FDIC

Federal Deposit Insurance Corporation
550 17th Street NW, Washington, D.C. 20429-9990

Financial Institution Letter
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MARKET RISK CAPITAL

Applicability of Market Risk Capital Rules

Summary: Banks are reminded that reporting a significant amount of trading assets on the balance sheet, or increasing the percentage of assets reported as trading assets, may subject a bank to the market risk capital requirements (Part 325, Appendix C, of the FDIC's Rules and Regulations). In general, these requirements are applicable to banks whose gross "trading activity" equals $1 billion or more, or 10 percent or more of total assets. Banks that adopt Financial Accounting Standards Board Statement No. 159, *The Fair Value Option for Financial Assets and Liabilities* (FAS 159), and apply this option to securities should determine whether the resulting designation of these securities as trading would result in the application of the market risk capital requirements. The market risk capital rules require banks to have certain risk measurement systems in place prior to conducting trading activity that meets the size criteria outlined above. Institutions that expect to exceed the threshold minimums should contact their FDIC Regional Office in advance to discuss plans and preparations for complying with the market risk capital requirements.

Distribution:
FDIC-Supervised Banks (Commercial and Savings)

Suggested Routing:
Chief Executive Officer
Chief Financial Officer
Chief Risk Officer

Related Topics:
Risk-Based Capital Rules
12 CFR Part 325
Appendix C: Market Risk

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Highlights:

- FAS 159 requires that securities to which the fair value option is applied be reported as trading securities. For most banks, FAS 159 is effective on January 1, 2008; however, early adoption is permitted under certain conditions.
- Market risk capital requirements may apply to banks with gross trading assets and liabilities of either 10 percent or more of quarter-end total assets or $1 billion or more as reported on the most recent quarterly Call Report.
- Banks that report significant amounts of securities as trading securities as a result of FAS 159, or for other reasons, could become subject to the market risk capital requirements as a result of the 10 percent of total assets threshold.
- Banks that are subject to market risk capital requirements are required to measure market risk using a Value-at-Risk (VaR) model that meets the requirements set forth in the market risk capital rules.
- Banks whose trading activity is nearing or exceeding the threshold minimums should contact their FDIC Regional Office to discuss their plans regarding the adoption of the risk measurement and management requirements set forth in Appendix C.
- The market risk capital rules are currently under review. Proposed changes to the market risk rules are set forth in the federal banking agencies' Joint Notice of Proposed Rulemaking (see FIL 87-2006, dated September 25, 2006).