a joint final rule on October 11, 2013 (78 FR 62018) and the FDIC issued a substantially identical interim final rule on September 10, 2013 (78 FR 55340). On April 8, 2014, the FDIC adopted the interim final rule as a final rule with no substantive changes. 79 FR 20754 (April 14, 2014).

² 12 CFR 324.2.

eligible guarantees be provided by a defined eligible guarantor. In developing the 2013 capital rules, the agencies' intention was to keep the same approach.

Accordingly, the requirement in the 2013 revised capital rules that eligible guarantees be provided only by eligible guarantors unintentionally limited the risk-based capital recognition of guarantees for wholesale exposures under the advanced approaches. To address this issue, FDIC staff, together with staffs of the Federal Reserve and the OCC, proposed an NPR that would reinstate the guarantee requirements of the credit risk mitigation framework of the advanced approaches, which, as previously stated, the banking agencies had not intended to change in the 2013 revised capital rules. On April 8, 2014, the Board approved the FDIC's publication of the NPR in the *Federal Register* with a comment period ending June 13, 2014.³

The agencies received two comments, one from a monoline insurance company and one from a trade association. The trade association fully supported the proposed rule and requested that advanced approaches banking organizations be permitted to adopt the rule as finalized prior to the official effective date in order to facilitate consistent public disclosures. The monoline insurance company requested that the definition of eligible guarantor be expanded to include monoline insurers that meet certain conditions. FDIC staff, together with staffs of the Federal Reserve and the OCC, believes that the commenter's proposed expansion of the definition of eligible guarantor would be contrary to objectives of the capital framework to mitigate interconnectedness and systemic vulnerabilities. As stated in the preamble of the 2013 capital rule, guarantees issued by monoline bond insurers can exhibit significant wrong-way risk. Therefore, the Final Rule adopts the NPR without change.

The final rule would modify the definition of eligible guarantee to reinstate the requirements of the credit risk mitigation framework of the advanced approaches. The

³ 79 FR 24618 (May 1, 2014)

requirement that the eligible guarantee be made by an “eligible guarantor” would be removed with respect to wholesale exposures for advanced approaches banking organizations. Guarantees that serve for credit risk mitigation purposes under the standardized approach and under the securitization framework of the advanced approaches continue to be restricted to guarantees provided by eligible guarantors. Further, this revision would not affect the calculation of the risk-based capital floor requirements under the standardized approach, which serves as a floor for the risk-based capital requirements applicable to advanced approaches banking organizations. If approved, the Final Rule is effective September 1, 2014; however, advanced approaches banking organizations may elect to adopt the requirements earlier than the effective date.

Conclusion

FDIC staff recommends that the FDIC Board adopt the attached Final Rule and authorize its publication in the *Federal Register*.

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