

Press Releases

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OTS 99-12 - Revisions to Uniform Risk-Based Capital Rules Adopted for Thrifts and Banks

Office of Thrift Supervision

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Revisions to Uniform Risk-Based Capital Rules Adopted for Thrifts and Banks

WASHINGTON, D.C., March 2, 1999 -- The Office of Thrift Supervision (OTS) and three other federal banking agencies today adopted revised uniform risk-based capital requirements for thrifts and banks for three types of assets:

- Construction loans on presold residential properties;
- Real estate loans secured by junior liens on 1- to 4-family residential properties; and
- Investments in mutual funds

The rule also simplifies and makes uniform the Tier 1 leverage standards, referred to in OTS regulations as the leverage ratio of core capital to adjusted total assets.

The key change from the rule as it was proposed Oct. 27, 1997, involves the treatment of junior liens on one-to-four family residential property. The final rule treats first and second mortgage liens to the same borrower by the same institution as a single extension of credit, if there are no intervening loans. Thus, thrifts and banks that hold both liens must calculate the risk-based capital requirement on the combined liens, assigning a 50-percent risk weight if the combined lien meets that category's criteria, and a 100-percent risk weight if it does not. The proposed rule treated the liens separately, and would have required all junior liens to be risk-weighted at 100 percent.

Risk-based capital standards require thrifts and banks to hold more capital for higher-risk assets. Each loan or other asset is weighted according to risk. For example, a qualifying one-to-four-family mortgage loan is generally assigned a risk weight of 50 percent, meaning 50 percent of the book value of that asset is included in the calculation of risk-weighted assets. In contrast, a commercial loan is risk-weighted at 100 percent.

Two other major provisions contained in the final rule adopted by OTS, Comptroller of the Currency (OCC), Federal Deposit Insurance Corporation (FDIC), and Federal Reserve System are:

Construction loans on presold residential property: All four agencies adopted the current FDIC and Federal Reserve practice of assigning a 50-percent risk weight to qualifying residential construction loans once the property is sold and other criteria satisfied, even if the sale occurs after the thrift makes the construction loan. OTS and the OCC previously permitted institutions to use a 50-percent risk weight only if the property was sold before the institution made the construction loan.

Mutual funds: An institution must assign its total investment in a mutual fund to the highest risk weight applicable to any asset that the fund is authorized to hold according to its prospectus. An institution, however, may opt to assign the investment on a pro-rata basis to different risk weight categories according to the investment limits for different categories in the fund's prospectus. Under previous OTS rules, the risk weight for the investment was the highest weight of any asset actually held by the fund, rather than the limits in the prospectus. On a case-by-case basis, institutions had been permitted to allocate multiple risk weights to the investment based on the fund's actual holdings.

In addition, the final rule simplifies the agencies' Tier 1 leverage standards by making them uniform and by aligning the leverage standards to the agencies' prompt corrective action regulations. All institutions, other than those with the highest composite supervisory rating of one, are required to have a Tier 1 capital ratio (the ratio of Tier 1 capital to total assets) of 4 percent. Institutions with the highest supervisory rating continue to be subject to a lower 3 percent Tier 1 leverage ratio requirement.

The rule, published in today's Federal Register, and effective April 1, 1999, is one of a series of steps the agencies are taking to implement a provision of the Riegle Community Development and Regulatory Improvement Act of 1994 requiring the federal banking agencies to work toward uniform regulations and policies.

[Risk-Based Capital Standards](#): Construction Loans on Presold Residential Properties; Junior Liens on 1- to 4-Family Residential Properties; and Investments in Mutual Funds; Leverage Capital Standards: Tier 1 Leverage Ratio; Final Rules

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The Office of Thrift Supervision (OTS), a bureau of the U.S. Treasury, regulates and supervises the nation's thrift industry. OTS' mission is to ensure the safety and soundness of thrift institutions and to support their role as home mortgage lenders and providers of other community credit and financial services. For copies of news releases or other documents call PubliFax at 202/906-5660, or visit the OTS web page at <http://www.ots.treas.gov>.