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Unraveling Bank Regulatory Developments Affecting Lending: Leveraged Lending Guidance, Basel III Capital and Liquidity Coverage Ratio Rule and More

Navigating Changes in the Long-Term Lending, Leveraged Lending, Securities Finance and Repo Markets

THURSDAY, SEPTEMBER 10, 2015

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

Lisa M. Ledbetter, Partner, **Jones Day**, Washington, D.C.

Ralph F. (Chip) MacDonald, III, Partner, **Jones Day**, Atlanta

The audio portion of the conference may be accessed via the telephone or by using your computer's speakers. Please refer to the instructions emailed to registrants for additional information. If you have any questions, please contact **Customer Service at 1-800-926-7926 ext. 10**.

APPENDIX 1

OVERVIEW OF U.S. BASEL III CAPITAL RULES

September 10, 2015

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U.S. Basel III Capital Rules

- General
  - Capital Minimums are increased.
  - Types of capital are more limited:
    - -- No new trust preferred with phase out of existing trust preferred for banks over $15 billion of assets. Smaller banks' trust preferreds are grandfathered.
    - -- Common stock and perpetual noncumulative preferred stock are most valuable under the regulations
    - -- Voting common stock should be a majority of CET1
    - -- The terms of capital instruments, especially subordinated debt, are changed
    - -- All buyback and redemptions of capital will be subject to prior regulatory scrutiny and approval
- The Prompt Corrective Action ("PCA") Rules of FDI Act, Section 38 are revised to reflect the new capital measures, and will affect deteriorating banks more quickly.

U.S. Basel III Capital Rules (cont'd)

- Risk weightings of assets and off-balance sheet exposures are revised in various cases.

- The amounts and risk weights of certain assets will require better capital planning, and may cause capital to be reallocated internally to seek better returns on investment.

- The changes in treatment of deferred tax assets and the increased risk weights on NPAs will cause problem banks to be resolved or recapitalized faster.

  - The value of DTAs will be diminished.

- Banks will need continuing and better access to the capital markets.

- Returns and shareholder value will depend on improved capital planning.

Basel III Capital Ratios

	Jan. 1, 2015	Fully Phased in Jan. 1, 2019
Minimum CET1 / RWA	4.50%	4.50%
CET1 Conservation Buffer	—	2.50%
Total CET1	4.50%	7.00%
Deductions and threshold deductions[1]	40.00%	100.00%
Minimum Tier 1 Capital	6.00%	6.00%
Minimum Tier 1 Capital *plus* capital conservation buffer[2]	—	8.50%
Minimum Total Capital	8.00%	8.00%
Minimum Total Capital *plus* conservation buffer[3]	8.00%	10.50%

[1] 20% per year phase in starting 2015.

[2] 6.625%, 7.25%, 7.875% for 2016, 2017 and 2018, respectively.

[3] 8.625%, 9.25% and 9.875% in 2016, 2017 and 2018, respectively.

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Basel III Capital Ratios (cont'd)

Minimum Ratios

	Current	Basel III
CET1 / RWA	—	4.5%
Leverage Ratio	4.0%	4.0%
Tier 1 capital/RWA	4.0%	6.0%
Total capital/RWA	8.0%	8.0%
Capital conservation buffer	—	2.50%

Prompt Corrective Action Categories
(Effective January 1, 2015)

	Minimums	
	Current	Basel III
Well capitalized		
CET1	–	6.5%
Tier 1 risk-based capital	6.0%	8.0%
Total risk-based capital	10.0%	10.0%
Tier 1 leverage ratio	5.0%	5.0%
Undercapitalized		
CET1	–	< 6.0%
Tier 1 risk-based capital	< 4.0%	< 6.0%
Total risk-based capital	< 8.0%	< 8.0%
Tier 1 leverage ratio	< 5.0%	< 4.0%
Critically undercapitalized	Tangible equity to total assets ≤ 2.0%	Tangible equity to total assets ≤ 2.0%

Capital Conservation Buffer

- The capital conservation buffer amount does not affect PCA levels.

- Capital conservation buffer deficiencies may restrict or limit dividends, share buy-backs and distributions on Tier 1 capital instruments ("capital actions") and discretionary bonuses based on the amount of "eligible retained earnings."

- "Eligible retained earnings" means the most recent 4 quarters of net income less capital distributions (net of certain tax effects, if the tax effects are not already included in net income.

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Capital Conservation Buffer (cont'd)

- Calculation of the capital conservation buffer:
  - Subtract the Basel III minimum ratios for each of CET1 (4.5%), Tier 1 Risk-Based Capital (6.0%) and Total Risk-Based Capital Ratio (8.0%) from the bank's actual capital under each of these measures.
  - The actual buffer used to determine capital actions and discretionary bonuses is the lowest buffer percentage for all 3 capital ratios.
  - If any of these capital ratios is less than the minimum required, the capital conservation buffer is zero.

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Capital Conservation Buffer (cont'd)

- Fully phased in buffer limits on capital actions and discretionary bonus are subject to regulatory discretion in light of bank risk, CCAR, enforcement actions, etc.

Buffer %	Buffer % Limit
More than 2.50%	None
> 1.875% ≤ 2.50%	60.0%
> 1.250% ≤ 1.875%	40.0
> 0.625% ≤ 1.250%	20.0
≤ 0.625	- 0 -

- The phase-in occurs January 1, 2016 to January 1, 2019.

Selected Standardized Approach Risk Weights

- One-to-Four Family, First Lien Residential Mortgages
  - Significant changes from 2012 Proposal
  - Considerably simplified from 2012 Proposal
  - 50% risk weight when made in accordance with prudent underwriting standards on owner-occupied or rented properties
  - 100% on all others
  - The banking agencies may develop and propose changes in the treatment of residential mortgages taking into account market, regulatory and product developments, and implementation issues

Selected Standardized Approach Risk Weights (cont'd)

- High Volatility CRE
  - Includes ADC loans, except where the LTV is less than regulatory maximums and the borrower has contributed before the loan is made and maintains at all times equity of 15% of the project's "as completed" value
  - Other exceptions include 1-4 family residences, certain community development investments, and the purchase and development of agricultural land
  - 150% risk weight

- Past due assets – 150% risk weight

  - Does not apply to HVCRE and 1-to-4 family residential mortgages

- Structured securities, including private label mortgage securities, trust preferred CDOs and ABS – up to 1,250%

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Selected Standardized Approach Risk Weights (cont'd)

- Substitutions for risk weights
  - Generally, risk weight applicable to collateralized portion of the exposure cannot be less than 20%
  - Collateral (U.S. government securities or cash) – may decrease risk weight from 20% to 0%
  - Guarantees may reduce risk weights to that of an applicable guarantor
- MSAs – 250% risk weight to extent not deducted from capital subject to the 10% / 15% of CET1 maximums
- DTAs – 250% risk weight to the extent not deducted from capital subject to the 10% / 15% of CET1 maximums
- Equity exposures other than FRB, FHLB and CDFIs – 250% to 600% risk weight

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