

DEPARTMENT OF REGULATORY AGENCIES

Division of Banking

TRUST COMPANIES

3 CCR 701-6

[Editor's Notes follow the text of the rules at the end of this CCR Document.]

TC4 Assessments and Fees [Section 11-109-303, C.R.S.]

(Repealed and recodified in 3 CCR 701-10 AR16)

TC5 Investment in Small Business Investment Companies [Section 11-109-902, C.R.S] [Expired 5/15/07 per House Bill 07-1167]

TC6 Collateralization of Deposits [Section 11-109-104, C.R.S.]

- A. On or after December 31, 1990, no trust company shall accept or hold savings deposits, time deposits, or certificates of deposit pursuant to Section 11-109-201 (1)(d), C.R.S., unless such deposits are insured by the Federal Deposit Insurance Corporation (FDIC) or its successor. A trust company is not authorized to receive and maintain transaction deposit accounts pursuant to Section 11-109-201(2), C.R.S.

TC7 Generally Accepted Accounting Principles [Section 11-109-402, C.R.S.]

- A. Generally accepted accounting principles (GAAP) as defined in this Rule shall consist of those opinions and statements generally recognized and supported by the Accounting Principles Board (APB) or the Financial Accounting Standards Board (FASB).
- B. While it is the Banking Board's intention to require that GAAP be followed whenever appropriate, certain statements filed by trust companies with various state and federal regulatory agencies are supervisory and regulatory documents, not primarily accounting documents. Because of the special supervisory, regulatory, and economic policy needs of trust company reports, the instructions do not always follow GAAP. In reporting transactions not covered in principle by regulatory instructions, trust companies may follow GAAP. However, in such circumstances, unless the trust company has already obtained a ruling from another regulatory agency pursuant to the policies expressed in Section 11-101-102, C.R.S., a specific ruling shall be sought promptly from the Banking Board.
- C. References: GAAP are issued by the FASB which is an arm of the Financial Accounting Foundation, an independently chartered institution. The APB is a committee of the American Institute of Certified Public Accountants. This Rule does not include amendments to or editions of the referenced material later than the effective date of this Rule. For more detailed information pertaining to this Rule, please contact the Secretary to the Colorado State Banking Board at 1560 Broadway, Suite 1175, Denver, Colorado 80202, (303) 894-7584.

TC8 Dividends [Section 11-109-501, C.R.S.]

A. Purpose

This Rule applies restrictions to the declaration and payment of dividends by a state chartered trust company.

B. Definitions

For the purposes of this Rule, the following definitions apply:

1. Capital surplus means the total of surplus as reportable in the trust company's Report of Condition and Income and surplus on perpetual preferred stock.
2. Retained net income means the net income of a specified period less the total amount of all dividends declared in that period.

C. Earnings Limitation on Payment of Dividends

Unless the dividend is approved by the Banking Board, a trust company shall not declare a dividend if the total amount of all dividends, including the proposed dividend, declared by such trust company in any calendar year exceeds the total of the trust company's retained net income of that year to date, combined with its retained net income of the preceding two years. The trust company's net income during the current year and its retained net income from the prior two calendar years is reduced by any net losses incurred in the current or prior two years, and any required transfers to surplus or to a fund for the retirement of preferred stock.

D. Date of Declaration of Dividend

The trust company shall use the date a dividend is declared for the purposes of determining compliance with this Rule.

TC9 Investment Limitations [Section 11-109-902(5), C.R.S.]

A. A trust company may, for its own account, purchase Type I securities in an unlimited amount, subject to the exercise of prudent judgment.

B. A trust company may, for its own account, purchase Type II, III, IV, and V securities, as described in 12 CFR Part 1, subject to the following restrictions:

1. Obligations of any issuer may be purchased up to a limit of 15 percent of the trust company's total capital provided that the purchase is based on adequate evidence of the maker's ability to perform,
2. Obligations of issuers having a maturity date of less than five (5) years may be purchased not to exceed 10 percent of the total capital, provided that the purchase is based on adequate evidence of the maker's ability to perform. This limitation shall be separate from and in addition to the limitation contained in Paragraph (B)(1).
3. The limitations prescribed in Paragraph (B)(1) and/or Paragraph (B)(2) of this Rule are reduced to 5 percent of total capital when purchase judgment is predicated on reliable estimates as described in 12 CFR Part 1.

4. Every trust company shall maintain in its files credit information adequate to demonstrate that it exercised prudence in its decision to purchase and to retain any security in its investment portfolio. Failure to maintain such information could result in the determination that the security is not a permissible trust company investment.

C. Reference

1. 12 CFR Part 1 was issued by the Comptroller of Currency effective December 2, 1996.
2. This Rule does not include amendments to or editions of the referenced material later than December 2, 1996. A copy of 12 CFR Part 1 may be examined at any State Publications Depository.
3. For more detailed information pertaining to these provisions, please contact the Secretary to the Colorado State Banking Board at 1560 Broadway, Suite 1175, Denver, Colorado 80202, 303-894-7584.

TC10 Reports of New Executive Officers, Directors, and Persons in Control and Related Late Filing Penalty [Section 11-109-402(5) and (6), C.R.S.]

- A. Any person who becomes an executive officer, director, or person responsible, directly or indirectly, for the management, control, or operation of a trust company, must notify the Division of Banking in writing within ninety (90) days thereafter.

The written notice must include a statement describing any civil or criminal offenses of which such person has been found guilty or liable by any federal or state court or federal or state regulatory agency.

- B. In addition, any person who becomes an executive officer, director, or person responsible, directly or indirectly, for the management, control, or operation of a trust company, must file a biographical report with the Division within ninety (90) days thereafter, if:

1. The trust company has been chartered less than two (2) years;
2. Within the preceding two (2) years, the trust company has undergone a change in control that required a notice to be filed pursuant to Section 11-109-401(2), C.R.S.;
3. Within the preceding two (2) years, the holding company became a registered holding company, unless the holding company is owned or controlled by a registered holding company, or the holding company was established in a reorganization in which substantially all of the shareholders of the holding company were shareholders of the trust company prior to the holding company's formation; or
4. The trust company or holding company is not in compliance with all minimum capital requirements applicable to the institution as determined on the basis of the institution's most recent report of condition, examination, or is otherwise in a troubled condition as indicated by a composite rating of 3, 4, or 5 at the institution's most recent examination by a state or federal banking regulator.

The biographical report to be filed with the Division of Banking may be either on the form provided by the Division of Banking or the form filed with the institution's federal regulator for reporting the change of executive officer, director, or person in control.

- C. For the purposes of this Rule, except as provided in Paragraph (D), the term “director” does not include an advisory director who:
1. Is not elected by the shareholders of the trust company;
 2. Is not authorized to vote on any matters before the board of directors; and
 3. Provides solely general policy advice to the board of directors.
- D. The Banking Board or the Division of Banking may otherwise determine that additional reporting is required of any person who becomes an executive officer, director, or person in control. Written notice will be provided by the Division of Banking to such person of any additional requirements.
- E. The Banking Board may assess a \$25.00 per day penalty for late filing of reports of new executive officers, directors, and persons in control that are required by Section 11-109-402(5) and (6), C.R.S., and this Rule. Said penalty may be waived by the Banking Board pursuant to statute. Filing of an incorrect report form is not grounds for the waiving of the penalty.

TC11 Scope of Directors' Examinations [Section 11-109-402(2), C.R.S.]

A. Definitions

For the purposes of this Rule, the term “reviewer” shall mean such public accountant or other independent person(s) as determined by the Banking Board.

B. Examination Scope

For the purposes of Section 11-109-402(2), C.R.S., a trust company (institution), at a minimum, shall perform annually the procedures as set forth in Appendix A as the scope of a directors' examination. The recommended procedures are intended to address the high risk areas common to all financial institutions. However, each institution must review its own particular business and determine if additional procedures are required to cover other high risk areas. The reviewer shall be informed of, and permitted access to, all examination reports, administrative orders, and any additional communications between the institution and the Division of Banking, including the Colorado State Banking Board, as well as the appropriate federal regulatory agency. The reviewer shall obtain the institution management's written representation that he or she has been informed of, and granted access to, all such documents prior to completion of the field work.

C. Extent of Testing

Where the procedures set forth in Appendix A require testing or determinations to be made, sampling may be used. Both judgmental and statistical sampling may be acceptable methods of selecting samples to test. Sample sizes should be consistent with generally accepted auditing standards, or as agreed upon by the reviewer and the client institution. In any event, the sampling method and extent of testing, including the sample size(s) used, shall be disclosed in the directors' examination report.

D. Reports to be Filed with the Division of Banking

After the completion of the procedures, or agreed-upon procedures, set forth in Appendix A, the independent reviewer shall evaluate the results of his audit work and promptly prepare and submit a report addressed to the board of directors of the institution. The report shall detail the findings and suggestions resulting from performance of the auditing procedures. Independent reviewers shall include in the report, at a minimum:

1. Financial statements (balance sheet and statement of earnings as of the examination date).
2. The accounts or items on which the procedures were applied.
3. The sampling methods used.
4. The procedures and agreed-upon extent of testing performed.
5. The accounting basis, either generally accepted accounting principles (GAAP) or regulatory required accounting, on which the accounts or items being audited are reported.
6. The reviewer's findings.
7. The as of date that the procedures were performed.

The reviewer shall sign and date the report. The report shall also disclose the reviewer's business address.

The institution must send a copy of the report, the engagement letter, and any management letter or similar letter of recommendation to the Division of Banking and, if applicable, to the appropriate federal regulators within thirty (30) days after its receipt, but no later than one hundred fifty (150) days after the date of examination. In addition, each institution shall promptly notify the Division of Banking when a reviewer is engaged to perform a directors' examination and when a change in its reviewer occurs.

E. References

Generally accepted accounting principles are issued by the Financial Accounting Standard Board which is an arm of the Financial Accounting Foundation, an independently chartered institution. Section 23A of the Federal Reserve Act, also known as 12 USC 371c, is a law enacted by the United States Congress and administered by the Board of Governors of the Federal Reserve System. Regulation O of the Board of Governors of the Federal Reserve System, also known as 12 CFR 215, is a regulation enacted by the Federal Reserve Board under the authority granted by the United States Congress and administered by the Board of Governors of the Federal Reserve System. This Rule does not include amendments to or editions of the referenced materials later than the effective date of the Rule, October 24, 1990.

For more detailed information pertaining to this Rule, please contact the secretary to the Colorado State Banking Board at 1560 Broadway, Suite 975, Denver, CO 80202, 303-894-7575.

APPENDIX A - TC11

For the purpose of Section 11-109-402(2), C.R.S., a trust company (institution), at a minimum, shall have the following procedures performed annually.

A. Securities

1. Review the investment policies and procedures established by the institution's board of directors. Review the board of directors', or investment committee, minutes for evidence that the policies and procedures are periodically reviewed and approved. The policies and procedures should include, but not be limited to:

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- a. Investment objectives, including use of “available for sale,” “held for sale” and trading activities;
 - b. Permissible types of investments;
 - c. Diversification guidelines to prevent undue concentration;
 - d. Maturity schedules;
 - e. Limitation on quality ratings;
 - f. Hedging activities and other uses of futures, forwards, options, and other financial instruments;
 - g. Handling exceptions to standard policies;
 - h. Valuation procedures and frequency;
 - i. Limitations on the investment authority of officers; AND
 - j. Frequency of periodic reports to the board of directors on securities holdings.
2. Test the investment procedures and ascertain whether information reported to the board of directors, or investment committee, for securities transactions is in agreement with the supporting data by comparing the following information on such reports to the trade tickets for a sample of items, including futures, forwards, and options:
 - a. Descriptions;
 - b. Interest rate;
 - c. Maturity;
 - d. Par value, or number of shares;
 - e. Cost; and
 - f. Market value on date of transaction, if different than cost.
 3. Using the same sample items, analyze the securities register for accuracy and confirm the existence of the sample items by examining securities physically held in the institution and confirming the safekeeping of those securities held by others.
 4. Balance investment subledger(s) or reconcile computer-generated trial balances with the general ledger control accounts for each type of security.
 5. Review policies and procedures for controls that are designed to ensure that unauthorized transactions do not occur. Ascertain through reading of policies, procedures, and board of directors' minutes whether investment officers and/or appropriate committee members have been properly authorized to purchase/sell investments and whether there are limitations or restrictions on delegated responsibilities.
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6. Obtain a schedule of the book, par, and market values of securities, as well as the rating classifications. Test the accuracy of the market values of a sample of securities and compare the ratings listed to see that they correspond with those of the rating agencies. Review the institution's documentation on any permanent declines in value that have occurred among the sample of securities to determine that any recorded declines in market value are appropriately computed. Examine the institution's computation of the allowance account for securities, if any, for proper presentation and adequacy.
7. Test securities income and accrued interest by:
 - a. Determining the institution's method of calculating and recording interest accruals;
 - b. Obtaining trial balances of accrued interest;
 - c. Testing the reconciliation of the trial balances to the general ledger;
 - d. Determining that interest accruals are not made on defaulted issues;
 - e. Selecting items from each type of investment and money market holding:
 - (1) Determining the stated interest rate and most recent interest payment date of coupon instruments by reference to sources of such information that are independent of the institution;
 - (2) Testing timely receipt of interest payments and correctness of entries to applicable general ledger accounts;
 - (3) Calculating accrued interest and comparing it to the trial balance; and
 - (4) Reviewing recorded book value for appropriate accretion of discount and amortization of premium; and
 - f. Performing an analytical review of yields on each type of investment and money market holdings for reasonableness.
8. Review investment accounts for volume of purchases, sales activity and length of time securities have been held. Inquire as to the institution's intent and ability to hold securities until maturity. If there is frequent trading in an investment account, such activity may be inconsistent with the notion that the institution has the intent and ability to hold securities to maturity. Test gains and losses on disposal of investment securities by sampling sales transactions and:
 - a. Determining sales prices by examining invoices or brokers' advices;
 - b. Checking for the use of trade date accounting and the computation of book value on trade date;
 - c. Determining that the general ledger has been properly relieved on the investment, accrued interest, premium, discount and other related accounts;
 - d. Recomputing the gain or loss and compare to the amount recorded in the general ledger; and

- e. Determining that the sales were approved by the board of directors or a designated committee or were in accordance with policies approved by the board of directors.
 - 9. Determine that sufficient and adequate securities have been collateralized against uninsured deposits, if applicable.
- B. Allowance for Fee Receivables
- 1. Review policies and procedures for ensuring the collectibility of fees due.
 - 2. Test charge-offs and recoveries for proper authorization and/or reporting by reference to the board of directors' minutes.
 - 3. Review the institution's computation of the amount needed in the allowance as of the end of the most recent quarter. Documentation should include consideration of the following matters:
 - a. Aging of delinquent fees;
 - b. Ability to offset fees to account assets;
 - c. Valuation and marketability of assets in fee delinquent accounts;
 - d. Trends in the level of delinquent fees as compared with previous loss and recovery experience;
 - e. Monitoring controls; and
 - f. Collection efforts, both internal and through outside sources.
- C. Insider Transactions

NOTE: For purposes of this section of the procedures, insiders include all affiliates of the institution, including its parent holding company, and all subsidiaries of the institution, as those terms are defined in section 23A of the Federal Reserve Act, as well as the institution's executive officers, directors, principal shareholders, and their related interests, as those terms are defined in section 215.2 of Federal Reserve Regulation O.

- 1. Review the institution's policies and procedures to ensure that extensions of credit to, and other transactions with, insiders are addressed. Ascertain that the policies include specific guidelines defining fair and reasonable transactions between the institution and insiders, and test insider transactions for compliance with the guidelines and statutory and regulatory requirements. Ascertain that the policies and procedures on extensions of credit comply with the requirements of Federal Reserve Regulation O.
- 2. Obtain an institution-prepared list of insiders, including any business relationships the institution may have other than as a nominal customer. Also obtain a list of extensions of credit to, and other transactions that the institution, its affiliates, and its subsidiaries have had with, insiders that are outstanding as of the audit date or that have occurred since the prior year's external auditing procedures were performed. Compare the lists to those prepared for the prior year's external auditing program to test for completeness.

3. Review the institution's policies and procedures to ensure that expense accounts of individuals who are executive officers, directors, and principal shareholders are addressed and test a sample of the actual expense account records for compliance with the policies and procedures.

D. Internal Controls - General Accounting and Administrative Controls

1. Review the board of directors' minutes to verify that account reconciliation policies have been established and approved and are reviewed periodically by the board of directors. Determine that management has implemented appropriate procedures to ensure the timely completion of reconciliations of accounting records and the timely resolution of reconciling items.
2. Determine whether the institution's policies regarding segregation of duties and required vacations for employees, including those involved in the EDP function, have been approved by the board of directors and verify that the policies and the implementing procedures established by management are periodically reviewed, are adequate, and are followed.
3. Confirm a sample of deposits in each of the various types of deposit accounts maintained by the institution. Inquire about controls over dormant deposit accounts.
4. Test to determine that reconciliations are prepared for all significant asset and liability accounts, such as "due from" accounts; demand deposits; NOW accounts; money market deposit accounts; other savings deposits; certificates of deposit; and other time deposits and their related accrued interest accounts, if any. Review reconciliations for:
 - a. Timeliness and frequency;
 - b. Accuracy and completeness; and
 - c. Review by appropriate personnel with no conflicting duties.
5. Compare a sample of balances per reconciliations to the general ledger and supporting trial balances.
6. Examine detail and aging of a sample of reconciling items from the accounts whose reconciliations have been tested and reviewed and a sample of items in suspense, clearing, and work-in-process accounts by:
 - a. Testing aging;
 - b. Determining whether items are followed up on and appropriately resolved on a timely basis; and
 - c. Discussing items remaining on reconciliations and in the suspense account with appropriate personnel to ascertain whether any should be written off.

Review a sample of charged-off reconciling and suspense items for proper authorization.
7. Verify through inquiry and observation that the institution maintains adequate records of its off-balance sheet activities. Review the institution's procedures to determine whether probable or reasonably possible losses exist.

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- E. Internal Controls - Electronic Data Processing Controls
1. Read the board of directors' minutes to determine whether the board of directors has reviewed and approved the institution's electronic data processing (EDP) policies, including those regarding outside servicers, if any, and the in-house use of individual personal computers (PCs) and personalized programs for official institution records, at least annually, confirm that management has established appropriate implementing procedures, and verify the institution's compliance with these policies and procedures.
 - a. The policies and procedures for either in-house processing or use of an outside service center should include:
 - (1) A contingency plan for continuation of operations and recovery when power outages, natural disasters, or other threats could cause disruption and/or major damage to the institution's data processing support, including compatibility of the servicer's plan with that of the institution;
 - (2) Requirements for EDP-related insurance coverage that include the following provisions:
 - (a) Extended blanket bond fidelity coverage to employees of the institution or servicer;
 - (b) Insurance on documents in transit, including cash letters; and
 - (c) Verification of the insurance coverage of the institution or service bureau and the courier service;
 - (3) Review of exception reports and adjusting entries approved by supervisors and/or officers;
 - (4) Controls for input preparation and control and output verification and distribution;
 - (5) "Back-up" of all systems, including off-premises rotation of files and programs;
 - (6) Security to ensure integrity of data and system modifications; and
 - (7) Necessary detail to ensure an audit trail.
 - b. When an outside service center is employed, the policies and procedures should address the following additional items:
 - (1) The requirement for a written contract for each automated application detailing ownership and confidentiality of files and programs, fee structure, termination agreement, and liability for documents in transit;
 - (2) Review of each contract by legal counsel; and
 - (3) Review of each third party review of the service bureau, if any.
 2. In the area of general EDP controls, determine through inquiry and observation that policies and procedures have been established for:
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- a. Management and user involvement and approval of new or modified application programs;
 - b. Authorization, approval, and testing of system software modifications;
 - c. The controls surrounding computer operations processing;
 - d. Restricted access to computer operations facilities and resources including:
 - (1) Off-premises storage of master disks and PC disks;
 - (2) Security of the data center and the institution's PCs; and
 - (3) Use and periodic changing of passwords.
3. With respect to EDP applications controls, inquire about and observe:
- a. The controls over:
 - (1) Input submitted for processing;
 - (2) Processing transactions;
 - (3) Output;
 - (4) Applications on PCs; and
 - (5) Telecommunications both between and within institution offices.
 - b. The security over unissued or blank supplies of potentially negotiable items; and
 - c. The control procedures on wire transfers including:
 - (1) Authorizations and agreements with customers, including who may initiate transactions;
 - (2) Limits on transactions; and
 - (3) Call back procedures.
- F. Trust Function
- 1. Supervisory Review
 - a. Determine the significant functions of the department, including areas of responsibility within the department and the financial institution.
 - b. Review the institution's written policies to determine that sufficient guidelines are established to meet fiduciary responsibilities and to comply with applicable laws. Policies should include:
 - (1) Account acceptance;
 - (2) Closed account review;

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- (3) Investments;
 - (4) Account review;
 - (5) Discretionary distributions;
 - (6) Conflicts of interest; and
 - (7) Other as needed for scope of fiduciary activities.
 - c. Ascertain the qualifications of the staff and of the board of directors giving consideration to the nature of the fiduciary responsibilities accepted.
 - d. Determine if board policies are implemented and followed.
 - 2. Accounting and Physical Controls
 - a. Verify account assets. Include a confirmation from holders of assets retained outside the department.
 - b. Determine that the assets are adequately safeguarded, and held separately from other assets of the institution.
 - c. Verify that a vault record of assets under joint custody is maintained.
 - d. Verify prompt ledger control of assets, including worthless assets, received as original and subsequent deposits of assets, including stock splits and dividends.
 - e. Verify that fiduciary cash accounts are regularly and appropriately reconciled to demand deposit or money market account statements.
 - f. Verify that internal balancing control procedures are performed each time account ledgers are posted.
 - g. Verify that suspense or operating accounts are reconciled at least monthly, contain only appropriate items, and are cleared in a timely manner.
 - h. Reconcile or verify the proper reconciliation of each of the following to the department's general ledger at least quarterly:
 - (1) Income cash;
 - (2) Principal cash;
 - (3) Invested income;
 - (4) Invested principal;
 - (5) Each type of investment, such as stock, bonds, real estate loans and real estate; and
 - (6) Investments by issuer.
 - i. If applicable, verify reconciliations or reconcile outstanding bonds for bond trusteeships, or paying agent activities.
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- j. Verify the accurate payment of dividends.
3. Activity Control
- a. Verify fees paid to the trust company.
 - b. Verify proceeds from sales of assets to brokers' invoices, sellers' receipts, or other evidence of sales price.
 - c. Verify payment for purchases of assets to brokers' invoices, sellers' receipts, or other evidence of purchase price.
 - d. Verify accuracy of amounts and receipt of income from investments.
4. Compliance
- a. Verify that transactions between fiduciary accounts and directors, officers, or employees of the institution, its holding company or other related entities do not constitute self-dealing. In general, self-dealing is considered to exist when the fiduciary uses or obtains the property held in a fiduciary capacity for his or her own benefit.
 - b. Review fiduciary account holdings of the following items in light of self-dealing issues:
 - (1) Stock, obligations, repurchase agreements, or deposit accounts with the institution, its affiliates or other related organizations in which there exists such an interest that might affect the best judgment of the institution.
 - (2) Obligations of directors, officers and employees of the institution, its holding company or affiliates or other entities with whom there exists a connection that might affect the exercise of the best judgment of the institution.
 - c. Verify that all accounts for which the institution has investment responsibilities are reviewed by the board of directors or a committee thereof.
 - d. Verify that cash receipts are promptly invested or distributed.
 - e. Verify and review the annual audit of each collective investment fund.
5. Administrative Review
- a. Complete administrative reviews of all major account types, including but not limited to, personal trusts, estates, corporate trusts, collective investment funds, pension trusts and profit sharing trusts. An acceptable administrative review would perform the following practices:
 - (1) Determine that the original or authenticated copy of the governing instrument is on file;
 - (2) Determine that synoptic and history records are current, reliable and comprehensive;
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- (3) Determine that accounts are administered and invested in conformance with management policies, governing instruments, laws, regulations and sound fiduciary principles;
- (4) Determine that the minutes of the board of directors and committee meetings document the review of trust company activities; significant practices for the board of directors' review include the acceptance of new accounts, the closing of accounts and the review of discretionary payments of principal or income; and
- (5) Test the accuracy of account statements submitted to beneficiaries.

TC12 Qualifications for Independent Person(s) Assuming Responsibility for Due Care of Directors' Examinations [Section 11-109-402(2), C.R.S.]

A. Qualifications

The following persons may qualify to be responsible for conducting a directors' examination of a trust company:

1. A Certified Public Accountant(s) who holds an active certificate under the laws of this state, or who may practice in this state under a reciprocal agreement between Colorado and the holder's state of certification.
2. A qualified independent person(s) or firm whose credentials have been submitted to and approved by the Colorado State Banking Board to conduct such examinations. The Banking Board will take into consideration such things as past proven work of the person or firm, professional reputation, training and education, and capacity to perform the examination in a timely manner.
3. The Banking Board reserves the right to revoke any previously approved qualification for due cause.

B. Independence

A person who conducts or reviews and/or approves a directors' examination of a trust company must be independent with respect to the trust company in fact and appearance.

Independence will be considered impaired if, for example, during the period of the directors' examination, or at the time of the issuing of the report, the person:

1. Was or is committed to acquire any direct, or material indirect, financial interest in the institution;
2. Is or was a trustee of any trust, or executor or administrator of any estate, if such trust or estate was or is committed to acquire any direct or material indirect financial interest in the institution;
3. Has or had any joint, closely-held business investment with the institution or any officer, director, or principal stockholder thereof that is material in relation to the net worth of either the institution or the person; or
4. Has or had any loan to or from the institution or any officer, director, or principal shareholder thereof other than loans of the following kinds made by a financial institution under normal lending procedures, terms, and requirements:

- a. Loans obtained by the person that are not material in relation to the net worth of the borrower;
- b. Home mortgages; and
- c. Other secured loans, except those secured solely by a guarantee of the person.

Independence will also be considered to be impaired if, during the period covered by the financial statements, during the period of the directors' examinations, or at the time of the issuing of the report, the person:

1. Was or is connected with the institution as a promoter, underwriter, voting trustee, director or officer, or in any capacity equivalent to that of a member of management or of an employee;
2. Was or is a trustee for any pension or profit sharing trust of the institution;
3. Received, or had a commitment to receive, other compensation from the institution or a third party for services or products of others to be procured by the institution; or
4. Received, or had a commitment from the institution to receive, a contingent fee. For this purpose, a contingent fee means compensation for the performance of services, payment of which or the amount of which is contingent upon the findings or results of such services.

TC13 Minimum Capital Ratios for Depository Trust Companies [Section 11-109-304, C.R.S.]

A. Purpose

The Colorado State Banking Board believes that a minimum leverage ratio is necessary because the risk-based capital guidelines detailed in Banking Board Rule TC14-Risk-Based Capital Definitions and Adequacy, that are designed solely as a measure of credit risk, create the possibility for significant leverage. Assets that have no credit risk receive a zero percent risk weight and, therefore, require no capital. However, the Banking Board believes that every institution should have at least a base level of capital as protection against risks not measured by the risk-based capital ratio.

B. Definitions: For the purposes of this Rule:

1. Adjusted total assets means the average total assets figure required to be computed for and stated in an institution's most recent quarterly Consolidated Report of Condition and Income (Call Report), minus end-of-quarter intangible assets, deferred tax assets, and credit-enhancing interest-only strips, that are deducted from Tier 1 capital, and minus nonfinancial equity investments for which a Tier 1 Capital deduction is required pursuant to Paragraph (C)(1)(h) of Banking Board Rule TC14. The Banking Board reserves the right to require an institution to compute and maintain its capital ratios on the basis of actual, rather than average, total assets when necessary to carry out the purposes of this Rule.
2. Tier 1 Capital means "Tier 1 Capital" as determined according to Banking Board Rule TC14-Risk Based Capital Definitions and Adequacy, including the deductions described therein.

3. Tier 2 Capital means "Tier 2 Capital" as determined according to Banking Board Rule TC14-Risk Based Capital Definitions and Adequacy, including the limitations described therein.
4. Total Capital means "Total Capital" as determined according to Banking Board Rule TC14-Risk Based Capital Definitions and Adequacy, including the deductions described therein.

C. Reservation of Authority

1. Deductions from capital. Notwithstanding the definitions of Tier 1 Capital and Tier 2 Capital, the Banking Board may find that a newly developed or modified capital instrument constitutes Tier 1 Capital or Tier 2 Capital, and may permit one or more institutions to include all or a portion of funds obtained through such capital instruments as Tier 1 or Tier 2 Capital, permanently or on a temporary basis, for the purpose of compliance with the Banking Board Rules.

Similarly, the Banking Board may find that a particular intangible asset, deferred tax asset or credit-enhancing interest-only strip need not be deducted from Tier 1 or Tier 2 Capital. Conversely, the Banking Board may find that a particular intangible asset, deferred tax asset, credit-enhancing interest-only strip or other Tier 1 or Tier 2 Capital component, has characteristics or terms that diminish its contribution to an institution's ability to absorb losses, and may require the deduction from Tier 1 or Tier 2 Capital of all of the component or of a greater portion of the component than is otherwise required.

2. Risk weight categories. Notwithstanding the risk categories in Banking Board Rule TC14, the Banking Board will look to the substance of the transaction and may find that the assigned risk weight for any asset, or the credit equivalent amount, or credit conversion factor for any off-balance sheet item does not appropriately reflect the risks imposed on an institution and may require another risk weight, credit equivalent amount, or credit conversion factor that the Banking Board deems appropriate. Similarly, if no risk weight, credit equivalent amount or credit conversion factor is specifically assigned, the Banking Board may assign any risk weight, credit equivalent amount, or credit conversion factor that the Banking Board deems appropriate. In making its determination, the Banking Board considers risks associated with the asset or off-balance sheet item as well as other relevant factors.

D. Initial Capital

No trust company shall be granted a charter unless it has paid-in capital stock of at least \$1,000,000, or such greater amount as the Banking Board may reasonably require. New trust companies will be required to maintain total capital in an amount necessary to satisfy minimum capital ratios, but not less than \$750,000.

E. Minimum Capital Ratios For Depository Trust Companies

1. Risk-based capital ratio. All institutions must have and maintain the minimum risk-based capital ratios as set forth in Banking Board Rule TC14.
2. Total asset leverage ratio (Leverage Ratio). All institutions must have and maintain Tier 1 Capital in an amount equal to at least 3.0 percent of adjusted total assets.

3. Additional leverage ratio requirements. An institution operating at or near the level in Paragraph (E)(2) of this Rule should have well-diversified risks, including no undue interest rate risk exposure; excellent control systems; good earnings; high asset quality; high liquidity; and well managed on- and off-balance sheet activities; and in general be considered a strong organization, rated composite 1 under the CAMELS rating system. For all but the most highly-rated institutions meeting the conditions set forth in this Paragraph, the minimum Tier 1 leverage ratio is 4 percent. In all cases, institutions should hold capital commensurate with the level and nature of all risks.

F. Establishment of Minimum Capital Ratios for an Individual Institution

1. Applicability

The Banking Board may require higher minimum capital ratios for an individual institution in view of its circumstances. For example, higher capital ratios may be appropriate for:

- a. A newly chartered institution;
- b. An institution receiving special supervisory attention;
- c. An institution that has, or is expected to have, losses resulting in capital inadequacy;
- d. An institution with significant exposure due to risks from concentrations of credit, certain risks arising from nontraditional activities, or management's overall inability to monitor and control financial and operating risks presented by concentrations of credit and nontraditional activities;
- e. An institution with significant exposure to declines in the economic value of its capital due to changes in interest rates;
- f. An institution with significant exposure due to fiduciary or operational risk;
- g. An institution exposed to a high degree of asset depreciation, or a low level of liquid assets in relation to short term liabilities;
- h. An institution exposed to a high volume of, or particularly severe, problem assets;
- i. An institution that is growing rapidly, either internally or through acquisition; or
- j. An institution that may be adversely affected by the activities or condition of its parent company, affiliate(s), or other persons or institutions including chain banking organizations, with which it has significant business relationships.

2. Standards for determination of appropriate individual minimum capital ratios. The appropriate minimum capital ratios for an individual institution cannot be determined solely through the application of a rigid mathematical formula or wholly objective criteria. The decision is necessarily based in part on subjective judgment grounded in Banking Board and Division of Banking expertise. The factors to be considered in the determination will vary in each case and may include, for example:

- a. The conditions or circumstances leading to the Banking Board's determination that higher capital ratios are appropriate or necessary for the institution;
- b. The exigency of those circumstances or potential problems;

- c. The overall condition, management strength, and future prospects of the institution and, if applicable, its parent company and/or affiliate(s);
 - d. The institution's liquidity, capital, risk asset and other ratios compared to the ratios of its peer group; and
 - e. The views of the institution's directors and senior management.
- G. Unsafe and unsound practice. Any institution that has less than its minimum leverage capital requirement is deemed to be engaged in unsafe and unsound practice. Except that such an institution that has entered into, and is in compliance with, a written agreement with the Banking Board, or has submitted to the Banking Board; and is in compliance with, a plan approved by the Banking Board to increase its Tier 1 leverage capital ratio to such a level as the Banking Board deems appropriate and to take such other action as may be necessary for the institution to be operated so as not to be engaged in such unsafe or unsound practice will not be deemed to be engaged in unsafe or unsound practice on account of its capital ratios. An institution must file a written capital restoration plan with the Banking Board within forty-five (45) days of the date that the institution receives notice or is deemed to have notice that the institution is undercapitalized, unless the Banking Board notifies the institution in writing that the plan is to be filed within a different period. The Banking Board is not precluded from taking any enforcement action against an institution with capital above the minimum requirement if the specific circumstances deem such action to be appropriate.
- H. Statute References to Capital
- 1. As referenced in the statutes, the following definitions will apply:
 - a. Section 11-109-306(1)(d), C.R.S., shall refer to the leverage ratio and Tier 1, Tier 2, and Total Capital.
 - b. Section 11-109-902(2), C.R.S., shall refer to Total Capital.
 - c. Section 11-109-902(3), C.R.S., shall refer to Total Capital.
 - d. Section 11-109-902(6), C.R.S., shall refer to Total Capital.
 - e. Section 11-109-902(7), C.R.S., shall refer to Total Capital.
 - f. Section 11-109-702(1), C.R.S., shall refer to the leverage ratio.

For more detailed information pertaining to these provisions, please contact the Secretary to the Colorado State Banking Board at 1560 Broadway, Suite 1175, Denver, Colorado 80202, (303) 894-7575.

TC13.5 Minimum Capital for Non-Depository Trust Companies

[Section 11-109-304, C.R.S.]

A. Purpose

The Colorado State Banking Board believes that trust companies should maintain certain minimum capital levels pursuant to policies set forth in Section 11-101-102, C.R.S., and relevant federal laws and regulations. Accordingly, Banking Board Rule TC13.5-Minimum Capital for Non Depository Trust Companies sets forth certain minimum capital requirements for non-depository trust companies.

B. Definitions: For the purpose of this Rule:

1. "Fiduciary Assets" means those assets held for benefit of, or in trust for others. The Trust Company may have investment discretion, or the investment authority may remain with the account holder or external manager.
2. Total capital means "total capital" as determined according to Banking Board Rule TC14 – Risk Based Capital Definitions and Adequacy, including the deductions described herein.

C. Initial Capital

No trust company shall be granted a charter unless it has paid-in capital of at least \$1,000,000, or such greater amount as the Banking Board may reasonably require.

D. Minimum Capital for Non-Depository Trust Companies

Non-depository trust companies must maintain total capital of not less than the greater of: (1) \$750,000, or (2) one tenth of one percent (.001) of fiduciary assets, such amount not to exceed five million (\$5,000,000).

E. Establishment of Minimum Capital for an Individual Institution

1. Applicability

The Banking Board may require higher minimum capital levels for an individual institution in view of its circumstances. For example, higher capital levels may be appropriate for:

- a. A newly chartered institution;
- b. An institution receiving special supervisory attention;
- c. An institution that has, or is expected to have, losses resulting in capital inadequacy;
- d. An institution with significant exposure due to risks from concentrations of credit, certain risks arising from nontraditional activities, or management's overall inability to monitor and control financial and operating risks presented by concentrations of credit and nontraditional activities;
- e. An institution with significant exposure to declines in the economic value of its capital due to changes in interest rates;
- f. An institution with significant exposure due to fiduciary or operational risk;
- g. An institution exposed to a high degree of asset depreciation or a low level of liquid assets in relation to short term liabilities;
- h. An institution exposed to a high volume of, or particularly severe, problem assets;
- i. An institution that is growing rapidly, either internally or through acquisition; or
- j. An institution that may be adversely affected by the activities or condition of its parent company, affiliate(s), or other persons or institutions including chain banking organizations, with which it has significant business relationships.

2. Standards for Determination of Appropriate Individual Minimum Capital. The appropriate minimum capital ratios for an individual institution cannot be determined solely through the application of a rigid mathematical formula or wholly objective criteria. The decision is necessarily based in part on subjective judgment grounded in Banking Board and Division of Banking expertise. The factors to be considered in the determination will vary in each case and may include, for example:
 - a. The conditions or circumstances leading to the Banking Board's determination that higher capital levels are appropriate or necessary for the institution;
 - b. The exigency of those circumstances or potential problems;
 - c. The overall condition, management strength, and future prospects of the institution and, if applicable, its parent company and/or affiliate(s);
 - d. The institution's liquidity, capital, risk asset and other ratios compared to the ratios of its peer group; and
 - e. The views of the institution's directors and senior management.
- F. Unsafe and unsound practice. Any institution that has less than its minimum capital requirement is deemed to be engaged in unsafe and unsound practice. Except that such an institution that has entered into, and is in compliance with, a written agreement with the Banking Board; or has submitted to the Banking Board, and is in compliance with, a plan approved by the Banking Board to increase its minimum capital to such a level as the Banking Board deems appropriate and to take such other action as may be necessary for the institution to be operated so as not to be engaged in such unsafe or unsound practice will not be deemed to be engaged in unsafe or unsound practice on account of its capital. An institution must file a written capital restoration plan with the Banking Board within forty-five (45) days of the date that the institution receives notice or is deemed to have notice that the institution is undercapitalized, unless the Banking Board notifies the institution in writing that the plan is to be filed within a different period. The Banking Board is not precluded from taking any enforcement action against an institution with capital above the minimum requirement if the specific circumstances deem such action to be appropriate.
- G. Compliance Date. Non-depository trust companies chartered prior to July 1, 2007 shall meet the minimum capital requirements of this rule no later than September 30, 2007.
- H. Statute References to Capital
 1. As referenced in the Colorado Revised Statutes, the following definitions will apply:
 - a. Section 11-109-306(1)(d), C.R.S., shall refer to the leverage ratio and Tier 1, Tier 2, and Total Capital;
 - b. Section 11-109-902(2), C.R.S., shall refer to Total Capital;
 - c. Section 11-109-902(3), C.R.S., shall refer to Total Capital;
 - d. Section 11-109-902(6), C.R.S., shall refer to Total Capital;
 - e. Section 11-109-902(7), C.R.S., shall refer to Total Capital;
 - f. Section 11-109-104(2), C.R.S., shall refer to Total Capital; and
 - g. Section 11-109-702(1), C.R.S., shall refer to Total Capital.

TC14 Risk-Based Capital Definitions and Adequacy [Section 11-103-201, C.R.S.]

A. Purpose.

An important function of the Banking Board and the Division of Banking is to evaluate the adequacy of capital maintained by each regulated institution. Such an evaluation involves the consideration of numerous factors, including the riskiness of an institution's assets and off-balance sheet items. This Rule implements the Banking Board's risk-based capital guidelines.

The risk-based capital ratio derived from these guidelines is an important factor in the Banking Board and the Division of Banking's evaluation of an institution's capital adequacy. However, because this measure addresses only credit risk, the 8 percent minimum ratio should not be viewed as the level to be targeted, but rather as a floor. The final supervisory judgment on an institution's capital adequacy is based on an individualized assessment of numerous factors, including those listed in Banking Board Rule CB101.51(E)(1). With respect to the consideration of these factors, the Banking Board and Division of Banking will give particular attention to any institution with significant exposure to declines in the economic value of its capital due to changes in interest rates. As a result, it may differ from the conclusion drawn from an isolated comparison of an institution's risk-based capital ratio to the 8 percent minimum specified in these guidelines. In addition to the standards established by these risk-based capital guidelines, all state-chartered trust companies must maintain a minimum capital-to-total assets ratio pursuant to Banking Board Rule TC13.

Certain components of capital, categories of on-balance sheet assets, and categories of off-balance sheet items appearing in this Rule may not apply to state chartered trust companies. Nothing in this Rule shall be construed to increase the powers of state chartered trust companies.

B. Definitions. For the purposes of this Rule, the following definitions apply:

1. "Adjusted carrying value" means the aggregate value that investments are carried on the balance sheet of the institution reduced by any unrealized gains on the investments that are reflected in such carrying value but excluded from the institution's Tier 1 capital and reduced by any associated deferred tax liabilities. For example, for investments held as available-for-sale (AFS), the adjusted carrying value of the investments would be the aggregate carrying value of the investments (as reflected on the consolidated balance sheet of the institution) less any unrealized gains on those investments that are included in other comprehensive income and that are not reflected in Tier 1 capital, and less any associated deferred tax liabilities. Unrealized losses on AFS nonfinancial equity investments must be deducted from Tier 1 capital pursuant to Paragraph (B)(10) of this Rule. The treatment of small business investment companies that are consolidated for accounting purposes under generally accepted accounting principles is discussed in Paragraph (C)(1)(h)(2) of this Rule. For investments in a nonfinancial company that is consolidated for accounting purposes, the institution's adjusted carrying value of the investment is determined under the equity method of accounting (net of any intangibles associated with the investment that are deducted from the institution's Tier 1 capital pursuant to Paragraph (C)(1)(e) of this Rule). Even though the assets of the nonfinancial company are consolidated for accounting purposes, these assets (as well as the credit equivalent amounts of the company's off-balance sheet items) are excluded from the institution's risk-weighted assets.
2. "Allowances for loan and lease losses" means those general valuation allowances that have been established through charges against earnings to absorb losses on loan and lease financing receivables. Allowances for loan and lease losses exclude allocated transfer risk reserves established, and specific reserves created against identified loss.

3. "Asset-backed commercial paper program" means a program that primarily issues externally rated commercial paper backed by assets or other exposures held in a bankruptcy-remote special purpose entity.
4. "Asset-backed commercial paper sponsor" means an institution that:
 - a. Establishes an asset-backed commercial paper program;
 - b. Approves the sellers permitted to participate in an asset-backed commercial paper program;
 - c. Approves the asset pools to be purchased by an asset-backed commercial paper program; or
 - d. Administers the asset-backed commercial paper program by monitoring the assets, arranging for debt placement, compiling monthly reports, or ensuring compliance with the program documents and with the program's credit and investment policy.
5. "Associated company" means any corporation, partnership, business trust, joint venture, association, or similar organization in which an institution directly or indirectly holds a 20 to 50 percent ownership interest.
6. "Banking and finance subsidiary" means any subsidiary of an institution that engages in banking- and finance-related activities.
7. "Cash items in the process of collection" means checks or drafts in the process of collection that are drawn on another depository institution, including a central bank, and that are payable immediately upon presentation in the country in which the reporting institution's office that is clearing or collecting the check or draft is located; United States Government checks that are drawn on the United States Treasury or any other United States Government or Government-sponsored agency and that are payable immediately upon presentation; broker's security drafts and commodity or bill-of-lading drafts payable immediately upon presentation in the United States or the country in which the reporting institution's office that is handling the drafts is located; and unposted debts.
8. "Central government" means the national governing authority of a country; it includes the departments, ministries and agencies of the central government and the central bank. The U.S. Central Bank includes the twelve Federal Reserve Banks. The definition of central government does not include the following: State, provincial or local governments; commercial enterprises owned by the central government that are entities engaged in activities involving trade, commerce or profit that are generally conducted or performed in the private sector of the United States economy; and noncentral government entities whose obligations are guaranteed by the central government.
9. "Commitment" means any arrangement that obligates an institution to:
 - a. Purchase loans or securities; or
 - b. Extend credit in the form of loans or leases, participations in loans or leases, overdraft facilities, revolving credit facilities, home equity lines of credit, liquidity facilities, or similar transactions.

10. “Common stockholders’ equity” means common stock, common stock surplus, undivided profits, capital reserves, and adjustments for the cumulative effect of foreign currency translation, less net unrealized holding losses on available-for-sale equity securities with readily determinable fair values.
11. “Conditional guarantee” means a contingent obligation of the United States Government or its agencies, or the central government of an Organization of Economic Cooperation and Development (OECD) country, the validity of which to the beneficiary is dependent upon some affirmative action; e.g., servicing requirements, on the part of the beneficiary of the guarantee or a third party.
12. “Deferred tax assets” means the tax consequences attributable to tax carryforwards and deductible temporary differences. Tax carryforwards are deductions or credits that cannot be used for tax purposes during the current period, but can be carried forward to reduce taxable income or taxes payable in a future period or periods. Temporary differences are financial events or transactions that are recognized in one period for financial statement purposes, but are recognized in another period or periods for income tax purposes. Deductible temporary differences are temporary differences that result in a reduction of taxable income in a future period or periods.
13. “Derivative contract” means generally a financial contract whose value is derived from the values of one or more underlying assets, reference rates or indexes of asset values. Derivative contracts include interest rate, foreign exchange rate, equity, precious metals and commodity contracts, or any other instrument that poses similar credit risks.
14. “Depository institution” means a financial institution that engages in the business of banking; that is recognized as a bank by the bank supervisory or monetary authorities of the country of its incorporation and the country of its principal banking operations; that receives deposits to a substantial extent in the regular course of business; and that has the power to accept demand deposits. In the United States, this definition encompasses all federally insured offices of commercial banks, mutual and stock savings banks, savings or building and loan associations (stock and mutual), cooperative banks, credit unions, and international banking facilities of domestic depository institutions. In addition, this definition encompasses all federally insured Colorado state chartered offices of industrial banks and trust companies. Bank holding companies are excluded from this definition. For the purposes of assigning risk weights, the differentiation between OECD depository institutions and non-OECD depository institutions is based on the country of incorporation. Claims on branches and agencies of foreign banks located in the United States are to be categorized on the basis of the parent bank’s country of incorporation.
15. “Equity investment” means any equity instrument including warrants and call options that give the holder the right to purchase an equity instrument, any equity feature of a debt instrument (such as a warrant or call option), and any debt instrument that is convertible into equity. An investment in any other instrument, including subordinated debt or other types of debt instruments, may be treated as an equity investment if the Banking Board determines that the instrument is the functional equivalent of equity or exposes the institution to essentially the same risks as an equity instrument.
16. “Exchange rate contracts” include: Cross-currency interest rate swaps; forward foreign exchange rate contracts; currency options purchased; and any similar instrument that, in the opinion of the Banking Board gives rise to similar risks.
17. “Goodwill” means an intangible asset that represents the excess of the purchase price over the fair market value of tangible and identifiable intangible assets acquired in purchases accounted for under the purchase method of accounting.

18. "Intangible assets" include mortgage and non-mortgage servicing assets [but exclude any interest only (IO) strips receivable related to these mortgage and nonmortgage servicing assets], purchased credit card relationships, goodwill, favorable leaseholds, and core deposit value.
19. "Interest rate contracts" include: Single currency interest rate swaps; basis swaps; forward rate agreements; interest rate options purchased; forward deposits accepted; and any similar instrument that, in the opinion of the Banking Board, gives rise to similar risks, including when-issued securities.
20. "Liquidity facility" means a legally binding commitment to provide liquidity to various types of transactions, structures, or programs. A liquidity facility that supports asset-backed commercial paper, in any amount, by lending to, or purchasing assets from any structure, program, or conduit constitutes an asset-backed commercial paper liquidity facility.
21. "Multifamily residential property" means any residential property consisting of five or more dwelling units including apartment buildings, condominiums, cooperatives, and other similar structures primarily for residential use, but not including hospitals, nursing homes, or other similar facilities.
22. "Nationally recognized statistical rating organization (NRSRO)" means an entity recognized by the Division of Market Regulation of the Securities and Exchange Commission (or any successor Division) (Commission or SEC) as a nationally recognized statistical rating organization for various purposes, including the Commission's uniform net capital requirements for brokers and dealers.
23. "Nonfinancial equity investment" means any equity investment held by an institution in a nonfinancial company through a small business investment company (SBIC) under section 302(b) of the Small Business Investment Act of 1958 or under the portfolio investment provisions of Regulation K. An equity investment made under section 302(b) of the Small Business Investment Act of 1958 in a SBIC that is not consolidated with the institution is treated as a nonfinancial equity investment in the manner provided in Paragraph (C)(1)(h)(2)(c) of this Rule. A nonfinancial company is an entity that engages in any activity that has not been determined to be permissible for an institution to conduct directly or to be financial in nature or incidental to financial activities under section 4(k) of the Bank Holding Company Act.
24. "OECD-based group of countries" comprises all full members of the OECD regardless of entry date, plus countries that have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the IMF's General Arrangements to Borrow but excludes any country that has rescheduled its external sovereign debt within the previous five years. These countries are hereinafter referred to as "OECD countries." A rescheduling of external sovereign debt generally would include any renegotiation of terms arising from a country's inability or unwillingness to meet its external debt service obligations, but generally would not include renegotiations of debt in the normal course of business, such as a renegotiation to allow the borrower to take advantage of a decline in interest rates or other changes in market conditions. (As of November 1995, the OECD included the following countries: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States; and Saudi Arabia had concluded special lending arrangements with the IMF associated with the IMF's General Arrangements to Borrow.)
25. "Original maturity" means, with respect to a commitment, the earliest possible date after a commitment is made on which the commitment is scheduled to expire (i.e., it will reach its stated maturity and cease to be binding on either party), provided that either:

- a. The commitment is not subject to extension or renewal and will actually expire on its stated expiration date; or
 - b. If the commitment is subject to extension or renewal beyond its stated expiration date, the stated expiration date will be deemed the original maturity only if the extension or renewal must be based upon terms and conditions independently negotiated in good faith with the customer at the time of the extension or renewal and upon a new, bona fide credit analysis utilizing current information on financial condition and trends.
26. "Preferred stock" includes the following instruments:
- a. "Convertible preferred stock," means preferred stock that is mandatorily convertible into either common or perpetual preferred stock;
 - b. "Intermediate-term preferred stock," means preferred stock with an original maturity of at least five years, but less than twenty (20) years;
 - c. "Long-term preferred stock," means preferred stock with an original maturity of twenty (20) years or more; and
 - d. "Perpetual preferred stock," means preferred stock without a fixed maturity date that cannot be redeemed at the option of the holder, and that has no other provisions that will require future redemption of the issue.
- For purposes of these instruments, preferred stock that can be redeemed at the option of the holder is deemed to have an "original maturity" of the earliest possible date on which it may be so redeemed.
27. "Public-sector entities" include states, local authorities and governmental subdivisions below the central government level in an OECD country. In the United States, this definition encompasses a state, county, city, town, or other municipal corporation, a public authority, and generally any publicly-owned entity that is an instrumentality of a state or municipal corporation. This definition does not include commercial companies owned by the public sector. (See "central government" definition for further explanation of commercial companies owned by the public sector.)
28. "Reciprocal holdings of bank capital instruments" means cross-holdings or other formal or informal arrangements in which two or more banking organizations swap, exchange, or otherwise agree to hold each other's capital instruments. This definition does not include holdings of capital instruments issued by other banking organizations that were taken in satisfaction of debts previously contracted, provided that the reporting institution has not held such instruments for more than five (5) years or a longer period approved by the Banking Board.
29. "Replacement cost" means, with respect to interest rate and exchange rate contracts, the loss that would be incurred in the event of a counterparty default, as measured by the net cost of replacing the contract at the current market value. If default would result in a theoretical profit, the replacement value is considered to be zero. The mark-to-market process should incorporate changes in both interest rates and counterparty credit quality.
30. "Residential properties" means houses, condominiums, cooperative units, and manufactured homes. This definition does not include boats or motor homes, even if used as a primary residence.

31. "Risk-weighted assets" means the sum of total risk-weighted balance sheet assets and the total of risk-weighted off-balance sheet credit equivalent amounts. Risk-weighted balance sheet and off-balance sheet assets are calculated pursuant to Paragraph (D) of this Rule.
 32. "Subsidiary" means any corporation, partnership, business trust, joint venture, association or similar organization in which an institution directly or indirectly holds more than a 50 percent ownership interest. This definition does not include ownership interests that were taken in satisfaction of debts previously contracted, provided that the reporting institution has not held the interest for more than five years or a longer period approved by the Banking Board.
 33. "Total capital" means the sum of an institution's core (Tier 1) and qualifying supplementary (Tier 2) capital elements.
 34. "Unconditionally cancelable" means, with respect to a commitment-type lending arrangement, that the institution may, at any time, with or without cause, refuse to advance funds or extend credit under the facility. In the case of home equity lines of credit, the institution is deemed able to unconditionally cancel the commitment if it can, at its option, prohibit additional extensions of credit, reduce the line, and terminate the commitment to the full extent permitted by relevant state and Federal law.
 35. "United States Government or its agencies" means an instrumentality of the United States Government whose debt obligations are fully and explicitly guaranteed as to the timely payment of principal and interest by the full faith and credit of the United States Government.
 36. "United States Government-sponsored agency" means an agency originally established or chartered to serve public purposes specified by the United States Congress, but whose obligations are not explicitly guaranteed by the full faith and credit of the United States Government.
 37. "Walkaway clause" means a provision in a bilateral netting contract that permits a nondefaulting counterparty to make a lower payment than it would make otherwise under the bilateral netting contract, or no payment at all, to a defaulter or the estate of a defaulter, even if the defaulter or the estate of the defaulter is a net creditor under the bilateral netting contract.
- C. Components of Capital. An institution's qualifying capital base consists of two types of capital--core (Tier 1) and supplementary (Tier 2).
1. Tier 1 Capital. The following elements comprise an institution's Tier 1 capital:
 - a. Common stockholders' equity;
 - b. Noncumulative perpetual preferred stock and related surplus (Preferred stock issues where the dividend is reset periodically based upon current market conditions and the institution's current credit rating, including but not limited to, auction rate, money market or remarketable preferred stock, are assigned to Tier 2 capital, regardless of whether the dividends are cumulative or noncumulative.); and
 - c. Minority interests in the equity accounts of consolidated subsidiaries, except that the following are not included in Tier 1 capital or total capital:

- (1) Minority interests in a small business investment company or investment fund that holds nonfinancial equity investments, and minority interests in a subsidiary that is engaged in nonfinancial activities and is held under one of the legal authorities listed in Paragraph (B)(23) of this Rule.
 - (2) Minority interests in consolidated asset-backed commercial paper programs sponsored by an institution if the consolidated assets are excluded from risk-weighted assets pursuant to Paragraph (D)(7)(e)(1) of this Rule.
- d. Less: Goodwill;
- e. Less: Other intangible assets, except mortgage servicing assets, purchased credit card relationships, and nonmortgage servicing assets subject to the following conditions. (Intangible assets are defined to exclude IO strips receivable related to these mortgage and non-mortgage servicing assets. See Paragraph (B)(18) of this Rule. Consequently, IO strips receivable related to mortgage and non-mortgage servicing assets are not required to be deducted under this Paragraph. However, credit-enhancing IO strips as defined in Paragraph (E)(1)(b) of this Rule are deducted from Tier 1 capital pursuant to Paragraph (C)(1)(g) of this Rule. Any noncredit-enhancing IO strips receivable are subject to a 100 percent risk weight under Paragraph (D)(7)(d) of this Rule.) For the purpose of determining Tier 1 capital, mortgage servicing assets, purchased credit card relationships, and nonmortgage servicing assets will be deducted from assets and from common stockholders' equity to the extent that these items do not meet the conditions, limitations, and restrictions described in this section. Institutions may elect to deduct disallowed servicing assets on a basis that is net of any associated deferred tax liability. Deferred tax liabilities netted in this manner cannot also be netted against deferred tax assets when determining the amount of deferred tax assets that are dependent upon future taxable income.
- (1) Valuation. The fair value of mortgage servicing assets, purchased credit card relationships, and nonmortgage servicing assets shall be estimated at least quarterly. The quarterly determination of the current fair value of the intangible asset must include adjustments for any significant changes in the original valuation assumptions, including changes in prepayment estimates. The Banking Board in its discretion may require independent fair value estimates on a case-by-case basis where it is deemed appropriate for safety and soundness purposes.
 - (2) Fair value limitation. For the purpose of calculating Tier 1 capital for minimum capital requirements (not for financial statement purposes), the balance sheet assets for mortgage servicing assets, purchased credit card relationships, and nonmortgage servicing assets will each be reduced to an amount equal to the lesser of:
 - (a) Ninety percent of the fair value of each intangible asset, determined pursuant to Paragraph (C)(1)(e)(1) of this Rule; or
 - (b) One hundred percent of the remaining unamortized book value.

- (3) Tier 1 capital limitation. The total of all intangible assets that are included in Tier 1 capital is limited to 100 percent of Tier 1 capital, of which no more than 25 percent of Tier 1 capital can consist of purchased credit card relationships and non-mortgage servicing assets in the aggregate. Calculation of these limitations must be based on Tier 1 capital net of goodwill and all other identifiable intangibles, other than purchased credit card relationships, mortgage servicing assets and nonmortgage servicing assets.
- f. Less: Certain deferred tax assets.
- (1) Tier 1 capital limitations. The maximum allowable amount of deferred tax assets that are dependent upon future taxable income will be limited to the lesser of:
- (a) The amount of deferred tax assets that the institution could reasonably expect to realize within one year of the quarter-end Call Report, based on its estimate of future taxable income for that year; or
- (b) Ten percent of Tier 1 capital, net of goodwill and all intangible assets other than purchased credit card relationships, mortgage servicing assets, and non-mortgage servicing assets.
- (2) Net unrealized holding gains and losses on available-for-sale securities. An institution may eliminate the deferred tax effects of any net unrealized holding gains and losses on available-for-sale debt securities before calculating the amount of deferred tax assets subject to the limit in Paragraph (C)(1)(f)(1) of this Rule. Institutions report these net unrealized holding gains and losses in their Call Reports as a separate component of equity capital, but exclude them from the definition of common stockholders' equity for regulatory capital purposes. An institution that adopts a policy to deduct these amounts must apply that approach consistently in all future calculations of the amount of disallowed deferred tax assets under Paragraph (C)(1)(f)(1) of this Rule.
- (3) Consolidated groups. The amount of deferred tax assets that an institution can realize from taxes paid in prior carryback years and from reversals of existing taxable temporary differences generally would not be deducted from capital. However, for an institution that is a member of a consolidated group (for tax purposes), the amount of carryback potential an institution may consider in calculating the limit on deferred tax assets under Paragraph (C)(1)(f)(1) of this Rule may not exceed the amount that the institution could reasonably expect to have refunded by its parent company.
- (4) Nontaxable purchase business combination. A deferred tax liability that is specifically associated with an intangible asset (other than purchased mortgage servicing rights and purchased credit card relationships) due to a nontaxable purchase business combination may be netted against that intangible asset in calculating the amount of net deferred tax assets under Paragraph (C)(1)(f)(1) of this Rule. Only the net amount of the intangible asset must be deducted from Tier 1 capital. Deferred tax liabilities netted in this manner cannot also be netted against deferred tax assets when determining the amount of net deferred tax assets that are dependent upon future taxable income.

- (5) Estimated future taxable income. Estimated future taxable income does not include net operating loss carryforwards to be used during that year or the amount of existing temporary differences expected to reverse within the year. An institution may use future taxable income projections for their closest fiscal year, provided it adjusts the projections for any significant changes that occur or that it expects to occur. Such projections must include the estimated effect of tax planning strategies that the institution expects to implement to realize net operating loss or tax credit carryforwards that will otherwise expire during the year.
- g. Less: Credit-enhancing IO strips (as defined in Paragraph (E)(1)(b) of this Rule). Credit-enhancing IO strips, whether purchased or retained, that exceed 25 percent of Tier 1 capital must be deducted from Tier 1 capital. Purchased and retained credit-enhancing IO strips, on a non-tax adjusted basis, are included in the total amount that is used for purposes of determining whether an institution exceeds its Tier 1 capital.
 - (1) The 25 percent limitation on credit-enhancing IO strips will be based on Tier 1 capital net of goodwill and all identifiable intangibles, other than purchased credit card relationships, mortgage servicing assets and non-mortgage servicing assets.
 - (2) Institutions must value each credit-enhancing IO strip included in Tier 1 capital at least quarterly. The quarterly determination of the current fair value of the credit-enhancing IO strip must include adjustments for any significant changes in original valuation assumptions, including changes in prepayment estimates.
 - (3) Institutions may elect to deduct disallowed credit-enhancing IO strips on a basis that is net of any associated deferred tax liability. Deferred tax liabilities netted in this manner cannot also be netted against deferred tax assets when determining the amount of deferred tax assets that are dependent upon future taxable income.
- h. Less: Nonfinancial equity investments as provided by this section.
 - (1) General.
 - (a) An institution must deduct from its Tier 1 capital the appropriate percentage, as determined pursuant to Table A, of the adjusted carrying value of all nonfinancial equity investments held by the institution and its subsidiaries.

TABLE A Deduction for Nonfinancial Equity Investments

Aggregate adjusted carrying value of all nonfinancial equity investments held directly or indirectly by institutions (as a percentage of the Tier 1 capital of the institution)¹	Deduction from Tier 1 capital (as a percentage of the adjusted carrying value of the investment)
Less than 15 percent	8.0 percent
Greater than or equal to 15 percent but less than 25 percent	12.0 percent
Greater than or equal to 25 percent	25.0 percent

¹ For purposes of calculating the adjusted carrying value of nonfinancial equity investments as a percentage of Tier 1 capital, Tier 1 capital is defined as the sum of the Tier 1 capital elements net of goodwill and net of all identifiable intangible assets other than mortgage servicing assets, nonmortgage servicing assets and purchased credit card relationships, but prior to the deduction for disallowed mortgage servicing assets, disallowed nonmortgage servicing assets, disallowed purchased credit card relationships, disallowed credit-enhancing IO strips (both purchased and retained), disallowed deferred tax assets, and nonfinancial equity investments.

- (b) Deductions for nonfinancial equity investments must be applied on a marginal basis to the portions of the adjusted carrying value of nonfinancial equity investments that fall within the specified ranges of the institution's Tier 1 capital. For example, if the adjusted carrying value of all nonfinancial equity investments held by an institution equals 20 percent of the Tier 1 capital of the institution, then the amount of the deduction would be 8 percent of the adjusted carrying value of all investments up to 15 percent of the institution's Tier 1 capital, and 12 percent of the adjusted carrying value of all investments equal to, or in excess of, 15 percent of the institution's Tier 1 capital.
- (c) The total adjusted carrying value of any nonfinancial equity investment that is subject to deduction under Paragraph (C)(1)(h) of this Rule is excluded from the institution's weighted risk assets for purposes of computing the denominator of the institution's risk-based capital ratio. For example, if 8 percent of the adjusted carrying value of a nonfinancial equity investment is deducted from Tier 1 capital, the entire adjusted carrying value of the investment will be excluded from risk-weighted assets in calculating the denominator of the risk-based capital ratio.
- (d) Institutions engaged in equity investment activities, including those institutions with a high concentration in nonfinancial equity investments (e.g., in excess of 50 percent of Tier 1 capital), will be monitored and may be subject to heightened supervision, as appropriate, by the Division of Banking to ensure that such institutions maintain capital levels that are appropriate in light of their equity investment activities, and the Banking Board may impose a higher capital charge in any case where the circumstances, such as the level of risk of the particular investment or portfolio of investments, the risk management systems of the institution, or other information, indicate that a higher minimum capital requirement is appropriate.

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- (2) Small business investment company investments (SBIC).
- (a) Notwithstanding Paragraph (C)(1)(h)(1)(a) of this Rule, no deduction is required for nonfinancial equity investments that are made by an institution or its subsidiary through a SBIC that is consolidated with the institution, or in a SBIC that is not consolidated with the institution, to the extent that such investments, in the aggregate, do not exceed 15 percent of the Tier 1 capital of the institution. Except as provided in Paragraph (C)(1)(h)(2)(b) of this Rule, any nonfinancial equity investment that is held through or in a SBIC and not deducted from Tier 1 capital will be assigned to the 100 percent risk-weight category and included in the institution's consolidated risk-weighted assets.
 - (b) If an institution has an investment in a SBIC that is consolidated for accounting purposes but the SBIC is not wholly owned by the institution, the adjusted carrying value of the institution's nonfinancial equity investments held through the SBIC is equal to the institution's proportionate share of the SBIC's adjusted carrying value of its equity investments in nonfinancial companies. The remainder of the SBIC's adjusted carrying value (i.e., the minority interest holders' proportionate share) is excluded from the risk-weighted assets of the institution.
 - (c) If an institution has an investment in a SBIC that is not consolidated for accounting purposes and has current information that identifies the percentage of the SBIC's assets that are equity investments in nonfinancial companies, the institution may reduce the adjusted carrying value of its investment in the SBIC proportionately to reflect the percentage of the adjusted carrying value of the SBIC's assets that are not equity investments in nonfinancial companies. The amount by which the adjusted carrying value of the institution's investment in the SBIC is reduced under this Paragraph will be risk weighted at 100 percent and included in the institution's risk-weighted assets.
 - (d) To the extent the adjusted carrying value of all nonfinancial equity investments that the institution holds through a consolidated SBIC or in a nonconsolidated SBIC equals or exceeds, in the aggregate, 15 percent of the Tier 1 capital of the institution, the appropriate percentage of such amounts, as set forth in Table A of this Rule, must be deducted from the institution's Tier 1 capital. In addition, the aggregate adjusted carrying value of all nonfinancial equity investments held through a consolidated SBIC and in a nonconsolidated SBIC (including any nonfinancial equity investments for which no deduction is required) must be included in determining, for the purposes of Table A of this Rule, the total amount of nonfinancial equity investments held by the institution in relation to its Tier 1 capital.

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- (3) Nonfinancial equity investments excluded.
- (a) Notwithstanding Paragraphs (C)(1)(h)(1) and (2) of this Rule, no deduction from Tier 1 capital is required for the following:
- (i) Nonfinancial equity investments (or portion of such investments) made by the institution prior to March 13, 2000, and continuously held by the institution since March 13, 2000.
 - (ii) Nonfinancial equity investments made on or after March 13, 2000, pursuant to a legally binding written commitment that was entered into by the institution prior to March 13, 2000, and that required the institution to make the investment, if the institution has continuously held the investment since the date the investment was acquired.
 - (iii) Nonfinancial equity investments received by the institution through a stock split or stock dividend on a nonfinancial equity investment made prior to March 13, 2000, provided that the institution provides no consideration for the shares or interests received, and the transaction does not materially increase the institution's proportional interest in the nonfinancial company.
 - (iv) Nonfinancial equity investments received by the institution through the exercise on or after March 13, 2000, of an option, warrant, or other agreement that provides the institution with the right, but not the obligation, to acquire equity or make an investment in a nonfinancial company, if the option, warrant, or other agreement was acquired by the institution prior to March 13, 2000, and the institution provides no consideration for the nonfinancial equity investments.
- (b) Any excluded nonfinancial equity investments described in Paragraph (C)(1)(h)(3)(a) of this Rule must be included in determining the total amount of nonfinancial equity investments held by the institution in relation to its Tier 1 capital for the purposes of Table A of this Rule. In addition, any excluded nonfinancial equity investments will be risk weighted at 100 percent and included in the institution's risk-weighted assets.

2. Tier 2 Capital. Tier 2 capital is limited to 100 percent of Tier 1 capital. The following elements comprise an institution's Tier 2 capital:
 - a. Allowance for loan and lease losses, up to a maximum of 1.25 percent of risk-weighted assets. (The amount of the allowance for loan and lease losses that may be included in capital is based on a percentage of risk-weighted assets. The gross sum of risk-weighted assets used in this calculation includes all risk-weighted assets, with the exception of the assets required to be deducted from capital under Paragraph (D) of this Rule in establishing risk-weighted assets (i.e., the assets required to be deducted from capital under Paragraph (C) of this Rule. An institution may deduct reserves for loan and lease losses in excess of the amount permitted to be included as capital, as well as allocated transfer risk reserves and reserves held against other real estate owned, from the gross sum of risk-weighted assets in computing the denominator of the risk-based capital ratio.)
 - b. Cumulative perpetual preferred stock, long-term preferred stock, convertible preferred stock, and any related surplus, without limit, if the issuing institution has the option to defer payment of dividends on these instruments. For long-term preferred stock, the amount that is eligible to be included as Tier 2 capital is reduced by 20 percent of the original amount of the instrument (net of redemptions) at the beginning of each of the last five years of the life of the instrument.
 - c. Hybrid capital instruments, without limit. Hybrid capital instruments are those instruments that combine certain characteristics of debt and equity, such as perpetual debt. To be included as Tier 2 capital, these instruments must meet the following criteria:
 - (1) The instrument must be unsecured, subordinated to the claims of depositors and general creditors, and fully paid up;
 - (2) The instrument must not be redeemable at the option of the holder prior to maturity, except with the prior approval of the Banking Board;
 - (3) The instrument must be available to participate in losses while the issuer is operating as a going concern (in this regard, the instrument must automatically convert to common stock or perpetual preferred stock, if the sum of the retained earnings and capital surplus accounts of the issuer shows a negative balance); and
 - (4) The instrument must provide the option for the issuer to defer principal and interest payments, if
 - (a) The issuer does not report a net profit for the most recent combined four quarters; and

- (b) The issuer eliminates cash dividends on its common and preferred stock.

(Mandatory convertible debt instruments that meet the requirements of Paragraphs (C)(2)(d)(1) through (7) and that unqualifiedly require the issuer to exchange either common or perpetual preferred stock for such instruments by a date at or before the maturity of the instrument (the maturity of these instruments must be 12 years or less), or that have been previously approved as capital by the Banking Board, are treated as qualifying hybrid capital instruments.)

- d. Term subordinated debt instruments and intermediate-term preferred stock and related surplus are included in Tier 2 capital, but only to a maximum of 50 percent of Tier 1 capital as calculated after deductions pursuant to Paragraphs (C)(1)(d) through (h) and Paragraph (C)(3) of this Rule. To be considered capital, term subordinated debt instruments must meet the following requirements:

- (1) Have original weighted average maturities of at least five years;
- (2) Be subordinated to the claims of depositors;
- (3) State on the instrument that it is not a deposit and is not insured by the Federal Deposit Insurance Corporation (FDIC);
- (4) Be approved as capital by the Banking Board;
- (5) Be unsecured;
- (6) Be ineligible as collateral for a loan by the issuing institution;
- (7) Provide that once any scheduled payments of principal begin, all scheduled payments shall be made at least annually and the amount repaid in each year shall be no less than in the prior year; and
- (8) Provide that no prepayment (including payment pursuant to an acceleration clause or redemption prior to maturity) shall be made without the prior written approval of the Banking Board.

Also, at the beginning of each of the last five years for the life of either type of instrument, the amount that is eligible to be included as Tier 2 capital is reduced by 20 percent of the original amount of that instrument (net of redemptions). (Capital instruments may be redeemed prior to maturity with the prior approval of the Banking Board. The Banking Board typically will consider requests for the redemption of capital instruments when the instruments are to be redeemed with the proceeds of, or replaced by, a like amount of a similar or higher quality capital instrument. However, the Banking Board reserves the authority to deny redemption in such circumstances or to allow redemption in other circumstances, based upon its evaluation of the circumstances of each case. The Banking Board must be notified in writing of any request for redemption at least thirty (30) days in advance of such redemption.)

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- e. Up to 45 percent of pretax net unrealized holding gains (that is, the excess, if any, of the fair value over historical cost) on available-for-sale equity securities with readily determinable fair values. However, the Banking Board may exclude all or a portion of these unrealized gains from Tier 2 capital if the Banking Board determines that the equity securities are not prudently valued. Unrealized gains (losses) on other types of assets, such as institution premises and available-for-sale debt securities, are not included in Tier 2 capital, but the Banking Board may take these unrealized gains (losses) into account as additional factors when assessing an institution's overall capital adequacy.
3. Deductions From Total Capital (the sum of Tier 1 capital plus Tier 2 capital). The following items are deducted from total capital:
 - a. Investments, both equity and debt, in unconsolidated banking and finance subsidiaries that are deemed to be capital of the subsidiary. The Banking Board may require deduction of investments in other subsidiaries and associated companies on a case-by-case basis.
 - b. Reciprocal holdings of capital instruments issued by banks.
- D. Risk Categories/Weights for On-Balance Sheet Assets and Off-Balance Sheet Items
1. The denominator of the risk-based capital ratio, i.e., an institution's risk-weighted assets, is derived by assigning that institution's assets and off-balance sheet items to one of the four risk categories detailed in Paragraph (D)(7) of this Rule. Each category has a specific risk weight.
 2. Before an off-balance sheet item is assigned a risk weight, it is converted to an on-balance sheet credit equivalent amount pursuant to Paragraph (D)(8) of this Rule.
 3. The risk weight assigned to a particular asset or on-balance sheet credit equivalent amount determines the percentages of that asset/credit equivalent that is included in the denominator of the institution's risk-based capital ratio. Any asset deducted from an institution's capital in computing the numerator of the risk-based capital ratio is not included as part of the institution's risk-weighted assets.
 4. The Banking Board reserves the right to require an institution to compute its risk-based capital ratio on the basis of average, rather than period-end, risk-weighted assets when necessary to carry out the purposes of these guidelines.

5. Some of the assets on an institution's balance sheet may represent an indirect holding of a pool of assets, e.g., mutual funds, that encompasses more than one risk weight within the pool. In those situations, the institution may assign the asset to the risk category applicable to the highest risk-weighted asset that pool is permitted to hold pursuant to its stated investment objectives in the fund's prospectus. Alternatively, the institution may assign the asset on a pro rata basis to different risk categories according to the investment limits in the fund's prospectus. In either case, the minimum risk weight that may be assigned to such a pool is 20 percent. If an institution assigns the asset on a pro rata basis, and the sum of the investment limits in the fund's prospectus exceeds 100 percent, the institution must assign the highest pro rata amounts of its total investment to the higher risk category. If, in order to maintain a necessary degree of liquidity, the fund is permitted to hold an insignificant amount of its assets in short-term, highly-liquid securities of superior credit quality (that do not qualify for a preferential risk weight), such securities generally will not be taken into account in determining the risk category into which the institution's holding in the overall pool should be assigned. The prudent use of hedging instruments by a fund to reduce the risk of its assets will not increase the risk-weighting of the investment in that fund above the 20 percent category. However, if a fund engages in any activities that are deemed to be speculative in nature or has any other characteristics that are inconsistent with the preferential risk weighting assigned to the fund's assets, the institution's investment in the fund will be assigned to the 100 percent risk category. More detail on the treatment of mortgage-backed securities is provided in Paragraph (D)(7)(c)(6) of this Rule.
6. In addition, when certain institutions that are engaged in trading activities calculate the risk-based capital ratio under this Rule, the institution must also refer to Appendix B, which incorporates capital charges for certain market risk into the risk-based capital ratio. When calculating the risk-based capital ratio, such institutions are required to refer to Appendix B for supplemental rules to determine qualifying and excess capital, calculate risk-weighted assets, calculate market risk equivalent assets and add them to risk-weighted assets, and calculate risk-based capital ratios as adjusted for market risk. (Trading activity means the gross sum of trading assets and liabilities as reported in the institution's most recent Call Report.
7. On-Balance Sheet Assets. The following are the risk categories/weights for on-balance sheet assets:
 - a. Zero percent risk weight.
 - (1) Cash, including domestic and foreign currency owned and held in all offices of an institution or in transit. Any foreign currency held by an institution should be converted into U.S. dollar equivalents.
 - (2) Deposit reserves and other balances at Federal Reserve banks.
 - (3) Securities issued by, and other direct claims on, the United States Government or its agencies, or the central governments of an OECD country.
 - (4) That portion of assets directly and unconditionally guaranteed by the United States Government or its agencies, or the central government of an OECD country. (For the treatment of privately-issued mortgage-backed securities where the underlying pool is comprised solely of mortgage-related securities issued by GNMA (see Paragraph (D)(7)(b)(7) of this Rule)).

- (5) That portion of local currency claims on, or unconditionally guaranteed by central governments of non-OECD countries, to the extent the institution has local currency liabilities in that country. Any amount of such claims that exceeds the amount of the institution's local currency liabilities is assigned to the 100 percent risk category of Paragraph (D)(7)(d) of this Rule.
- (6) Gold bullion held in the institution's own vaults or in another institution's vaults on an allocated basis, to the extent it is backed by gold bullion liabilities.
- (7) The book value of paid-in Federal Reserve Bank stock.
- (8) That portion of assets and off-balance sheet transactions collateralized by cash or securities issued or directly and unconditionally guaranteed by the United States Government or its agencies, or the central government of an OECD country provided that:
 - (a) The institution maintains control over the collateral:
 - (i) If the collateral consists of cash, the cash must be held on deposit by the institution or by a third party for the account of the institution;
 - (ii) If the collateral consists of OECD government securities, then the OECD government securities must be held by the institution or by a third party acting on behalf of the institution;
 - (b) The institution maintains a daily positive margin of collateral fully taking into account any change in the market value of the collateral held as security;
 - (c) Where the institution is acting as a customer's agent in a transaction involving the loan or sale of securities that is collateralized by cash or OECD government securities delivered to the institution, any obligation by the institution to indemnify the customer is limited to no more than the difference between the market value of the securities lent and the market value of the collateral received, and any reinvestment risk associated with the collateral is borne by the customer; and
 - (d) The transaction involves no more than minimal risk.

NOTE: Assets and off-balance sheet transactions collateralized by securities issued or guaranteed by the United States Government or its agencies, or the central government of an OECD country include, but are not limited to, securities lending transactions, repurchase agreements, collateralized letters of credit, such as reinsurance letters of credit, and other similar financial guarantees. Swaps, forwards, futures, and options transactions are also eligible, if they meet the collateral requirements. However, the Banking Board may, at its discretion, require that certain collateralized transactions be risk weighted at 20 percent if they involve more than a minimal risk.

- b. Twenty percent risk weight.
- (1) All claims on depository institutions incorporated in an OECD country, and all assets backed by the full faith and credit of depository institutions incorporated in an OECD country. This includes the credit equivalent amount of participations in commitments and standby letters of credit sold to other depository institutions incorporated in an OECD country, but only if the originating institution remains liable to the customer or beneficiary for the full amount of the commitment or standby letter of credit. Also included in this category are the credit equivalent amounts of risk participations in bankers' acceptances conveyed to other depository institutions incorporated in an OECD country. However, institution-issued securities that qualify as capital of the issuing institution are not included in this risk category, but are assigned to the 100 percent risk category of Paragraph (D)(7)(d) of this Rule.
 - (2) Claims on or guaranteed by depository institutions, other than the central bank, incorporated in a non-OECD country, with a residual maturity of one year or less.
 - (3) Cash items in the process of collection.
 - (4) That portion of assets collateralized by cash or securities issued or directly and unconditionally guaranteed by the United States Government or its agencies, or the central government of an OECD country, that does not qualify for the zero percent risk-weight category.
 - (5) That portion of assets conditionally guaranteed by the United States Government or its agencies, or the central government of an OECD country.
 - (6) Securities issued by, or other claims on, United States Government-sponsored agencies.
 - (7) That portion of assets guaranteed by United States Government-sponsored agencies. Privately issued mortgage-backed securities, e.g., CMOs and REMICs, where the underlying pool is comprised solely of mortgage-related securities issued by GNMA, FNMA, and FHLMC, will be treated as an indirect holding of the underlying assets and assigned to the 20 percent risk category of this Paragraph (D)(7)(b). If the underlying pool is comprised of assets that attract different risk weights, e.g., FNMA securities and conventional mortgages, the institution should generally assign the security to the highest risk category appropriate for any asset in the pool. However, on a case-by-case basis, the Banking Board may allow the institution to assign the security proportionately to the various risk categories based on the proportion in which the risk categories are represented by the composition cash flows of the underlying pool of assets. Before the Banking Board will consider a request to proportionately risk-weight such a security, the institution must have current information for the reporting date that details the composition and cash flows of the underlying pool of assets. Furthermore, before a mortgage-related security will receive a risk weight lower than 100 percent, it must meet the criteria set forth in Paragraph (D)(7)(c)(6) of this Rule.

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- (8) That portion of assets collateralized by the current market value of securities issued or guaranteed by United States Government-sponsored agencies.
 - (9) Claims representing general obligations of any public-sector entity in an OECD country, and that portion of any claims guaranteed by any such public-sector entity.
 - (10) Claims on, or guaranteed by, official multilateral lending institutions or regional development institutions in which the United States Government is a shareholder or contributing member. These institutions include, but are not limited to, the International Bank for Reconstruction and Development (World Bank), the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the European Investments Bank, the International Monetary Fund and the Bank for International Settlements.
 - (11) That portion of assets collateralized by the current market value of securities issued by official multilateral lending institutions or regional development institutions in which the United States Government is a shareholder or contributing member.
 - (12) That portion of local currency claims conditionally guaranteed by central governments of non-OECD countries, to the extent the institution has local currency liabilities in that country. Any amount of such claims that exceeds the amount of the institution's local currency liabilities is assigned to the 100 percent risk category of Paragraph (D)(7)(d) of this Rule.
 - (13) Claims on, or guaranteed by, a securities firm incorporated in an OECD country, that satisfies the following conditions:
 - (a) If the securities firm is incorporated in the United States, then the firm must be a broker-dealer that is registered with the SEC and must be in compliance with the SEC's net capital regulation.
 - (b) If the securities firm is incorporated in any other OECD country, then the institution must be able to demonstrate that the firm is subject to consolidated supervision and regulation, including its subsidiaries, comparable to that imposed on depository institutions in OECD countries; such regulation must include risk-based capital standards comparable to those applied to depository institutions under the Basel Capital Accord.
 - (c) The securities firm, whether incorporated in the United States or another OECD country, must also have a long-term credit rating pursuant to Paragraph (D)(7)(b)(13)(c)(i) of this Rule; a parent company guarantee pursuant to Paragraph (D)(7)(b)(13)(c)(ii) of this Rule; or a collateralized claim pursuant to Paragraph (D)(7)(b)(13)(c)(iii) of this Rule. Claims representing capital of a securities firm must be risk-weighted at 100 percent pursuant to Paragraph (D)(7)(d) of this Rule.

- (i) Credit Rating. The securities firm must have either a long-term issuer credit rating or a credit rating on at least one issue of long-term unsecured debt, from a NRSRO that is in one of the three highest investment-grade categories used by the NRSRO. If the securities firm has a credit rating from more than one NRSRO, the lowest credit rating must be used to determine the credit rating under this Paragraph.
- (ii) Parent company guarantee. The claim on, or guarantee by, the securities firm must be guaranteed by the firm's parent company, and the parent company must have either a long-term issuer credit rating or a credit rating on at least one issue of long-term unsecured debt, from a NRSRO that is in one of the three highest investment-grade categories used by the NRSRO.
- (iii) Collateralized claim. The claim on the securities firm must be collateralized subject to all of the following requirements:
 - a) The claim must arise from a reverse repurchase/repurchase agreement or securities lending/borrowing contract executed using standard industry documentation.
 - b) The collateral must consist of debt or equity securities that are liquid and readily marketable.
 - c) The claim and collateral must be marked-to-market daily.
 - d) The claim must be subject to daily margin maintenance requirements under standard industry documentation.
 - e) The contract from which the claim arises can be liquidated, terminated, or accelerated immediately in bankruptcy or similar proceedings, and the security or collateral agreement will not be stayed or avoided under the applicable law of the relevant jurisdiction. To be exempt from the automatic stay in bankruptcy in the United States, the claim must arise from a securities contract or a repurchase agreement under section 555 or 559, respectively, of the Bankruptcy Code, a qualified financial contract under section 11(e)(8) of the Federal Deposit Insurance Act, or a netting contract between or among financial institutions under section 401-407 of the Federal Deposit Insurance Corporation Improvement Act of 1991, or the Regulation EE.

- c. Fifty percent risk weight.
- (1) Revenue obligations of any public-sector entity in an OECD country for which the underlying obligor is the public-sector entity, but which are repayable solely from the revenues generated by the project financed through the issuance of the obligations.
 - (2) The credit equivalent amount of derivative contracts, calculated pursuant to Paragraph (D)(8)(g) of this Rule, that do not qualify for inclusion in a lower risk category.
 - (3) Loans secured by first mortgages on one-to-four family residential properties, either owner-occupied or rented, provided that such loans are not otherwise ninety (90) days or more past due, or on nonaccrual or restructured. If an institution holds the first and junior lien on a one-to-four family residential property and no other party holds an intervening lien, the transaction is treated as a single loan secured by a first lien for purposes of both determining the loan-to-value ratio and assigning a risk weight to the transaction. It is presumed that such loans will meet prudent underwriting standards. Furthermore, residential property loans made for the purpose of construction financing are assigned to the 100 percent risk category of Paragraph (D)(7)(d) of this Rule; however, these loans may be included in the 50 percent category of this Paragraph (D) if they are subject to a legally binding sales contract and satisfy the requirements of Paragraph (D)(7)(c)(4) of this Rule.
 - (4) Loans to residential real estate builders for one-to-four family residential property construction, if the institution obtains sufficient documentation demonstrating that the buyer of the home intends to purchase the home (i.e., a legally binding written sales contract) and has the ability to obtain a mortgage loan sufficient to purchase the home (i.e., a firm written commitment for permanent financing of the home upon completion), subject to the following additional criteria:
 - (a) The builder must incur at least the first 10 percent of the direct costs (i.e., actual costs of the land, labor, and material) before any drawdown is made under the construction loan, and the construction loan may not exceed 80 percent of the sales price of the presold home;
 - (b) The individual purchaser has made a substantial "earnest money deposit" of no less than 3 percent of the sales price of the home that must be subject to forfeiture by the individual purchaser if the sales contract is terminated by the individual purchaser; however, the earnest money deposit shall not be subject to forfeiture by reason of breach or termination of the sales contract on the part of the builder;
 - (c) The earnest money deposit must be held in escrow by the institution financing the builder or by an independent party in a fiduciary capacity; the escrow agreement must provide that in the event of default the escrow funds must be used to defray any cost incurred relating to any cancellation of the sales contract by the buyer;

- (d) If the individual purchaser terminates the contract, or if the loan fails to satisfy any other criterion under this section, then the institution must immediately recategorize the loan at a 100 percent risk weight and must accurately report the loan in the institution's next quarterly Call Report;
 - (e) The individual purchaser must intend that the home will be owner-occupied;
 - (f) The loan is made by the institution pursuant to prudent underwriting standards;
 - (g) The loan is not more than ninety (90) days past due, or on nonaccrual; and
 - (h) The purchaser is an individual(s) and not a partnership, joint venture, trust, corporation, or any other entity (including an entity acting as a sole proprietorship) that is purchasing one or more of the homes for speculative purposes.
- (5) Loans secured by a first mortgage on multifamily residential properties. The portion of multifamily residential property loans that is sold subject to a pro rata loss sharing arrangement may be treated by the selling institution as sold to the extent that the sales agreement provides for the purchaser of the loan to share in any loss incurred on the loan on a pro rata basis with the selling institution. The portion of multifamily residential property loans sold subject to any loss sharing arrangement, other than pro rata sharing of the loss, shall be accorded the same treatment as any other asset sold under an agreement to repurchase or sold with recourse under Paragraph (E)(2) of this Rule. For a multifamily residential property to be included in the 50 percent risk weight category it must comply with the following:
- (a) The amortization of principal and interest occurs in not more than thirty (30) years;
 - (b) The minimum original maturity for repayment of principal is not less than seven (7) years;
 - (c) All principal and interest payments have been made on a timely basis pursuant to the terms of the loan for at least one year immediately preceding the risk-weighting of the loan in the 50 percent risk weight category, and the loan is not otherwise ninety (90) days or more past due, or on nonaccrual status;
 - (d) The loan is made pursuant to all applicable requirements and prudent underwriting standards;

- (e) If the rate of interest does not change over the term of the loan:
 - (i) The current loan amount outstanding does not exceed 80 percent of the current value of the property, as measured by either the value of the property at origination of the loan (which is the lower of the purchase price or the value as determined by the initial appraisal, or if appropriate, the initial evaluation) or the most current appraisal, or if appropriate, the most current evaluation; and
 - (ii) In the most recent fiscal year, the ratio of annual net operating income generated by the property (before payment of any debt service on the loan) to annual debt service of the loan is not less than 120 percent;
- (f) If the rate of interest changes over the term of the loan:
 - (i) The current loan amount outstanding does not exceed 75 percent of the current value of the property, as measured by either the value of the property at origination of the loan (which is the lower of the purchase price or the value as determined by the initial appraisal, or if appropriate, the initial evaluation) or the most current appraisal, or if appropriate, the most current evaluation; and
 - (ii) In the most recent fiscal year, the ratio of annual net operating income generated by the property (before payment of any debt service on the loan) to annual debt service on the loan is not less than 115 percent; and
- (g) If the loan was refinanced by the borrower:
 - (i) All principal and interest payments on the loan being refinanced that were made in the preceding year prior to refinancing shall apply in determining the one-year timely payment requirement under Paragraph (D)(7)(c)(5)(c) of this Rule; and
 - (ii) The net operating income generated by the property in the preceding year prior to refinancing shall apply in determining the applicable debt service requirements under Paragraphs (D)(7)(c)(5)(e) and (f) of this Rule.

NOTE: For the purposes of the debt service requirements in Paragraphs (D)(7)(c)(5)(e)(ii) and (f)(ii) of this Rule, other forms of debt service coverage that generate sufficient cash flows to provide comparable protection to the institution may be considered for: (a) a loan secured by cooperative housing; or (b) a multifamily residential property loan if the purpose of the loan is for the development or purchase of multifamily residential property primarily intended to provide low- to moderate-income housing, including special operating reserve accounts or special operating subsidies provided by federal, state, local or private sources. However, the Banking Board reserves the right, on a case-by-case basis, to review the adequacy of any other forms of comparable debt service coverage relied on by the institution.

- (6) Privately-issued mortgage-backed securities, i.e., those that do not carry the guarantee of a government or government-sponsored agency, if the privately-issued mortgage-backed securities are, at the time the mortgage-backed securities are originated, fully secured by, or otherwise represent, a sufficiently secure interest in mortgages that qualify for the 50 percent risk weight under Paragraph (D)(7)(c)(3) through (5) of this Rule, provided they meet the following criteria:
- (a) The underlying assets must be held by an independent trustee that has a first priority, perfected security interest in the underlying assets for the benefit of the holders of the security;
 - (b) The holder of the security must have an undivided pro rata ownership interest in the underlying assets or the trust that issues the security must have no liabilities unrelated to the issued securities;
 - (c) The trust that issues the security must be structured such that the cash flows from the underlying assets fully meet the cash flow requirements of the security without undue reliance on any reinvestment income; and
 - (d) There must not be any material reinvestment risk associated with any funds awaiting distribution to the holder of the security.

NOTE: If all of the underlying mortgages in the pool do not qualify for the 50 percent risk weight, the institution should generally assign the entire value of the security to the 100 percent risk category of Paragraph (D)(7)(d) of this Rule; however, on a case-by-case basis, the Banking Board may allow the institution to assign only the portion of the security which represents an interest in, and the cash flows of, nonqualifying mortgages to the 100 percent risk category, with the remainder being assigned a risk weight of 50 percent. Before the Banking Board will consider a request to risk weight a mortgage-backed security on a proportionate basis, the institution must have current information for the reporting date that details the composition and cash flows of the underlying pool of mortgages.

- d. One hundred percent risk weight. All other assets not specified above, including, but not limited to:
- (1) Claims on or guaranteed by depository institutions incorporated in a non-OECD country, as well as claims on the central bank of a non-OECD country, with a residual maturity exceeding one year;
 - (2) All non-local currency claims on non-OECD central governments, as well as local currency claims on non-OECD central governments that are not included in Paragraph (D)(7)(a)(5) of this Rule;
 - (3) Asset- or mortgage-backed securities that are externally rated are risk-weighted pursuant to Paragraph (E)(4) of this Rule;
 - (4) All stripped mortgage-backed securities, including IO portions, principal only portions (POs), and other similar instruments, regardless of the issuer or guarantor;
 - (5) Obligations issued by any state or any political subdivision thereof for the benefit of a private party or enterprise where that party or enterprise, rather than the issuing state or political subdivision, is responsible for the timely payment of principal and interest on the obligation, e.g., industrial development bonds;
 - (6) Claims on commercial enterprises owned by non-OECD and OECD central governments;
 - (7) Any investment in an unconsolidated subsidiary that is not required to be deducted from total capital;
 - (8) Instruments issued by depository institutions incorporated in OECD and non-OECD countries that qualify as capital of the issuer;
 - (9) Investments in fixed assets, premises, and other real estate owned;
 - (10) Claims representing capital of a securities firm notwithstanding Paragraph (D)(7)(b)(13) of this Rule.

NOTE: An institution subject to the market risk capital requirements pursuant to Appendix B of this Rule may calculate the capital requirement for qualifying securities borrowing transactions pursuant to Paragraph (C)(1)(a)(2) of Appendix B of this Rule.

- e. Asset-backed commercial paper programs subject to consolidation.
- (1) An institution that qualifies as a primary beneficiary and must consolidate an asset-backed commercial paper program as a variable interest entity under generally accepted accounting principles may exclude the consolidated asset-backed commercial paper program assets from risk-weighted assets if the institution is the sponsor of the consolidated asset-backed commercial paper program.

- (2) If an institution excludes such consolidated asset-backed commercial paper program assets from risk-weighted assets, the institution must assess the appropriate risk-based capital charge against any risk exposures of the institution arising in connection with such asset-backed commercial paper program, including direct credit substitutes, recourse obligations, residual interests, asset-backed commercial paper liquidity facilities, and loans pursuant to Paragraphs (D) and (E) of this Rule.
 - (3) If an institution is either not permitted to exclude consolidated asset-backed commercial paper program assets or elects not to exclude consolidated asset-backed commercial paper program assets from its risk-weighted assets, the institution must assess a risk-based capital charge based on the appropriate risk weight of the consolidated asset-backed commercial paper program assets pursuant to Paragraphs (D)(7) and (E) of this Rule. Any direct credit substitutes and recourse obligations (including residual interests and asset-backed commercial paper liquidity facilities), and loans that sponsoring institutions provide to such asset-backed commercial paper programs are not subject to a capital charge under Paragraph (E) of this Rule.
 - (4) If an institution has multiple overlapping exposures (such as a program-wide credit enhancement and an asset-backed commercial paper liquidity facility) to an asset-backed commercial paper program that is not consolidated for risk-based capital purposes, the institution must apply the highest capital charge applicable to the exposures but is not required to hold capital multiple times for the overlapping exposures under Paragraph (E) of this Rule.
 - f. Other variable interest entities subject to consolidation. If an institution is required to consolidate the assets of a variable interest entity other than an asset-backed commercial paper program under generally accepted accounting principles, the institution must assess a risk-based capital charge based on the appropriate risk weight of the consolidated assets pursuant to Paragraphs (D)(7) and (E) of this Rule. Any direct credit substitutes and recourse obligations (including residual interests), and loans that an institution may provide to such a variable interest entity are not subject to any capital charge under Paragraph (E) of this Rule.
8. Off-Balance Sheet Activities. The risk weight assigned to an off-balance sheet item is determined by a two-step process. First, the face amount of the off-balance sheet item is multiplied by the appropriate credit conversion factor specified in this Paragraph (D)(8). This calculation translates the face amount of an off-balance sheet item into an on-balance sheet credit equivalent amount. Second, the resulting credit equivalent amount is then assigned to the proper risk category using the criteria regarding obligors, guarantors and collateral listed in Paragraph (D)(7) of this Rule, or external credit rating pursuant to Paragraph (E)(4) of this Rule, if applicable. Collateral and guarantees are applied to the face amount of an off-balance sheet item; however, with respect to derivative contracts under Paragraph (D)(8)(g) of this Rule, collateral and guarantees are applied to the credit equivalent amounts of such derivative contracts. The following are the credit conversion factors and the off-balance sheet items to which they apply. However, direct credit substitutes, recourse obligations, and securities issued in connection with asset securitizations are treated as described in Paragraph (E) of this Rule.
 - a. One hundred percent credit conversion factor.
 - (1) Risk participations purchased in bankers' acceptances.

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- (2) Contingent obligations with a certain draw down, e.g., legally binding agreements to purchase assets at a specified future date.
 - (3) Indemnification of customers whose securities the institution has lent as agent. If the customer is not indemnified against loss by the institution, the transaction is excluded from the risk-based capital calculation. When an institution lends its own securities, the transaction is treated as a loan. When an institution lends its own securities or, acting as agent, agrees to indemnify a customer, the transaction is assigned to the risk weight appropriate to the obligor or collateral that is delivered to the lending or indemnifying institution or to an independent custodian acting on their behalf.
- b. Fifty percent credit conversion factor.
- (1) Transaction-related contingencies including, among other things, performance bonds and performance-based standby letters of credit related to a particular transaction. A “performance-based standby letter of credit” is any letter of credit, or similar arrangement, however named or described, that represents an irrevocable obligation to the beneficiary on the part of the issuer to make payment on account of any default by the account party in the performance of a non-financial or commercial obligation. Participations in performance-based standby letters of credit are treated pursuant to Paragraph (E) of this Rule. To the extent permitted by law or regulation, performance-based standby letters of credit include such things as arrangements backing subcontractors’ and suppliers’ performance, labor and materials contracts, and construction bids.
 - (2) Unused portion of commitments with an original maturity exceeding one year; however, commitments that are asset-backed commercial paper liquidity facilities must satisfy the eligibility requirements under Paragraph (D)(8)(f)(2) of this Rule. Participations in commitments are treated pursuant to Paragraph (E) of this Rule.
 - (3) Revolving underwriting facilities, note issuance facilities, and similar arrangements pursuant to which the institution’s customer can issue short-term debt obligations in its own name, but for which the institution has a legally binding commitment to either:
 - (a) Purchase the obligations the customer is unable to sell by a stated date; or
 - (b) Advance funds to its customer, if the obligations cannot be sold.
- c. Twenty percent credit conversion factor.
- (1) Trade-related contingencies. These are short-term, self-liquidating instruments used to finance the movement of goods and are collateralized by the underlying shipment. A commercial letter of credit is an example of such an instrument.
- d. Ten percent credit conversion factor.

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- (1) Unused portion of asset-backed commercial paper liquidity facilities with an original maturity of one year or less that satisfy the eligibility requirements under Paragraph (D)(8)(f)(2) of this Rule.
- e. Zero percent credit conversion factor.
- (1) Unused portion of commitments with an original maturity of one year or less, but excluding any asset-backed commercial paper liquidity facilities.
 - (2) Unused portion of commitments with an original maturity of greater than one year, if they are unconditionally cancelable (see Paragraph (B)(34) of this Rule) at any time at the option of the institution and the institution has the contractual right to make, and in fact does make, either:
 - (a) A separate credit decision based upon the borrower's current financial condition, before each drawing under the lending facility; or
 - (b) An annual (or more frequent) credit review based upon the borrower's current financial condition to determine whether or not the lending facility should be continued.
 - (3) The unused portion of retail credit card lines or other related plans that are unconditionally cancelable by the institution pursuant to applicable law.
- f. Liquidity facility provided to asset-backed commercial paper.
- (1) Noneligible asset-backed commercial paper liquidity facilities treated as recourse or direct credit substitute. Unused portion of asset-backed commercial paper liquidity facilities that do not meet the criteria for an eligible liquidity facility provided to asset-backed commercial paper pursuant to Paragraph (D)(8)(f)(2) of this Rule must be treated as recourse or as a direct credit substitute, and assessed the appropriate risk-based capital charge pursuant to Paragraph (E) of this Rule.
 - (2) Eligible asset-backed commercial paper liquidity facility. Except as provided in Paragraph (D)(8)(f)(3) of this Rule, in order for the unused portion of an asset-backed commercial paper liquidity facility to be eligible for either the 50 percent or 10 percent credit conversion factors under Paragraph (D)(8)(b)(2) or (D)(8)(d) of this Rule, the asset-backed commercial paper liquidity facility must satisfy the following criteria:
 - (a) At the time of draw, the asset-backed commercial paper liquidity facility must be subject to an asset quality test that:
 - (i) Precludes funding of assets that are ninety (90) days or more past due or in default; and

- (ii) If the assets that an asset-backed commercial paper liquidity facility is required to fund are externally rated securities at the time they are transferred into the program, the asset-backed commercial paper liquidity facility must be used to fund only securities that are externally rated investment grade at the time of funding. If the assets are not externally rated at the time they are transferred into the program, then they are not subject to this investment grade requirement.
 - (b) The asset-backed commercial paper liquidity facility must provide that, prior to any draws, the institution's funding obligation is reduced to cover only those assets that satisfy the funding criteria under the asset quality test as provided in Paragraph (D)(8)(f)(2)(a) of this Rule.
 - (3) Exception to eligibility requirements for assets guaranteed by the United States Government or its agencies, or the central government of an OECD country. Notwithstanding the eligibility requirements for asset-backed commercial paper program liquidity facilities in Paragraph (D)(8)(f)(2), the unused portion of an asset-backed commercial paper liquidity facility may still qualify for either the 50 percent or 10 percent credit conversion factors under Paragraph (D)(8)(b)(2) or (D)(8)(d) of this Rule, if the assets required to be funded by the asset-backed commercial paper liquidity facility are guaranteed, either conditionally or unconditionally, by the United States Government or its agencies, or the central government of an OECD country.
 - (4) Transition period for asset-backed commercial paper liquidity facilities. Notwithstanding the eligibility requirements for asset-backed commercial paper program liquidity facilities in Paragraph (D)(8)(f)(1) of this Rule, the unused portion of an asset-backed commercial paper liquidity facility will be treated as eligible liquidity facilities pursuant to Paragraph (D)(8)(f)(2) of this Rule, regardless of their compliance with the definition of eligible liquidity facilities, until September 30, 2005. On that date and thereafter, the unused portions of asset-backed commercial paper liquidity facilities that do not meet the eligibility requirements in Paragraph (D)(8)(f)(1) of this Rule will be treated as recourse obligations or direct credit substitutes.
- g. Derivative Contracts.
- (1) Calculation of Credit Equivalent Amounts. The credit equivalent amount of a derivative contract equals the sum of the current credit exposure and the potential future credit exposure of the derivative contract. The calculation of credit equivalent amounts must be measured in U.S. dollars, regardless of the currency or currencies specified in the derivative contract.

- (a) Current credit exposure. The current credit exposure for a single derivative contract is determined by the mark-to-market value of the derivative contract. If the mark-to-market value is positive, then the current exposure equals that mark-to-market value. If the mark-to-market value is zero or negative, then the current exposure is zero. The current credit exposure for multiple derivative contracts executed with a single counterparty and subject to a qualifying bilateral netting contract is determined as provided by Paragraph (D)(8)(g)(2)(a) of this Rule.
- (b) Potential future credit exposure. The potential future credit exposure for a single derivative contract, including a derivative contract with a negative mark-to-market value, is calculated by multiplying the notional principal of the derivative contract by one of the credit conversion factors in Table B for the appropriate category. The potential future credit exposure for gold contracts shall be calculated using the foreign exchange rate conversion factors. For any derivative contract that does not fall within one of the specified categories in Table B, the potential future credit exposure shall be calculated using the other commodity conversion factors. Subject to examiner review, institutions should use the effective rather than the apparent or stated notional amount in calculating the potential future credit exposure. The potential future credit exposure for multiple derivative contracts executed with a single counterparty and subject to a qualifying bilateral netting contract is determined as provided by Paragraph (D)(8)(g)(2)(a) of this Rule.

TABLE B Conversion Factor Matrix 1					
Remaining Maturity ²	Interest Rate	Foreign Exchange Rate and Gold	Equity ²	Precious Metals	Other Commodities
One Year or Less	0.0%	1.0%	6.0%	7.0%	10.0%
More Than One Year to 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%

1 For derivative contracts with multiple exchanges of principal, the conversion factors are multiplied by the number of remaining payments in the derivative contract.

2 For derivative contracts that automatically reset to zero value following a payment, the remaining maturity equals the time until the next payment. However, interest rate contracts with remaining maturities of greater than one year shall be subject to a minimum conversion factor of 0.5 percent

NOTE: For purposes of calculating either the potential future credit exposure under Paragraph (D)(8)(g)(1)(b) of this Rule or the gross potential future credit exposure under Paragraph (D)(8)(g)(2)(a)(2) of this Rule for foreign exchange contracts and other similar contracts in which the notional principal is equivalent to the cash flows, total notional principal is the net receipts to each party falling due on each value date in each currency. No potential future credit exposure is calculated for single currency interest rate swaps in which payments are made based upon two floating rate indices (so-called floating/floating or basis swaps); the credit equivalent amount is measured solely on the basis of the current credit exposure.

- (2) Derivative contracts subject to a qualifying bilateral netting contract.
- (a) Netting calculation. The credit equivalent amount for multiple derivative contracts executed with a single counterparty and subject to a qualifying bilateral netting contract pursuant to Paragraph (D)(8)(g)(2)(b) of this Rule is calculated by adding the net current credit exposure and the adjusted sum of the potential future credit exposure for all derivative contracts subject to the qualifying bilateral netting contract.
- (i) Net current credit exposure. The net current exposure is the net sum of all positive and negative mark-to-market values of the individual derivative contracts subject to a qualifying bilateral netting contract. If the net sum of the mark-to-market value is positive, then the net current credit exposure is equal to the net sum of the mark-to-market value. If the net sum of the mark-to-market values is zero or negative, then the net current credit exposure is zero.
- (ii) Adjusted sum of the potential future credit exposure. The adjusted sum of the potential future credit exposure is calculated as:

$$A_{\text{net}} = 0.4 \times A_{\text{gross}} + (0.6 \times \text{NGR} \times A_{\text{gross}})$$

A_{net} is the adjusted sum of the potential future credit exposure, A_{gross} is the gross potential future credit exposure, and NGR is the net to gross ratio. A_{gross} is the sum of the potential future credit exposure (as determined pursuant to Paragraph (D)(8)(g)(1)(b) of this Rule) for each individual derivative contract subject to the qualifying bilateral netting contract. The NGR is the ratio of the net current credit exposure to the gross current credit exposure. In calculating the NGR, the gross current credit exposure equals the sum of the positive current credit exposures (as determined pursuant to Paragraph (D)(8)(g)(1)(a) of this Rule) of all individual derivative contracts subject to the qualifying bilateral netting contract.

- (b) Qualifying bilateral netting contract. In determining the current credit exposure for multiple derivative contracts executed with a single counterparty, an institution may net derivative contracts subject to a qualifying bilateral netting contract by offsetting positive and negative mark-to-market values, provided that:
 - (i) The qualifying bilateral netting contract is in writing.
 - (ii) The qualifying bilateral netting contract is not subject to a walkaway clause.
 - (iii) The qualifying bilateral netting contract creates a single legal obligation for all individual derivative contracts covered by the qualifying bilateral netting contract. In effect, the qualifying bilateral netting contract must provide that the institution would have a single claim or obligation either to receive or to pay only the net amount of the sum of the positive and negative mark-to-market values on the individual derivative contracts covered by the qualifying bilateral netting contract. The single legal obligation for the net amount is operative in the event that a counterparty, or a counterparty to whom the qualifying bilateral netting contract has been assigned, fails to perform due to any of the following events: default, insolvency, bankruptcy, or other similar circumstances.
 - (iv) The institution obtains a written and reasoned legal opinion(s) that represents, with a high degree of certainty, that in the event of a legal challenge, including one resulting from default, insolvency, bankruptcy, or similar circumstances, the relevant court and administrative authorities would find the institution's exposure to be the net amount under:
 - a) The law of the jurisdiction in which the counterparty is chartered or the equivalent location in the case of noncorporate entities, and if a branch of the counterparty is involved, then also under the law of the jurisdiction in which the branch is located;
 - b) The law of the jurisdiction that governs the individual derivative contracts covered by the bilateral netting contract; and
 - c) The law of the jurisdiction that governs the qualifying bilateral netting contract.
 - (v) The institution establishes and maintains procedures to monitor possible changes in relevant law and to ensure that the qualifying bilateral netting contract continues to satisfy the requirement of this section.

- (vi) The institution maintains in its files documentation adequate to support the netting of a derivative contract. (By netting individual derivative contracts for the purpose of calculating its credit equivalent amount, an institution represents that documentation adequate to support the netting of a set of derivative contract(s) is in the institution's files and available for inspection by the Banking Board. Upon determination by the Banking Board that an institution's files are inadequate or that a qualifying bilateral netting contract may not be legally enforceable in any one of the bodies of law described in Paragraphs (D)(8)(g)(2)(b)(iv)(a) through (c) of this Rule, the underlying derivative contracts may not be netted for the purposes of this section.)
 - (3) Risk-weighting. Once the institution determines the credit equivalent amount for a derivative contract or a set of derivative contracts subject to a qualifying bilateral netting contract, the institution assigns that amount to the risk weight category appropriate to the counterparty, or, if relevant, the nature of any collateral or guarantee. However, the maximum weight that will be applied to the credit equivalent amount of such derivative contract(s) is 50 percent. (Derivative contracts are an exception to the general rule of applying collateral and guarantees to the face value of off-balance sheet items. The sufficiency of collateral and guarantees is determined on the basis of the credit equivalent amount of derivative contracts. However, collateral and guarantees held against a qualifying bilateral netting contract are not recognized for capital purposes unless it is legally available for all contracts included in the qualifying bilateral netting contract.)
 - (4) Exceptions. The following derivative contracts are not subject to the above calculation, and therefore, are not part of the denominator of an institution's risk-based capital ratio:
 - (a) An exchange rate contract with an original maturity of 14 calendar days or less (gold contracts do not qualify for this exception); and
 - (b) A derivative contract that is traded on an exchange requiring the daily payment of any variations in the market value of the contract.
- E. Recourse, Direct Credit Substitutes and Positions in Securitizations
- 1. Definitions. For purposes of Paragraph (E) of this Rule, the following definitions apply:
 - a. "Credit derivative" means a contract that allows one party (the protection purchaser) to transfer the credit risk of an asset or off-balance sheet credit exposure to another party (the protection provider). The value of a credit derivative is dependent, at least in part, on the credit performance of a "reference asset."
 - b. "Credit-enhancing interest-only strip" means an on-balance sheet asset that, in form or in substance:

- (1) Represents the contractual right to receive some or all of the interest due on transferred assets; and
 - (2) Exposes the institution to credit risk directly or indirectly associated with the transferred assets that exceeds its pro rata claim on the assets whether through subordination provisions or other credit enhancing techniques.
- c. "Credit-enhancing representations and warranties" means representations and warranties that are made or assumed in connection with a transfer of assets (including loan servicing assets) and that obligate an institution to protect investors from losses arising from credit risk in the assets transferred or the loans serviced. Credit-enhancing representations and warranties include promises to protect a party from losses resulting from the default or nonperformance of another party or from an insufficiency in the value of the collateral. Credit-enhancing representations and warranties do not include:
- (1) Early-default clauses and similar warranties that permit the return of, or premium refund clauses covering, one-to-four family residential first mortgage loans (as described in Paragraph (D)(7)(c)(3) of this Rule) for a period not to exceed one hundred twenty (120) days from the date of transfer. These warranties may cover only those loans that were originated within one year of the date of transfer;
 - (2) Premium refund clauses that cover assets guaranteed, in whole or in part, by the U.S. Government, a U.S. Government agency, or a U.S. Government-sponsored enterprise, provided the premium refund clauses are for a period not to exceed one hundred twenty (120) days from the date of transfer; or
 - (3) Warranties that permit the return of assets in instances of fraud, misrepresentation or incomplete documentation.
- d. "Direct credit substitute" means an arrangement in which an institution assumes, in form or in substance, credit risk associated with an on- or off-balance sheet asset or exposure that was not previously owned by the institution (third-party asset), and the risk assumed by the institution exceeds the pro rata share of the institution's interest in the third-party asset. If an institution has no claim on the third-party asset, then the institution's assumption of any credit risk is a direct credit substitute. Direct credit substitutes include:
- (1) Financial standby letters of credit that support financial claims on a third party that exceed an institution's pro rata share in the financial claim;
 - (2) Guarantees, surety arrangements, credit derivatives and similar instruments backing financial claims that exceed an institution's pro rata share in the financial claim;
 - (3) Purchased subordinated interests that absorb more than their pro rata share of losses from the underlying assets;
 - (4) Credit derivative contracts under which the institution assumes more than its pro rata share of credit risk on a third-party asset or exposure;

- (5) Loans of lines of credit that provide credit enhancement for the financial obligations of a third party;
 - (6) Purchased loan servicing assets if the servicer is responsible for credit losses or if the servicer makes or assumes credit-enhancing representations and warranties with respect to the loans serviced. Mortgage servicer cash advances that meet the conditions of Paragraph (E)(1)(i)(1) and (2) of this Rule, are not direct credit substitutes;
 - (7) Clean-up calls on third-party assets. Clean-up calls that are 10 percent or less of the original pool balance and that are exercisable at the option of the institution are not direct credit substitutes; and
 - (8) Unused portion of noneligible asset-backed commercial paper liquidity facilities.
- e. "Externally rated" means that an instrument or obligation has received a credit rating from at least one nationally recognized statistical rating organization.
- f. "Face amount" means the notional principal, or face value, amount of an off-balance sheet item; the amortized cost of an asset not held for trading purposes; and the fair value of a trading asset.
- g. "Financial asset" means cash or other monetary instrument, evidence of debt, evidence of an ownership interest in an entity, or a contract that conveys a right to receive or exchange cash or another financial instrument from another party.
- h. "Financial standby letter of credit" means a letter of credit or similar arrangement that represents an irrevocable obligation to a third-party beneficiary:
- (1) To repay money borrowed by, or advanced to, or for the account of, a second party (the account party); or
 - (2) To make payment on behalf of the account party, in the event that the account party fails to fulfill its obligation to the beneficiary.
- i. "Mortgage servicer cash advance" means funds that a residential mortgage servicer advances to ensure an uninterrupted flow of payments, including advances made to cover foreclosure costs or other expenses to facilitate the timely collection of the loan. A mortgage servicer cash advance is not a recourse obligation or a direct credit substitute if:
- (1) The servicer is entitled to full reimbursement and this right is not subordinated to other claims on the cash flows from the underlying asset pool; or
 - (2) For any one loan, the servicer's obligation to make nonreimbursable advances is contractually limited to an insignificant amount of the outstanding principal amount of that loan.
- j. "Nationally recognized statistical rating organization (NRSRO)" means an entity recognized by the Division of Market Regulation of the Securities and Exchange Commission (or any successor Division) (Commission) as a nationally recognized statistical rating organization for various purposes, including the Commission's uniform net capital requirements for brokers and dealers.

- k. "Recourse" means an institution's retention, in form or in substance, of any credit risk directly or indirectly associated with an asset it has sold that exceeds a pro rata share of that institution's claim on the asset. If an institution has no claim on a sold asset, then the retention of any credit risk is recourse. A recourse obligation typically arises when an institution transfers assets and retains an explicit obligation to repurchase assets or to absorb losses due to a default on the payment of principal or interest or any other deficiency in the performance of the underlying obligor or some other party. Recourse may also exist implicitly if an institution provides credit enhancement beyond any contractual obligation to support assets it has sold. The following are examples of recourse arrangements:
- (1) Credit-enhancing representations and warranties made on transferred assets;
 - (2) Loans servicing assets retained pursuant to an agreement under which the institution will be responsible for losses associated with the loans serviced. Mortgage servicer cash advances that meet the conditions of Paragraph (E)(1)(i)(1) and (2) of this Rule, are not recourse agreements;
 - (3) Retained subordinated interests that absorb more than their pro rata share of losses from the underlying assets;
 - (4) Assets sold under an agreement to repurchase, if the assets are not already included on the balance sheet;
 - (5) Loan strips sold without contractual recourse where the maturity of the transferred portion of the loan is shorter than the maturity of the commitment under which the loan is drawn;
 - (6) Credit derivatives issued that absorb more than the institution's pro rata share of losses from the transferred assets;
 - (7) Clean-up calls. Clean-up calls that are 10 percent or less of the original pool balance and that are exercisable at the option of the institution are not recourse arrangements; and
 - (8) Noneligible asset-backed commercial paper liquidity facilities.
- l. "Residual interest" means any on-balance sheet asset that represents an interest (including a beneficial interest) created by a transfer that qualifies as a sale (pursuant to generally accepted accounting principles) of financial assets, whether through a securitization or otherwise, and that exposes an institution to any credit risk directly or indirectly associated with the transferred asset that exceeds a pro rata share of that institution's claim on the asset, whether through subordination provisions or other credit enhancement techniques. Residual interests generally include credit-enhancing IO strips, spread accounts, cash collateral accounts, retained subordinated interests (and other forms of overcollateralization) and similar assets that function as a credit enhancement. Residual interests further include those exposures that, in substance, cause the institution to retain the credit risk of an asset or exposure that had qualified as a residual interest before it was sold. Residual interests generally do not include interests purchased from a third party.

- m. "Risk participation" means a participation in which the originating party remains liable to the beneficiary for the full amount of an obligation (e.g., a direct credit substitute) notwithstanding that another party has acquired a participation in that obligation.
 - n. "Securitization" means the pooling and repackaging by a special purpose entity of assets or other credit exposures that can be sold to investors. Securitization includes transactions that create stratified credit risk positions whose performance is dependent upon an underlying pool of credit exposures, including loans and commitments.
 - o. "Structured finance program" means a program where receivable interests and asset-backed securities issued by multiple participants are purchased by a special purpose entity that repackages those exposures into securities that can be sold to investors. Structured finance programs allocate credit risks, generally, between the participants and credit enhancement provided to the program.
 - p. "Traded position" means a position retained, assumed or issued in connection with a securitization that is externally rated, where there is a reasonable expectation that, in the near future, the rating will be relied upon by:
 - (1) Unaffiliated investors to purchase the position; or
 - (2) An unaffiliated third party to enter into a transaction involving the position, such as a purchase, loan or repurchase agreement.
2. Credit equivalent amounts and risk weights of recourse obligations and direct credit substitutes.
- a. Credit-equivalent amount. Except as otherwise provided, the credit-equivalent amount for a recourse obligation or direct credit substitute is the full amount of the credit-enhanced assets for which the institution directly or indirectly retains or assumes credit risk multiplied by a 100 percent conversion factor.
 - b. Risk-weight factor. To determine the institution's risk-weighted assets for off-balance sheet recourse obligations and direct credit substitutes, the credit equivalent amount is assigned to the risk category appropriate to the obligor in the underlying transaction, after considering any associated guarantees or collateral. For a direct credit substitute that is an on-balance sheet asset (e.g., a purchased subordinated security), an institution must calculate risk-weighted assets using the amount of the direct credit substitute and the full amount of the assets it supports, i.e., all the more senior positions in the structure.
3. Credit equivalent amount and risk weight of participations in, and syndications of, direct credit substitutes. The credit equivalent amount for a participation interest in, or syndication of, a direct credit substitute is calculated and risk weighted as follows:

- a. In the case of a direct credit substitute in which an institution has conveyed a risk participation, the full amount of the assets that are supported by the direct credit substitute is converted to a credit equivalent amount using a 100 percent conversion factor. The pro rata share of the credit equivalent amount that has been conveyed through a risk participation is then assigned to whichever risk-weight category is lower: the risk-weight category appropriate to the obligor in the underlying transaction, after considering any associated guarantees or collateral, or the risk-weight category appropriate to the party acquiring the participation. The pro rata share of the credit equivalent amount that has not been participated out is assigned to the risk-weight category appropriate to the obligor after considering any associated guarantees or collateral.
 - b. In the case of a direct credit substitute in which the institution has acquired a risk participation, the acquiring institution's pro rata share of the direct credit substitute is multiplied by the full amount of the assets that are supported by the direct credit substitute and converted using a 100 percent credit conversion factor. The resulting credit equivalent amount is then assigned to the risk-weight category appropriate to the obligor in the underlying transaction, after considering any associated guarantees or collateral.
 - c. In the case of a direct credit substitute that takes the form of a syndication where each institution or participating entity is obligated only for its pro rata share of the risk and there is no recourse to the originating entity, each institution's credit equivalent amount will be calculated by multiplying only its pro rata share of the assets supported by the direct credit substitute by a 100 percent conversion factor. The resulting credit equivalent amount is then assigned to the risk-weight category appropriate to the obligor in the underlying transaction, after considering any associated guarantees or collateral.
4. Externally rated positions: credit-equivalent amounts and risk weights.
- a. Traded positions. With respect to a recourse obligation, direct credit substitute, residual interest (other than a credit-enhancing IO strip) or asset- or mortgage-backed security that is a "traded position" and that has received an external rating on a long-term position that is one grade below investment grade or better, or a short-term position that is investment grade, the institution may multiply the face amount of the position by the appropriate risk weight, determined pursuant to Tables C or D of this Rule (stripped mortgage-backed securities or other similar instruments, such as IO or PO strips, that are not credit enhancing must be assigned to the 100 percent risk category). If a traded position receives more than one external rating, the lowest single rating will apply.

TABLE C		
Long-Term Rating Category	Examples	Risk Weight (In Percent)
Highest or second highest investment grade	AAA, AA	20
Third highest investment grade	A	50
Lowest investment grade	BBB	100
One category below investment grade	BB	200

TABLE D		
Short-Term Rating Category	Examples	Risk Weight (In Percent)
Highest investment grade	A-1, P-1	20
Second highest investment grade	A-2, P-2	50
Lowest investment grade	A-3, P-3	100

b. Non-traded positions. A recourse obligation, direct credit substitute, residual interest (but not a credit-enhancing IO strip) or asset- or mortgage-backed security extended in connection with a securitization that is not a “traded position” may be assigned a risk weight pursuant to Paragraph (E)(4)(a) of this Rule if:

- (1) It has been externally rated by more than one NRSRO;
- (2) It has received an external rating on a long-term position that is one category below investment grade or better or a short-term position that is investment grade by all NRSROs providing a rating;
- (3) The ratings are publicly available, and
- (4) The ratings are based on the same criteria used to rate traded positions.

If the ratings are different, the lowest rating will determine the risk category to which the recourse obligation, residual interest or direct credit substitute will be assigned.

5. Senior positions not externally rated. For a recourse obligation, direct credit substitute, residual interest or asset- or mortgage-backed security that is not externally rated but is senior or preferred in all features to a traded position (including collateralization and maturity) an institution may apply a risk weight to the face amount of the senior position pursuant to Paragraph (E)(4)(a) of this Rule, based upon the traded position, subject to any current or prospective supervisory guidance and the institution satisfying the Banking Board that this treatment is appropriate. This Paragraph (E) will apply only if the traded position provides substantive credit support to the unrated position until the unrated position matures.

6. Residual Interests.
 - a. Concentration limit on credit-enhancing IO strips. In addition to the capital requirement provided by Paragraph (E)(6)(b) of this Rule, an institution must deduct from Tier 1 capital all credit-enhancing IO strips in excess of 25 percent of Tier 1 capital pursuant to Paragraph (C)(1)(e) of this Rule.
 - b. Credit-enhancing IO strip capital requirement. After applying the concentration limit to credit-enhancing IO strips pursuant to Paragraph (E)(6)(a) of this Rule, an institution must maintain risk-based capital for a credit-enhancing IO strip equal to the remaining amount of the credit-enhancing IO strip (net of any existing associated deferred tax liability), even if the amount of risk-based capital required to be maintained exceeds the full risk-based capital requirement for the assets transferred. Transactions that, in substance, result in the retention of credit risk associated with a transferred credit-enhancing IO strip will be treated as if the credit-enhancing IO strip was retained by the institution and not transferred.
 - c. Other residual interests capital requirement. Except as provided in Paragraphs (E)(4) or (5) of this Rule, an institution must maintain risk-based capital for a residual interest (excluding a credit-enhancing IO strip) equal to the face amount of the residual interest that is retained on the balance sheet (net of any existing associated deferred tax liability), even if the amount of risk-based capital required to be maintained exceeds the full risk-based capital requirement for the assets transferred. Transactions that, in substance, result in the retention of credit risk associated with a transferred residual interest will be treated as if the residual interest was retained by the institution and not transferred.
 - d. Residual interests and other recourse obligations. Where the aggregate capital requirement for residual interests (including credit-enhancing IO strips) and recourse obligations arising from the same transfer of assets exceed the full risk-based capital requirement for those assets, an institution must maintain risk-based capital equal to the greater of the risk-based capital requirement for the residual interest as calculated under Paragraphs (E)(6)(a) through (c) of this Rule or the full risk-based capital requirement for the assets transferred.

7. Positions that are not rated by an NRSRO. A position (but not a residual interest) extended in connection with a securitization and that is not rated by an NRSRO may be risk-weighted based on the institution's determination of the credit rating of the position, as specified in Table E of this Rule, multiplied by the face amount of the position. In order to qualify for this treatment, the institution's system for determining the credit rating of the position must meet one of the three alternative standards set out in Paragraphs (E)(7)(a) through (c) of this Rule.

TABLE E		
Rating Category	Examples	Risk Weight (In Percent)
Investment grade	BBB, or Better	100
One category below investment grade	BB	200

- a. Internal risk rating used for asset-backed programs. A direct credit substitute (but not a purchased credit-enhancing IO strip) is assumed by an institution in connection with an asset-backed commercial paper program sponsored by the institution and the institution is able to demonstrate to the satisfaction of the Banking Board, prior to relying upon its use, that the institution's internal credit risk rating system is adequate. Adequate internal credit risk rating systems usually contain the following criteria:
- (1) The internal credit risk system is an integral part of the institution's risk management system that explicitly incorporates the full range of risks arising from an institution's participation in securitization activities;
 - (2) Internal credit ratings are linked to measurable outcomes, such as the probability that the position will experience any loss, the position's expected loss given default, and the degree of variance in losses given default on that position;
 - (3) The institution's internal credit risk system must separately consider the risk associated with the underlying loans or borrowers, and the risk associated with the structure of a particular securitization transaction;
 - (4) The institution's internal credit risk system must identify gradations of risk among "pass" assets and other risk positions;
 - (5) The institution must have clear, explicit criteria that are used to classify assets into each internal risk grade, including subjective factors;
 - (6) The institution must have independent credit risk management or loan review personnel assigning or reviewing the credit risk ratings;
 - (7) An internal audit procedure should periodically verify that internal risk ratings are assigned pursuant to the institution's established criteria;
 - (8) The institution must monitor the performance of the internal credit risk ratings assigned to nonrated, nontraded direct credit substitutes over time to determine the appropriateness of the initial credit risk rating assignment and adjust individual credit risk ratings, or the overall internal credit risk ratings system, as needed; and
 - (9) The internal credit risk system must make credit risk rating assumptions that are consistent with, or more conservative than, the credit risk rating assumptions and methodologies of NRSROs.

- b. Program Ratings. A direct credit substitute or recourse obligation (but not a residual interest) is assumed or retained by an institution in connection with a structured finance program and a NRSRO has reviewed the terms of the program and stated a rating for positions associated with the program. If the program has options for different combinations of assets, standards, internal credit enhancements and other relevant factors, and the NRSRO specifies ranges of rating categories to them, the institution may apply the rating category applicable to the option that corresponds to the institution's position. In order to rely on a program rating, the institution must demonstrate to the Banking Board's satisfaction that the credit risk rating assigned to the program meets the same standards generally used by NRSROs for rating traded positions. The institution must also demonstrate to the Banking Board's satisfaction that the criteria underlying the NRSRO's assignment of ratings for the program are satisfied for the particular position. If an institution participates in a securitization sponsored by another party the Banking Board may authorize the institution to use this approach based on a program rating obtained by the sponsor of the program.
 - c. Computer Program. The institution is using an acceptable credit assessment computer program to determine the rating of a direct credit substitute or recourse obligation (but not a residual interest) extended in connection with a structured finance program. A NRSRO must have developed the computer program and the institution must demonstrate to the Banking Board's satisfaction that ratings under the program correspond credibly and reliably with the rating of traded positions.
8. Limitations on risk-based capital requirements.
- a. Low-level exposure rule. If the maximum contractual exposure to loss retained or assumed by an institution is less than the effective risk-based capital requirement, as determined pursuant to Paragraph (E)(2) of this Rule, for the asset supported by the institution's position, the risk-based capital required under this Rule is limited to the institution's contractual exposure, less any recourse liability account established pursuant to generally accepted accounting principles. This limitation does not apply when an institution provides credit enhancement beyond any contractual obligation to support assets that it has sold.
 - b. Related on-balance sheet assets. If an asset is included in the calculation of the risk-based capital requirements under this Paragraph (E) of this Rule and also appears as an asset on an institution's balance sheet, the asset is risk-weighted only under this Paragraph (E) of this Rule, except in the case of loan servicing assets and similar arrangements with embedded recourse obligations or direct credit substitutes. In that case, both the on-balance sheet servicing assets and the related recourse obligations or direct credit substitutes must both be separately risk-weighted and incorporated into the risk-based capital calculation.
9. Alternative Capital Calculation for Small Business Obligations.
- a. Definitions. For purposes of this Paragraph (E)(9):
 - (1) "Qualified institution" means an institution that:
 - (a) Is well capitalized without applying the capital treatment described in this Paragraph (E)(9), or

- (b) Is adequately capitalized without applying the capital treatment described in this Paragraph (E)(9) and has received written permission from the Banking Board to apply the capital treatment described in this Paragraph (E)(9).
 - (2) "Recourse" has the meaning given to such term under generally accepted accounting principles.
 - (3) "Small business" means a business that meets the criteria for a small business concern established by the Small Business Administration.
 - b. Capital and reserve requirements. Notwithstanding the risk-based capital treatment outlined in Paragraph (C)(1)(g) and any other subsection (other than subsection (9) of this Paragraph (E)), with respect to a transfer of a small business loan or a lease of personal property with recourse that is a sale under generally accepted accounting principles, a qualified institution may elect to apply the following treatment:
 - (1) The institution establishes and maintains a non-capital reserve under generally accepted accounting principles sufficient to meet the reasonable estimated liability of the institution under the recourse arrangement; and
 - (2) For purposes of calculating the institution's risk-based capital ratio, the institution includes only the face amount of its recourse in its risk-weighted assets.
 - c. Limit on aggregate amount of recourse. The total outstanding amount of recourse retained by a qualified institution with respect to transfers of small business loans and leases of personal property and included in the risk-weighted assets of the institution as described in Paragraph (E)(9)(b) of this Rule may not exceed 15 percent of the institution's total capital after adjustments and deductions, unless the Banking Board specifies a greater amount by order.
 - d. Institution that ceases to be qualified or that exceeds aggregate limit. If an institution ceases to be a qualified institution or exceeds the aggregate limit in Paragraph (E)(9)(c) of this Rule, the institution may continue to apply the capital treatment described in Paragraph (E)(9)(b) of this Rule to transfers of small business loans and leases of personal property that occurred when the institution was qualified and did not exceed the limit.
- F. Target Ratios
 - 1. As of December 31, 1992:
 - a. All institutions are expected to maintain a minimum ratio of total capital (after deductions) to risk-weighted assets of 8.0 percent.
 - b. Tier 2 capital elements qualify as part of an institution's total capital base up to a maximum of 100 percent of that institution's Tier 1 capital.
 - c. In addition to the standards established by these risk-based capital guidelines, all institutions must maintain a minimum capital-to-total asset ratio, pursuant to the provisions of Banking Board Rule CB101.51.

APPENDIX A MARKET RISK

A. Purpose and Applicability.

1. The purpose of this Appendix is to ensure that institutions with significant exposure to market risk maintain adequate capital to support that exposure. This Appendix supplements and adjusts the risk-based capital ratio calculations under this Rule with respect to those institutions.
2. Applicability.
 - a. This Appendix applies to any institution whose trading activity (on a worldwide consolidated basis) equals:
 - (1) Ten percent or more of total assets as reported in the most recent Call Report; or
 - (2) One billion dollars or more.

NOTE: Trading activity means the gross sum of trading assets and liabilities as reported in the institution's most recent quarterly Call Report.
 - b. The Banking Board may apply this Appendix to any institution if it deems it necessary or appropriate for safe and sound practices.
 - c. The Banking Board may exclude any institution otherwise meeting the criteria from Paragraph (A)(2)(a) of this Appendix from coverage under this Appendix if it determines the institution meets such criteria as a consequence of accounting, operational, or similar considerations, and the Banking Board deems it consistent with safe and sound practices.

B. Definitions

1. "Covered position" means all positions in an institution's trading account, and all foreign exchange and commodity positions, whether or not in the trading account. Positions include on-balance sheet assets and liabilities and off-balance sheet items. Securities subject to repurchase and lending agreements are included as if they are still owned by the lender. Asset-backed commercial paper liquidity facilities, in form or in substance, in an institution's trading account are excluded from covered positions, and instead, are subject to the risk-based capital requirements as provided in this Rule. (Subject to supervisory review, an institution may exclude structural positions in foreign currencies from its covered positions.)
2. "Market risk" means the risk of loss resulting from movements in market prices. Market risk consists of general market risk and specific risk components.
 - a. "General market risk" means changes in the market value of covered positions resulting from broad market movements, such as changes in the general level of interest rates, equity prices, foreign exchange rates, or commodity prices.
 - b. "Specific risk" means changes in the market value of specific positions due to factors other than broad market movements and includes default and event risk as well as idiosyncratic variations.
3. Tier 1 and Tier 2 capital are defined in Paragraph (C) of this Rule.

4. Tier 3 capital is subordinated debt that is unsecured; is fully paid up; has an original maturity of at least two years; is not redeemable before maturity without prior approval by the Banking Board; includes a lock-in clause precluding payment of either interest or principle (even at maturity) if the payment would cause the issuing institution's risk-based capital ratio to fall or remain below the minimum required under this Rule; and does not contain and is not covered by any covenants, terms, or restrictions that are inconsistent with safe and sound practices.
 5. "Value-at-risk (VAR)" means the estimate of the maximum amount that the value of covered positions could decline during a fixed holding period within a stated confidence level, measured pursuant to Paragraph (D) of this Appendix.
- C. Adjustments to the Risk-Based Capital Ratio Calculations
1. Risk-based capital ratio denominator. An institution subject to this Appendix shall calculate its risk-based capital ratio denominator as follows:
 - a. Adjusted risk-weighted assets.
 - (1) Covered positions. Calculate adjusted risk-weighted assets, which equals risk-weighted assets (as calculated pursuant to this Rule), excluding the risk-weighted amounts of all covered positions (except foreign exchange positions outside the trading account and over-the-counter derivative positions). (Foreign exchange positions outside the trading account and all over-the-counter derivative positions, whether or not in the trading account, must be included in adjusted risk-weighted assets).
 - (2) Securities borrowing transactions. In calculating adjusted risk-weighted assets, an institution also may exclude a receivable that results from the institution's posting of cash collateral in a securities borrowing transaction to the extent that the receivable is collateralized by the market value of the borrowed securities and is subject to the following conditions:
 - (a) The borrowed securities must be includable in the trading account and must be liquid and readily marketable;
 - (b) The borrowed securities must be marked to market daily;
 - (c) The receivable must be subject to a daily margining requirement; and
 - (d) The securities borrowing transaction must be a securities contract for purposes of section 555 of the Bankruptcy Code, a qualified financial contract for purposes of section 11(e)(8) of the Federal Deposit Insurance Act, or a netting contract between or among financial institutions, for purposes of section 401-407 of the Federal Deposit Insurance Corporation Improvement Act of 1991 or Regulation EE.
 - b. Measure for market risk. Calculate the measure for market risk, which equals the sum of the VAR-based capital charge, the specific risk add-on (if any), and the capital charge for de minimus exposures (if any).

- (1) VAR-based capital charge. The VAR-based capital charge equals the higher of:
 - (a) The previous day's VAR measure; or
 - (b) The average of the daily VAR measures for each of the preceding sixty (60) business days multiplied by three, except as provided in Paragraph (D)(5) of this Appendix;
 - (2) Specific risk add-on. The specific risk add-on is calculated pursuant to Paragraph (E) of this Appendix; and
 - (3) Capital charge for de minimus exposure. The capital charge for de minimus exposure is calculated pursuant to Paragraph (D)(1) of this Appendix.
 - c. Market risk equivalent assets. Calculate market risk equivalent assets by multiplying the measure for market risk (as calculated in Paragraph (C)(1)(b) of this Appendix) by 12.5.
 - d. Denominator calculation. Add market risk equivalent assets (as calculated in Paragraph (C)(1)(c) of this Appendix) to adjusted risk-weighted assets (as calculated in Paragraph (C)(1)(a) of this Appendix). The resulting sum is the institution's risk-based capital ratio denominator.
2. Risk-based capital ratio numerator. An institution subject to this Appendix shall calculate its risk-based capital ratio numerator by allocating capital as follows:
 - a. Credit risk allocation. Allocate Tier 1 and Tier 2 capital equal to 8.0 percent of adjusted risk-weighted assets (as calculated in Paragraph (C)(1)(a) of this Appendix).

(An institution may not allocate Tier 3 capital to support credit risk.)
 - b. Market risk allocation. Allocate Tier 1, Tier 2, and Tier 3 capital equal to the measure for market risk as calculated in Paragraph (C)(1)(b) of this Appendix. The sum of Tier 2 and Tier 3 capital allocated for market risk must not exceed 250 percent of Tier 1 capital allocated for market risk. (This requirement means that Tier 1 capital allocated in this Paragraph must equal at least 28.6 percent of the measure for market risk.)
 - c. Restrictions.
 - (1) The sum of Tier 2 capital (both allocated and excess) and Tier 3 capital (allocated in Paragraph (C)(2)(b) of this Appendix) may not exceed 100 percent of Tier 1 capital (both allocated and excess).

(Excess Tier 1 capital means Tier 1 capital that has not been allocated in Paragraphs (C)(2)(a) and (b) of this Appendix. Excess Tier 2 capital means Tier 2 capital that has not been allocated in Paragraphs (C)(2)(a) and (b) of this Appendix, subject to the restrictions in Paragraph (C)(2)(c) of this Appendix.)

(2) Term subordinated debt (and intermediate-term preferred stock and related surplus) included in Tier 2 capital (both allocated and excess) may not exceed 50 percent of Tier 1 capital (both allocated and excess).

d. Numerator calculation. Add Tier 1 capital (both allocated and excess), Tier 2 capital (both allocated and excess), and Tier 3 capital (allocated under Paragraph (C)(2)(b) of this Appendix). The resulting sum is the institution's risk-based capital ratio numerator.

D. Internal Models

1. General. For risk-based capital purposes, an institution subject to this Appendix must use its internal model to measure its daily VAR, pursuant to the requirements of this Appendix. The Banking Board may permit an institution to use alternative techniques to measure the market risk of de minimus exposures so long as the techniques adequately measure associated market risk.

(An institution's internal model may use any generally accepted measurement techniques, such as variance-covariance models, historical simulations, or Monte Carlo simulations. However, the level of sophistication and accuracy of an institution's internal model must be commensurate with the nature and size of its covered positions. An institution that modifies its existing modeling procedures to comply with the requirements of this Appendix for risk-based capital purposes should, nonetheless, continue to use the internal model it considers most appropriate in evaluating risks for other purposes.)

2. Qualitative requirements. An institution subject to this Appendix must have a risk management system that meets the following minimum qualitative requirements:

- a. The institution must have a risk control unit that reports directly to senior management and is independent from business trading units.
- b. The institution's internal risk measurement model must be integrated into the daily management process.
- c. The institution's policies and procedures must identify, and the institution must conduct, appropriate stress tests and backtests. The institution's policies and procedures must identify the procedures to follow in response to the results of such tests.

(Stress tests provide information about the impact of adverse market events on an institution's covered positions. Backtests provide information about the accuracy of an internal model by comparing an institution's daily VAR measures to its corresponding daily trading profits and losses.)

d. The institution must conduct independent reviews of its risk measurement and risk management systems at least annually.

3. Market risk factors. The institution's internal model must use risk factors sufficient to measure the market risk inherent in all covered positions. The risk factors must address interest rate risk, equity price risk, foreign exchange rate risk, and commodity price risk.

(For material exposures in the major currencies and markets, modeling techniques must capture spread risk and must incorporate enough segments of the yield curve--at least six--to capture differences in volatility and less than perfect correlation of rates along the yield curve.)

4. Quantitative requirements. For regulatory capital purposes, VAR measures must meet the following quantitative requirements:
 - a. The VAR measures must be calculated on a daily basis using a 99 percent, one-tailed confidence level with a price shock equivalent to a ten (10) business day movement in rates and prices. In order to calculate VAR measures based on a ten (10) day price shock, the institution may either calculate ten (10) day figures directly or convert VAR figures based on holding periods other than ten (10) days to the equivalent of a ten (10) day holding period (for instance, by multiplying a one (1) day VAR measure by the square root of ten).
 - b. The VAR measures must be based on an historical observation period (or effective observation period for an institution using a weighting scheme or other similar method) of at least one (1) year. The institution must update data sets at least once every three (3) months or more frequently as market conditions warrant.
 - c. The VAR measurements must include the risks arising from the non-linear price characteristics of options positions and the sensitivity of the market value of the positions to changes in the volatility of the underlying rates or prices. An institution with a large or complex options portfolio must measure the volatility of options positions by different maturities.
 - d. The VAR measures may incorporate empirical correlations within and across risk categories, provided that the institution's process for measuring correlations is sound. In the event that the VAR measures do not incorporate empirical correlations across risk categories, then the institution must add the separate VAR measures for the four major risk categories to determine its aggregate VAR measure.

5. Backtesting
 - a. Beginning one (1) year after an institution starts to comply with this Appendix, it must conduct backtesting by comparing each of its most recent two hundred fifty (250) business days' actual net trading profit or loss with the corresponding daily VAR measures generated for internal risk measurement purposes and calibrated to a one-day holding period and a 99 percent, one-tailed confidence level.

(Actual net trading profits and losses typically include such things as realized and unrealized gains and losses on portfolio positions as well as fee income and commissions associated with trading activities.)
 - b. Once each quarter, the institution must identify the number of exceptions that is, the number of business days for which the magnitude of the actual daily net trading loss, if any, exceeds the corresponding daily VAR measures.
 - c. An institution must use the multiplication factor indicated in Table 1 of this Appendix in determining its capital charge for market risk under Paragraph (C)(1)(b)(1)(b) of this Appendix until it obtains the next quarter's backtesting results, unless the Banking Board determines that a different adjustment or other action is appropriate.

TABLE 1 MULTIPLICATION FACTOR BASED ON RESULTS OF BACKTESTING

Number of Exceptions	Multiplication Factor
4 or Fewer	3.00
5	3.40
6	3.50
7	3.65
8	3.75
9	3.85
10 or More	4.00

E. Specific Risk

1. Specific risk surcharge. For the purposes of this Paragraph (C)(1)(b)(2) of this Appendix, an institution shall calculate its specific risk surcharge as follows:
 - a. Internal models that incorporate specific risk.
 - (1) No specific risk surcharge required for qualifying internal models. An institution that incorporates specific risk in its internal model has no specific risk surcharge for purposes of Paragraph (C)(1)(b)(2) of this Appendix if the institution demonstrates to the Banking Board that its internal model adequately measures all aspects of specific risk, including default and event risk, of covered debt and equity positions. In evaluating an institution's internal model, the Banking Board will take into account the extent to which the internal model:
 - (a) Explains the historical price variation in the trading portfolio; and
 - (b) Captures concentrations.
 - (2) Specific risk surcharge for modeled specific risk that fails to adequately measure default or event risk. An institution that incorporates specific risk in its internal model but fails to demonstrate that its internal model adequately measures all aspects of specific risk, including default and event risk, as provided by Paragraph (E)(1)(a) of this Appendix, must calculate its specific risk surcharge pursuant to one of the following methods:
 - (a) If the institution's internal model separates the VAR measure into a specific risk portion and a general market risk portion, then the specific risk surcharge equals the previous day's specific risk portion.
 - (b) If the institution's internal model does not separate the VAR measure into a specific risk portion and a general market risk portion, then the specific risk surcharge equals the sum of the previous day's VAR measure for subportfolios of covered debt and equity positions.
 - b. Specific risk surcharge for specific risk not modeled. If an institution does not model specific risk pursuant to Paragraph (E)(1)(a) of this Appendix, then the institution shall calculate its specific risk surcharge using the standard specific risk capital charge pursuant to Paragraph (E)(3) of this Appendix.

2. Covered debt and equity position. If a model includes the specific risk of covered debt positions but not covered equity positions (or vice versa), then the institution may reduce its specific risk charge for the included positions under Paragraph (E)(1)(a)(2) of this Appendix. The specific risk charge for the positions not included equals the standard specific risk capital charge under Paragraph (E)(3) of this Appendix.
3. Standard specific risk capital charge. The standard specific risk capital charge equals the sum of the components for covered debt and equity positions as follows:
 - a. Covered debt positions
 - (1) For the purposes of Paragraph (E) of this Appendix, covered debt positions means fixed-rate or floating-rate debt instruments located in the trading account and instruments located in the trading account with values that react primarily to changes in interest rates, including certain non-convertible preferred stock, convertible bonds, and instruments subject to repurchase and lending agreements. Also included are derivatives (including written and purchased options) for which the underlying instrument is a covered debt instrument that is subject to a non-zero specific risk capital charge.
 - (a) For covered debt positions that are derivatives, an institution must risk-weight (as described in Paragraph (E)(3)(a)(3) of this Appendix) the market value of the effective notional amount of the underlying debt instrument or index portfolio. Swaps must be included as the notional position in the underlying debt instrument or index portfolio, with a receiving side treated as a long position and a paying side treated as a short position; and
 - (b) For covered debt positions that are options, whether long or short, an institution must risk-weight (as described in Paragraph (E)(3)(a)(3) of this Appendix) the market value of the effective notional amount of the underlying debt instrument or index multiplied by the option's delta.
 - (2) An institution may net long and short covered debt positions (including derivatives) in identical debt issues or indices.
 - (3) An institution must multiply the absolute value of the current market value of each net long or short covered debt position by the appropriate specific risk weighting factor indicated in Table 2 of this Appendix. The specific risk capital charge component for covered debt positions is the sum of the weighted values.

TABLE 2 SPECIFIC RISK WEIGHTING FACTORS FOR COVERED DEBT POSITIONS

Category	Remaining Maturity (Contractual)	Weighting Factor (In Percent)
Government ¹	N/A	0.00
Qualifying ²	6 Months or Less	0.25
	Over 6 Months to 24 Months	1.00
	Over 24 Months	1.60
Other ³	N/A	8.00

1 The "government" category includes all debt instruments of central governments of OECD countries (as defined in Paragraph (B)(24) of this Rule) including bonds, Treasury bills, and other short-term instruments, as well as local currency instruments of non-OECD central governments to the extent the institution has liabilities booked in that currency.

2 The "qualifying" category includes debt instruments of United States Government-sponsored agencies (as defined in Paragraph (B)(36) of this Rule), general obligation debt instruments issued by states and other political subdivisions of OECD countries, multilateral development banks, and debt instruments issued by United States depository institutions or OECD-banks that do not qualify as capital of the issuing institution. This category also includes other debt instruments, including corporate debt and revenue instruments issued by states and other political subdivisions of OECD countries that are:

- a. Rated investment grade by at least two nationally recognized credit rating services;
- b. Rated investment grade by one nationally recognized credit rating agency and not rated less than investment-grade by any other credit rating agency; or
- c. Unrated, but deemed to be of comparable investment quality by the reporting institution and the issuer has instruments listed on a recognized stock exchange, subject to review by the Banking Board.

3 The "other" category includes debt instruments that are not included in the government or qualifying categories.

b. Covered equity positions

- (1) For the purposes of this Paragraph (E) of this Appendix, covered equity positions means equity instruments located in the trading account and instruments located in the trading account with values that react primarily to changes in equity prices, including voting or non-voting common stock, certain convertible bonds, and commitments to buy or sell equity instruments. Also included are derivatives (including written and purchased options) for which the underlying is a covered equity position.
 - (a) For covered equity positions that are derivatives, an institution must risk weight (as described in Paragraph (E)(3)(b)(3) of this Appendix) the market value of the effective notional amount of the underlying equity instrument or equity portfolio. Swaps must be included as the notional position in the underlying equity instrument or index portfolio, with a receiving side treated as a long position and a paying side treated as a short position; and
 - (b) For covered equity positions that are options, whether long or short, an institution must risk weight (as described in Paragraph (E)(3)(b)(3) of this Appendix) the market value of the effective notional amount of the underlying equity instrument or index multiplied by the option's delta.

- (2) An institution may net long and short covered equity positions (including derivatives) in identical equity issues or equity indices in the same market.

(An institution may also net positions in depository receipts against an opposite position in the underlying equity or identical equity in different markets, provided that the institution includes the costs of conversion.)

(3)

- (a) An institution must multiply the absolute value of the current market value of each net long or short covered equity position by a risk weighting factor of 8.0 percent, or by 4.0 percent if the equity is held in a portfolio that is both liquid and well-diversified. For covered equity positions that are index contracts comprising a well-diversified portfolio of equity instruments, the net long or short position is multiplied by a risk weighting factor of 2.0 percent.

(A portfolio is liquid and well-diversified if: (1) It is characterized by a limited sensitivity to price changes of any single equity issue or closely related group of equity issues held in the portfolio; (2) The volatility of the portfolio's value is not dominated by the volatility of any individual equity issue or by equity issues from any single industry or economic sector; (3) It contains a large number of individual equity positions, with no single position representing a substantial portion of the portfolio's total market value; and (4) It consists mainly of issues traded on organized exchanges or in well-established over-the-counter markets.)

- (b) For covered equity positions from the following futures-related arbitrage strategies, an institution may apply a 2.0 percent risk weighting factor to one side (long or short) of each position with the opposite side exempt from charge:

- (i) Long and short positions in exactly the same index at different dates or in different market centers; or
- (ii) Long and short positions in index contracts at the same date in different but similar indices.

- (c) For futures contracts on broadly-based indices that are matched by offsetting positions in a basket of stocks comprising the index, an institution may apply a 2.0 percent risk weighting factor to the futures and stock basket positions (long and short), provided that such trades are deliberately entered into and separately controlled, and that the basket of stocks comprises at least 90 percent of the capitalization of the index.

- (4) The specific risk capital charge component for covered equity positions is the sum of the weighted values.

F. The Banking Board reserves the authority to modify the application of any provisions in this Appendix to any institution, upon reasonable justification.

TC15 Suspicious Activity Reports [Section 11-109-103, C.R.S.] [Repealed eff. 04/30/2016]

TC16 Insurance [Section 11-109-104(1)(f), C.R.S.]

- A. A trust company must, at all times, maintain a surety bond appropriate to the size and scope of the company's business, but in no event in an amount less than \$1,000,000. In addition, a trust company must, at all times, maintain a fiduciary errors and omissions insurance policy appropriate to the size and scope of the company's business, but in no event in an amount less than \$1,000,000. In determining the amount of the surety bond and errors and omissions insurance, the trust company's board of directors shall give due and careful consideration to known elements and factors constituting risk and hazards for the company.
- B. Any surety bond or errors and omissions insurance secured by a trust company shall provide that the bonding company providing the bond(s), in the event of cancellation or nonrenewal of such bond(s), will give at least ninety (90) days notice to the trust company and to the State Bank Commissioner.

TC17 Deposit of Securities [Section 11-109-104(1)(a), C.R.S.]

- A. Purpose. The purpose of this Rule is to protect the Division of Banking against any expense it may incur in liquidating a trust company (nondeposit-taking trust company) when the assets of such trust company available to the Division of Banking for this purpose are insufficient.
- B. Definitions: For the purpose of this Rule:
 - 1. "Trust company" shall mean a Colorado trust company that is not authorized to accept or hold savings deposits, time deposits or certificates of deposit pursuant to Section 11-109-201(1)(d), C.R.S., of the Colorado Banking Code.
 - 2. "Depository trust company" shall mean a Colorado trust company that is authorized to accept and hold savings deposits, time deposits and certificates of deposit and whose deposits are insured by the Federal Deposit Insurance Corporation.
 - 3. "Eligible Securities" shall mean any investment or security that qualifies as Liquid Capital, as that term is defined in Banking Board Rule TC13.5.
 - 4. "Custodian" shall mean any commercial bank, trust company, depository trust company, or other entity approved by the Division of Banking, other than the trust company, for which the eligible securities are being held, approved by the State Bank Commissioner to hold in custody eligible securities.
- C. Deposit of Eligible Securities
 - 1. A trust company shall deposit with one or more custodians eligible securities having a market value of not less than \$250,000. Eligible securities, even if commingled with other assets of a trust company, shall be deemed by operation of law to be held in trust for the benefit of the Division of Banking in the event of the involuntary liquidation of a trust company. Upon deposit, a trust company shall notify the Division of Banking in writing of the name, address, and telephone number of each custodian and the identity and value of each of the eligible securities deposited with the custodian(s).
 - 2. The Custodial Agreement between a trust company and a custodian holding the eligible securities shall include the following:

“Upon receiving an Order issued by the Colorado State Banking Board that it is taking possession of and seizing the eligible securities hereunder, the custodian shall immediately surrender title and possession of such eligible securities to the State Bank Commissioner. The custodian(s) shall not be liable for any such relinquishment of the eligible securities undertaken in good faith and upon notice that appears valid on its face.”

3. A trust company shall include with each quarterly Report of Condition filed with the Division of Banking a list of the eligible securities on deposit with its custodian(s), together with the market value of the eligible securities as of the end of such quarter.
 4. A trust company may, from time to time, substitute other eligible securities for eligible securities on deposit with its custodian(s) provided that:
 - a. The market value of the substitute eligible securities will, when added to the value of the remaining eligible securities, equal or exceed the amount of the required deposit;
 - b. The Division of Banking is given not less than seven (7) days prior written notice identifying the eligible securities and the market value of the eligible securities to be withdrawn from the custodian(s), and listing the eligible securities and the market value of the eligible securities to be substituted therefore; and
 - c. A copy of the notice sent to the Division of Banking is sent to the custodian(s).
- D. Priority of division of banking.

In the event of the involuntary liquidation of a trust company, as provided in Sections 11-109-702 and 11-109-704, C.R.S., the custodian(s) shall immediately surrender the eligible securities to the Banking Board; and the Division of Banking shall have a first and prior claim against the eligible securities to satisfy the obligations incurred by the Division of Banking in carrying out its duties and responsibilities under Sections 11-109-702 and 11-109-704, C.R.S.

TC18 Investments in Loans [Section 11-109-902(1)(a), C.R.S.]

A. Purpose.

The purpose of this Rule is to permit Colorado trust companies that are insured by the Federal Deposit Insurance Corporation to diversify their investment portfolios by purchasing existing commercial loans or participations in existing commercial loans. It does not authorize Colorado trust companies to originate or make commercial loans, consumer loans, mortgage loans, or any other type of loan or to have a direct borrower-lender relationship with any person or business customer.

B. Definitions

1. An “existing commercial loan” means a direct or indirect loan or extension of credit that was made or initiated by a lender or financial institution, other than a Colorado trust company, to a business customer on the basis of any obligation of that customer to repay the funds, or repayable from specific property pledged by or on behalf of the business customer.

2. A “commercial loan” means a direct or indirect loan from a lender or financial institution to a business customer for the purpose of providing funds needed by that customer's business. The term “commercial loan” does not include bankers' acceptances, loans secured by bills of lading or warehouse receipts covering readily marketable securities, or loans to depository institutions, including but not limited to commercial banks, industrial banks, savings and loan associations, credit unions, or trust companies, or to non-depository trust companies.
3. “Business customer” means a corporation, partnership, joint venture, association, business trust, limited liability company, not-for-profit corporation, or similar entity or organization.

C. Purchase of Existing Commercial Loans.

A trust company may invest in existing commercial loans to the same extent that it could acquire or invest in such loans if it were operating as a national bank, subject to the following limitations and conditions:

1. The trust company's capital ratios fall within the adequately capitalized category with a risk-based capital ratio of at least 8 percent, a Tier 1 capital ratio of at least 5 percent, and a leverage ratio of at least 4 percent. The capital ratios are defined in Banking Board Rule TC13-Minimum Capital Ratios, and Banking Board Rule TC14-Risk-Based Capital Definitions and Adequacy.
2. The aggregate of existing commercial loans shall not exceed 50 percent of the trust company's assets.
3. Except where an existing loan is in default, an existing commercial loan shall be maintained and serviced by the originator of the loan or someone acting on behalf of the originator and not by the trust company.
4. Existing commercial loans do not exceed the lending limits contained in this Rule.
5. For all investments in existing commercial loans, a reserve for loan losses shall be established in accordance with the requirements applicable to state chartered commercial banks.
6. Before investing in existing commercial loans, a trust company shall amend its investment policy to include the guidelines and procedures to be utilized by the trust company in acquiring and monitoring such credits.
7. Before investing in existing commercial loans, a trust company shall have an officer qualified by character and experience consistent with the responsibilities and duties relating to investments in commercial loans.
8. A written lending policy, approved by the directors of the trust company, shall provide a foundation for sound portfolio management.
9. Investing in existing commercial loans shall be supervised by the board of directors of the trust company or a committee thereof.
10. The purchase of existing commercial loans from an affiliate shall be subject to the provisions of Sections 23A and 23B of the Federal Reserve Act.

D. Participations.

A trust company may purchase a participation in a loan that qualifies as an existing commercial loan provided that such participation comes within the limitations and conditions set forth in the preceding Paragraph.

E. Lending Limits.

An existing commercial loan representing obligations of the same obligor or business customer shall not exceed 15 percent of the trust company's total capital.

1. Combining Existing Commercial Loans to Separate Borrowers

a. General Rule

Existing commercial loans to one person will be attributed to other persons, for the purpose of this Rule, when: (1) the proceeds of such loans or extensions of credit are to be used for the direct benefit of the other person or persons; or (2) a common enterprise is deemed to exist between the persons.

b. Common Enterprise

- (1) Whether two or more persons are engaged in a common enterprise will depend upon a realistic evaluation of the facts and circumstances of the particular transaction.
- (2) Where the expected source of repayment for each existing commercial loan is the same for each person, a common enterprise will be deemed to exist and such loans or extensions of credit must be combined.
- (3) Where existing commercial loans are made to persons who are related through common control, including where one person is controlled by another person, a common enterprise will be deemed to exist if the persons are engaged in interdependent businesses or there is a substantial financial interdependence among them. A common enterprise will be deemed to exist when 50 percent or more of one person's gross receipts or gross expenditures, on an annual basis, are derived from transactions with one or more persons related through common control, as defined in this Paragraph of this Rule. Gross receipts and expenditures include gross revenues/expenses, intercompany loans, dividends, capital contributions, and similar receipts or payments.
- (4) A common enterprise will also be deemed to exist when separate persons borrow from the lender for the purpose of acquiring a business enterprise of which those persons will own more than 50 percent of the voting securities.
- (5) For the purpose of this Rule, control shall be presumed to exist when:
 - (a) One or more persons acting in concert directly or indirectly own, control, or have power to vote 25 percent or more of any class of voting securities of another person; or

- (b) One or more persons acting in concert control, in any manner, the election of a majority of the directors, trustees, or other persons exercising similar functions of another person; or
 - (c) Any other circumstances exist that indicate that one or more persons acting in concert directly or indirectly exercise a controlling influence over the management or policies of another person.
- c. Loans to Corporations
 - (1) For the purpose of this Rule, a corporation is a subsidiary of any person that owns or beneficially owns more than 50 percent of the voting stock of the corporation. Such ownership need not be direct. Thus, if Corporation A owns more than 50 percent of the voting stock of Corporation X which, in turn, owns more than 50 percent of the voting stock of Corporation Y, Corporation Y would be considered a subsidiary of both Corporation A and of Corporation X. For the purpose of this Rule, corporation includes a limited liability company organized under the laws of certain states.
 - (2) Existing commercial loans to a person and its subsidiary or to subsidiaries of one person need not be combined where the trust company has determined that the person and subsidiaries involved are not engaged in a common enterprise as that term is defined in this Rule.
 - (3) Notwithstanding Paragraph (E)(1)(c)(2) of this Rule, existing commercial loans to a corporate group may not exceed 50 percent of the trust company's total capital. This aggregate limitation applies only to existing commercial loans made pursuant to Paragraphs (E)(1)(b) and (c) of this Rule. A corporate group includes a person and all of its subsidiaries.
- d. Loans to Partnerships, Joint Ventures, and Associations
 - (1) Existing commercial loans to a partnership, joint venture, or association shall, for the purpose of this Rule, be considered loans or extensions of credit to each member of such partnership, joint venture, or association.
 - (2) Existing commercial loans to members of a partnership, joint venture, or association shall, for the purpose of this rule, be attributed to the partnership, joint venture, or association where one or more of the tests set forth in Paragraph (E)(1)(a) of this Rule is satisfied with respect to one or more such members. However, loans to members of a partnership, joint venture, or association will not be attributed to other members of the partnership, joint venture, or association under this section of this Rule unless one or more of the tests set forth in Paragraph (E)(1)(a) of this Rule is satisfied with respect to such other members. The tests set forth in Paragraph (E)(1)(a) of this Rule shall be deemed to be satisfied when existing commercial loans are made to members of a partnership, joint venture, or association for the purpose of purchasing an interest in such partnership, joint venture, or association.

- (3) The Rule set forth in Paragraph (E)(1)(d)(1) of this Rule is not applicable to limited partners in limited partnerships or to members of joint ventures or associations if such partners or members, by terms of the partnership or membership agreement, are not to be held liable for the debts or actions of the partnership, joint venture, or association. However, the Rules set forth in Paragraph (E)(1) of this Rule are applicable to such partners or members.
2. Exceptions to the Lending Limits
 - a. Discount of Commercial Business Paper
 - (1) Existing commercial loans arising from the discount of commercial or business paper evidencing an obligation to the person negotiating it with recourse shall not be subject to any limitation based on capital.
 - (2) This exception applies to negotiable paper given in payment of the purchase price of commodities in domestic or export transactions purchased for resale or to be used in connection with the fabrication of a product, or to be used for any other business purpose that may reasonably be expected to provide funds for payment of the paper. Existing commercial loans arising from the discount of paper of the kind described in this Paragraph must bear the full recourse endorsement of the owner. However, existing commercial loans arising from the discount of such paper in export transactions may be endorsed by such owner without recourse or with limited recourse, or may be accompanied by a separate agreement for limited recourse; provided, that if transferred without full recourse, the paper must be supported by an assignment of appropriate insurance covering the political, credit, and transfer risks applicable to the paper. Insurance provided by the Export-Import Bank or the Foreign Credit Insurance Association is considered appropriate for this purpose. Existing commercial loans based on this exception are not subject to any limitation.
 - (3) Since the reason for the unlimited credit under this exception is that the paper arises from the sale of a commodity that may reasonably be expected to provide funds for payment of the paper, failure to pay either principal or interest when due removes the reason for unlimited credit. Therefore, although the line of credit to the maker or endorser should not be classified as excessive by reason of such default, the paper on which the default has occurred must thereafter be taken into consideration in determining whether additional existing commercial loans may be acquired within the limits of this Rule. The same principles of disqualification from the exception applies to any renewal or extension of either the entire loan or an installment thereof.
 - b. Loans Secured by U.S. Obligations
 - (1) Existing commercial loans secured by bonds, notes, certificates of indebtedness, or Treasury bills of the United States or by other such obligations fully guaranteed as to principal and interest by the United States shall not be subject to any limitation based on capital.
 - (2) This exception applies only to the extent that existing commercial loans are fully secured by the current market value of obligations of the United States or guaranteed by the United States.

- (3) If the market value of the collateral declines to the extent that the existing commercial loan is no longer in conformance with this exception and exceeds the general 15 percent limitation, the existing commercial loan must be brought into conformance within five (5) business days.

c. Loans to or Guaranteed by a Federal Agency

- (1) Existing commercial loans to or secured by unconditional takeout commitments or guarantees of any department, agency, bureau, board, commission, or establishment of the United States or any corporation wholly owned directly or indirectly by the United States shall not be subject to any limitation based on capital.
- (2) This exception may apply to only that portion of the existing commercial loan that is covered by a federal guarantee or commitment.
- (3) For purposes of this exception, the commitment or guarantee must be payable in cash or its equivalent within sixty (60) days after demand for payment is made.
- (4) A guarantee or commitment is unconditional if the protection afforded the lender is not substantially diminished or impaired in the case of loss resulting from factors beyond the lender's control. Protection against loss is not materially diminished or impaired by procedural requirements, such as an agreement to take over only in the event of default, including default over a specific period of time, a requirement that notification of default be given within a specified period after its occurrence, or a requirement of good faith on the part of the lender.

d. Loans Secured by Segregated Deposit Accounts

- (1) Existing commercial loans secured by a segregated deposit account by the lender shall not be subject to any limitation based on capital.
- (2) The trust company must ensure that a security interest has been perfected by the lender in the deposit, including the assignment of a specifically identified deposit and any other actions required by state law.
- (3) Deposit accounts that may qualify for this exception include deposits in any form generally recognized as deposits. In the case of a deposit eligible for withdrawal prior to the maturity of the secured loan, the trust company must ensure that the lender has established internal procedures that will prevent the release of the security.

- (4) A deposit that is denominated and payable in a currency other than that of the existing commercial loan that it secures may be eligible for this exception if it is freely convertible to U.S. dollars. The trust company must ensure that the lender revalues the deposit at least monthly, using appropriate foreign exchange rates, to ensure that the existing commercial loan remains fully secured. This exception applies to only that portion of the loan or extension of credit that is covered by the U.S. dollar value of the deposit. If the U.S. dollar value of the deposit falls to the extent that the existing commercial loan is in nonconformance with this exception and exceeds the general 15 percent limitation, the trust company must ensure that the loan is brought into conformance by the lender within five (5) business days, except where judicial proceedings, regulatory actions, or other extraordinary occurrences prevent the lender from taking such action. This exception is not authority for lenders to take deposits denominated in foreign currencies.

3. Loans Charged Off in Whole or in Part

The lending limits apply to all existing existing commercial loans purchased by the trust company, including such loans that have been charged off on the books of the trust company in whole or in part. Existing commercial loans that have become unenforceable by reason of discharge in bankruptcy or are no longer legally enforceable for other reasons, are not existing commercial loans for purposes of this Rule.

4. Approval by Banking Board

Upon application by a trust company to the Banking Board, the Banking Board may allow a trust company to exceed the "lending limits" to purchase a specific existing commercial loan if the trust company proves that such loan will not adversely impact the safe and sound operations of the trust company and the protection of customers of the trust company. In making its decision, the Banking Board shall consider the quality of the existing commercial loans.

The Banking Board shall also have the authority to determine when an existing commercial loan putatively made to a person shall, for the purpose of this Paragraph, be attributed to another person.

TC19 Investment in a Subsidiary [Section 11-109-902(5), C.R.S.]

A. General Limitations

A trust company may invest in a subsidiary corporation or limited liability company (LLC) that engages in activities in which the parent trust company may engage, subject to the same limitations the parent trust company would be subject to if it were engaged in the activity, provided that the parent trust company holds at least an 80 percent ownership interest in the subsidiary corporation or LLC.

B. Additional Limitations

The subsidiary of a trust company may invest in a subsidiary corporation or LLC at less than an 80 percent ownership level provided that each of the following conditions are met:

1. The activities of the subsidiary corporation or LLC in which the investment is made are limited to activities that are part of, or incidental to, the trust company business;

2. The trust company is able to prevent the subsidiary corporation or LLC from engaging in activities that do not meet the foregoing standard;
3. The trust company's loss exposure is limited, as both a legal and accounting matter, and the trust company does not have open-ended liability for the obligations of the subsidiary corporation or LLC; and
4. The investment is convenient or useful to the trust company in carrying out its business and not a mere passive investment unrelated to the trust company's business.

TC20 Reports of Condition and Income (Call Report) Filing Requirements [Section 11-109-402(4)(a), C.R.S.]

A. Depository Trust Company Requirements

[Emergency rule expired 07/29/2020]

B. Non-Depository Trust Company Requirements

Non-depository trust companies must file quarterly Reports of Condition and Income (Call Reports) directly with the Colorado Division of Banking in paper form.

TC21 Fiduciary Self-Dealing [Section 11-109-103, C.R.S.]

- A. Unless lawfully authorized by the instrument creating the relationship, by court order or by Colorado law, funds held by a trust company as fiduciary shall not be invested in stock or obligations of, or property acquired from, the trust company or its directors, officers or employees of such affiliates. If the retention of stock or obligations of the trust company or its affiliates is authorized by the instrument creating the relationship, by a court order or by Colorado law, a trust company as fiduciary may exercise rights to purchase its own stock or securities convertible into its own stock when offered pro rata to stockholders. When the exercise of rights or receipt of the stock dividend results in fractional shareholding, additional fractional shares may be purchased to compliment the fractional shares acquired.
- B. A trust company may sell assets held by it as fiduciary in one account if the transaction is fair to both accounts and if such transaction is not prohibited by the terms of the governing instrument.
- C. A trust company may deposit funds of the estate or trust account as time or demand deposits in its own banking department and may borrow money on behalf of the fiduciary account from itself and may pledge or encumber estate or trust assets as security for such loan, provided such transactions are fair to the fiduciary account.

TC22 Establishment of a Colorado Office Location by a Trust Company Chartered in Another State [Section 11-109-202, C.R.S., et. seq.]

A. Definitions

For the purposes of this Rule

1. "Home state" means the state where the trust company is chartered.
2. "Home state supervisor" means the state supervisory agency with primary responsibility for chartering and supervising the trust company.

3. "Out-of-state trust company" shall mean any trust company chartered under the laws of another state and domiciled in that state.
4. "Representative trust office" shall have the same meaning as defined at Section 11-109-101(6), C.R.S.
5. "Trust business" shall have the same meaning as defined at Section 11-109-101(10), C.R.S.
6. "Trust office" shall have the same meaning as defined at Section 11-109-101(13), C.R.S.

B. Establishment of a Representative Trust Office

1. The Banking Board shall issue a certificate of authority to an out-of-state trust company to establish a representative trust office in Colorado upon finding that:
 - a. The out-of-state trust company is lawfully chartered and operating in good standing in the home state;
 - b. The out-of-state trust company has the authority to operate a representative office outside of its home state and the establishment of such office has been approved by the applicant's board of directors;
 - c. A trust company chartered by, and in good standing with, the Colorado Division of Banking would be allowed by the applicant's home state supervisor to establish a representative trust office under similar terms and conditions in the applicant's home state;
 - d. The applicant's home state supervisor has entered into a cooperative regulatory and information sharing agreement with the Division of Banking, and/or has entered into the Conference of State Bank Supervisors Nationwide Cooperative Agreement for the Supervision of Multi-State Trust Institutions;
 - e. The name that the representative trust office is to be operated under is not the same, or deceptively similar to that of an existing Colorado bank, trust company, or industrial bank; and,
 - f. The applicant has certified that a trust business will not be conducted at the representative office.

C. Establishment of a Trust Office

1. The Banking Board shall issue a certificate of authority to an out-of-state trust company to establish a trust office and conduct a trust business in Colorado upon finding that:
 - a. The out-of-state trust company is lawfully chartered and operating in good standing in the home state;
 - b. The out-of-state trust company has the authority to operate a trust office outside of its home state and the establishment of such office has been approved by the applicant's board of directors;

- c. A trust company chartered by, and in good standing with, the Colorado Division of Banking would be allowed by the applicant's home state supervisor to establish a trust office under similar terms and conditions in the applicant's home state;
- d. The applicant's home state supervisor has entered into a cooperative regulatory and information sharing agreement with the Division of Banking, and/or has entered into the Conference of State Bank Supervisors Nationwide Cooperative Agreement for the Supervision of Multi-State Trust Institutions;
- e. The name that the trust office is to be operated under is not the same, or deceptively similar to that of an existing Colorado bank, trust company, or industrial bank;
- f. If the applicant proposes to accept deposits, such deposits are insured by the Federal Deposit Insurance Corporation; and,
- g. The applicant maintains capital at or above the minimum standards as set forth in Banking Board Rule TC13 for depository trust companies, or Banking Board Rule TC13.5 for nondepository trust companies.
 - (1) An applicant may satisfy the minimum capital requirement by depositing eligible securities in accordance with the requirements of Banking Board Rule TC17 in an amount, when combined with the applicant's equity capital, sufficient to meet the required minimum capital levels.

D. Certificate of Authority

Before a certificate of authority is issued for a representative trust office or trust office, and annually thereafter on or before January 1 of each succeeding year, the out-of-state trust company shall pay to the Colorado Division of Banking a fee in an amount as set by the Banking Board and published in accordance with Banking Board Rule TC4. Each certificate of authority shall expire on January 1 unless the annual fee for the year has been paid prior to such date and the out-of-state trust company certifies in writing that it is, and shall remain, in compliance with the conditions of Paragraph (B) or (C) of this Rule, as applicable.

E. Termination of Certificate of Authority

The Commissioner may, upon ten (10) days notice, terminate a certificate of authority if it is determined that the out-of-state trust company is not in compliance with the conditions of Paragraph (B) or (C) of this Rule, as applicable. Within ten (10) days following receipt of the termination notice, the out-of-state trust company may file an application with the Banking Board for hearing to rescind the Commissioner's determination.

TC23 Application Procedures for Private Family Trust Company Charter [Section 11-109-1003, C.R.S.] [Repealed eff. 11/14/2013]

TC24 Private Family Trust Company Exemptions [Section 11-109-1003(1), C.R.S.] [Repealed eff. 11/14/2013]

TC25 Revocation of Exemption [Section 11-109-1006, C.R.S.] [Repealed eff. 11/14/2013]

TC26 Conversion of a Private Family Trust Company to a Public Trust Company [Section 11-109-1007, C.R.S.] [Repealed eff. 11/14/2013]

TC27 Change of Control of a Private Family Trust Company [Section 11-109-1007, C.R.S.]
[Repealed eff. 11/14/2013]

Editor's Notes

History

Rule TC13.5 eff. 07/30/2007.

Rules TC23-TC27 eff. 12/30/2008.

Rules TC23-TC27 repealed eff. 11/14/2013.

Rule TC15 repealed eff. 04/30/2016.

Rules TC11 D.7, TC20 A emer. rules eff. 04/02/2020; expired 07/29/2020.

Rules TC11 D.7, TC11 E eff. 04/14/2022.

Annotations

Rule TC5 (adopted 12/15/2005) was not extended by House Bill 07-1167 and therefore expired 05/15/2007.