



Market Square Plaza | 17 N Second Street
Suite 1300 | Harrisburg, PA 17101
717.787.2665 | F 717.787.8773 | www.dobs.pa.gov

(Sent via e-mail)

February 19, 2015

To: CHIEF EXECUTIVE OFFICERS OF ALL PENNSYLVANIA STATE-CHARTERED BANKS,
BANK AND TRUST COMPANIES, AND SAVINGS BANKS

On January 1, 2015, revisions to capital regulations affecting U.S. depository institutions took effect.¹ The new rules, often known as Basel III, have several provisions, many of which phase-in over time. A key provision of the new rules permits all non-advanced approaches institutions² to make a one-time, irrevocable election to determine how most items reported in Accumulated Other Comprehensive Income (AOCI) will be handled for regulatory capital purposes. As a reminder, AOCI includes such items as unrealized gains and losses on certain securities. **The following information is intended to underscore the importance of this irrevocable election and to encourage you and the institution's board of directors to fully understand the implications of this election prior to March 31, 2015.**

With the filing of the March 31, 2015 Consolidated Reports of Condition and Income (Call Report), an institution that is not an advanced approaches institution must choose to either opt out or not opt out of the requirement to include most components of AOCI in common equity tier 1 capital. This election is irrevocable.

- For institutions that opt out, most AOCI items will not be included in the calculation of common equity tier 1 capital. In other words, most AOCI items will be treated, for regulatory capital purposes, in the same manner in which they were prior to the effective date.
- For institutions that do not opt out, most AOCI items will be included in the calculation of common equity tier 1 capital. This will affect the calculation of your legal lending limit pursuant to Sections 306 or 516 of the Banking Code of 1965, 7 P.S. §§ 306 or 516, as applicable.
- If a top-tier banking organization makes the AOCI opt-out election, all consolidated banking subsidiary organizations under it must make the same election.

The March 31, 2015 Call Report forms and instructions for Schedule RC-R, Regulatory Capital³ illustrate how to make this election on the reporting forms.

I recommend that the board of directors of all state-chartered, non-advanced approaches institutions carefully consider all implications of this election in both the long and short terms, as well as in different economic environments. The decision should be documented. As a reminder, examiners consider the amount of unrealized losses in the investment portfolio (and exposure to the possibility of unrealized losses) when qualitatively assessing capital adequacy and liquidity, regardless of the election decision. This could affect the assignment of CAMELS ratings and supervisory determinations going forward.

¹ Federal Register, Vol. 78, No. 198, October 11, 2013. <http://www.gpo.gov/fdsys/pkg/FR-2013-10-11/pdf/2013-21653.pdf>

² Generally, those institutions with less than \$250 billion in total assets. These institutions may also be referred to as those using the standardized approach for certain capital calculation purposes.

³ <https://www.fdic.gov/regulations/resources/call/index.html>

Please contact Robert C. Lopez, Director, Bureau of Commercial Institutions, at (717) 783-8240, or Joseph A. Moretz, Manager, Applications Division, at (717) 783-2253, if you or your staff have any questions regarding this important election.

Sincerely,

Redacted

/s/ Wendy S. Spícher
Deputy Secretary
Depository Institutions

Attachment

Revised Capital Rule References

To better illustrate the importance of this election, it is helpful to focus on the largest single component of AOCI—unrealized gains and losses on available-for-sale (AFS) securities. The table below compares how these items impact capital before and after the revised rules take effect and for both institutions that opt out and institutions that do not opt out.

Investment position	Treatment for institutions that opt out (same as current treatment)	Treatment for institutions that do not opt out
Unrealized gains <i>or</i> losses on AFS <i>debt</i> securities	Net Amount Filtered out (excluded from) regulatory capital	Recognized in Common Equity Tier 1 Capital
Unrealized losses on AFS <i>equity</i> securities	Net Amount Recognized in Common Equity Tier 1 Capital	Recognized in Common Equity Tier 1 Capital
Unrealized gains on AFS <i>equity</i> securities	Net Amount Recognized (up to 45%) in Tier 2 Capital	Recognized in Common Equity Tier 1 Capital

The following online references may prove helpful in further understanding this election and other capital rule revisions.

- [Interagency Community Bank Guide to the New Capital Rule](#)

http://www.fdic.gov/regulations/capital/Community_Bank_Guide.pdf

- [Expanded Community Bank Guide to the New Capital Rule for FDIC-Supervised Banks](#)

http://www.fdic.gov/regulations/capital/Community_Bank_Guide_Expanded.pdf

- Part 324: September 3, 2014 Final Rule: Regulatory Capital Rules: [Regulatory Capital, Revisions to the Supplementary Leverage Ratio](#)

https://www.fdic.gov/news/board/2014/2014-09-03_notice_dis_c_fr.pdf

- FDIC: [Regulatory Capital page](#)

<http://www.fdic.gov/regulations/capital/index.html>

- FDIC: [Capital Estimation Tool](#)

http://www.fdic.gov/regulations/capital/Bank_Estimation_Tool.xlsm