

obligation to make a payment to the customer or to a third party in the event the customer fails to repay an outstanding debt obligation or fails to perform a contractual obligation is treated, for risk-based capital purposes, as respectively, a financial guarantee standby letter of credit or a performance standby.

f. A loan commitment, on the other hand, involves an obligation (with or without a material adverse change or similar clause) of the banking organization to fund its customer in the normal course of business should the customer seek to draw down the commitment.

g. Sale and repurchase agreements and asset sales with recourse (to the extent not included on the balance sheet) and forward agreements also are converted at 100 percent.⁴⁸ So-called "loan strips" (that is, short-term advances sold under long-term commitments without direct recourse) are treated for risk-based capital purposes as assets sold with recourse and, accordingly, are also converted at 100 percent.

h. Forward agreements are legally binding contractual obligations to purchase assets with certain drawdown at a specified future date. Such obligations include forward purchases, forward forward deposits placed,⁴⁹ and partly-paid shares and securities; they do not include commitments to make residential mortgage loans or forward foreign exchange contracts.

i. Securities lent by a banking organization are treated in one of two ways, depending upon whether the lender is at risk of loss. If a banking organization, as agent for a customer, lends the customer's securities and does not indemnify the customer against loss, then the transaction is excluded from the risk-based capital calculation. If,

⁴⁸ In regulatory reports and under GAAP, bank holding companies are permitted to treat some asset sales with recourse as "true" sales. For risk-based capital purposes, however, such assets sold with recourse and reported as "true" sales by bank holding companies are converted at 100 percent and assigned to the risk category appropriate to the underlying obligor or, if relevant, the guarantor or nature of the collateral, provided that the transactions meet the definition of assets sold with recourse (including assets sold subject to pro rata and other loss sharing arrangements), that is contained in the instructions to the commercial bank Consolidated Reports of Condition and Income (Call Report). This treatment applies to any assets, including the sale of 1- to 4-family and multifamily residential mortgages, sold with recourse. Accordingly, the entire amount of any assets transferred with recourse that are not already included on the balance sheet, including pools of 1- to 4-family residential mortgages, are to be converted at 100 percent and assigned to the risk category appropriate to the obligor, or if relevant, the nature of any collateral or guarantees. The terms of a transfer of assets with recourse may contractually limit the amount of the institution's liability to an amount less than the effective risk-based capital requirement for the assets being transferred with recourse. If such a transaction is recognized as a sale under GAAP, the amount of total capital required is equal to the maximum amount of loss possible under the recourse provision, less any amount held in an associated non-capital liability account established pursuant to GAAP to cover estimated probable losses under the recourse provision.

⁴⁹ Forward forward deposits accepted are treated as interest rate contracts.

alternatively, a banking organization lends its own securities or, acting as agent for a customer, lends the customer's securities and indemnifies the customer against loss, the transaction is converted at 100 percent and assigned to the risk weight category appropriate to the obligor, to any collateral delivered to the lending banking organization, or, if applicable, to the independent custodian acting on the lender's behalf. Where a banking organization is acting as agent for a customer in a transaction involving the lending or sale of securities that is collateralized by cash delivered to the banking organization, the transaction is deemed to be collateralized by cash on deposit in a subsidiary lending institution for purposes of determining the appropriate risk-weight category, provided that any indemnification is limited to no more than the difference between the market value of the securities and the cash collateral received and any reinvestment risk associated with that cash collateral is borne by the customer.

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By order of the Board of Governors of the Federal Reserve System, February 7, 1995.

William W. Wiles,

Secretary of the Board.

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FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 325

RIN 3064-AB20

Capital Maintenance

AGENCY: Federal Deposit Insurance Corporation (FDIC).

ACTION: Final rule.

SUMMARY: The FDIC is amending its capital standards for insured state nonmember banks to establish a limitation on the amount of certain deferred tax assets that may be included in (that is, not deducted from) Tier 1 capital for risk-based and leverage capital purposes. Under the final rule, deferred tax assets that can be realized through carrybacks to taxes paid on income earned in prior periods generally will not be subject to limitation for regulatory capital purposes. On the other hand, deferred tax assets that can only be realized if an institution earns sufficient taxable income in the future will be limited for regulatory capital purposes to the amount that the institution is expected to realize within one year of the most recent calendar quarter-end date, based on the institution's projection of taxable income for that year, or ten percent of Tier 1 capital, whichever is less. Deferred tax assets in excess of these limitations will be deducted from Tier

1 capital and from assets for purposes of calculating both the risk-based and leverage capital ratios.

This regulatory capital limit was developed on a consistent basis by the FDIC, the Board of Governors of the Federal Reserve System (FRB), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS) (hereafter, the federal banking agencies or the agencies) in response to the issuance by the Financial Accounting Standards Board (FASB) of Statement No. 109, "Accounting for Income Taxes" (FASB 109), in February 1992.

The capital limitation is intended to balance the FDIC's continued concerns about deferred tax assets that are dependent upon future taxable income against the fact that such assets will, in many cases, be realized. The limitation also ensures that state nonmember banks do not place excessive reliance on deferred tax assets to satisfy the minimum capital standards.

EFFECTIVE DATE: April 1, 1995.

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SUPPLEMENTARY INFORMATION:

I. Background

Characteristics of Deferred Tax Assets

Deferred tax assets are assets that reflect, for financial reporting purposes, amounts that will be realized as reductions of future taxes or as future receivables from a taxing authority. Deferred tax assets may arise because of specific limitations under tax laws of different tax jurisdictions that require that certain net operating losses (*i.e.*, when, for tax purposes, expenses exceed revenues) or tax credits be carried forward if they cannot be used to recover taxes previously paid. These "tax carryforwards" are realized only if the institution generates sufficient future taxable income during the carryforward period.

Deferred tax assets may also arise from the tax effects of certain events that have been recognized in one period for financial statement purposes but will result in deductible amounts in a future period for tax purposes, *i.e.*, the tax effects of "deductible temporary differences." For example, many depository institutions may report higher income to taxing authorities than