

Federal Reserve Bank of San Francisco
101 Market Street, San Francisco, California 94105

April 12, 2006

**BANKING SUPERVISION AND REGULATION:
PROPOSED RULEMAKING IMPLEMENTING
BASEL II RISK-BASED CAPITAL
REQUIREMENTS**

To State Member Banks, Bank
Holding Companies, U.S. Branches
and Agencies of Foreign Banks,
and Others Concerned,
in the Twelfth Federal Reserve District

Proposed Rulemaking Implementing Basel II Risk-Based Capital Requirements

The Federal Reserve Board has issued an interagency notice of proposed rulemaking (NPR) that would implement Basel II risk-based capital requirements in the United States for large, internationally active banking organizations. Detailing the agencies' plan for implementing the Basel Committee on Banking Supervision's new capital accord (Basel II), the NPR would replace U.S. rules implementing the Basel Capital Accord of 1988 (Basel I) for banks that meet qualifying criteria.

The proposed rule would require the largest, internationally active banks to enhance the measurement and management of their risks, have rigorous processes for assessing overall capital adequacy in relation to their total risk profile, and to publicly disclose this information.

"Given the increasing complexity of the activities at our largest banks, and the related risks of those activities, I fully support efforts to develop a more appropriately risk-sensitive capital framework for those institutions," said Board Chairman Ben S. Bernanke. "The current Basel I framework has become increasingly inadequate for capturing the risks at large, complex U.S. banking organizations."

The NPR builds on an advance notice of proposed rule making (ANPR) issued by the agencies in August 2003. It includes a number of prudential safeguards including the following:

- Requirement that a bank satisfactorily completes a four-quarter parallel run period, beginning no sooner than January 1, 2008, before operating under the Basel II framework.
- Following a successful parallel run, a bank would have to progress through three transitional periods of at least one year each, during which, there would be temporary floors on potential declines in risk-based capital requirements.
- Finally, a bank would then need approval from its primary federal supervisor to move to each of the transitional floors before moving to full Basel II at the end of the transition period.

"As a central bank and a supervisor of banks and bank and financial holding companies, the Federal Reserve is committed to ensuring that the Basel II framework delivers a strong and risk-sensitive base of capital," said Governor Susan S. Bies. "That is why the proposal contains safeguards to ensure strong capital levels during and after the transition to Basel II, and why we will remain vigilant in monitoring Basel II's impact on an ongoing basis."

The Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS) also are considering the NPR. The Board authorized

the staff to publish the NPR in the *Federal Register* for public comment after the other agencies complete their approval processes. For the OCC and OTS, that includes review by the Office of Management and Budget (OMB).

Additional Information

All circulars and documents are available on the Internet through the Federal Reserve Bank of San Francisco's Internet site, at <http://www.frbsf.org/banking/letters>.

For additional information about the proposed rulemaking for Basel II risk-based capital requirements, please contact our Banking Supervision and Regulation Department at (415) 974-3206.

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Attachment: [Cover Memorandum](#)
[Board Memorandum](#)
[Draft Basel II NPR](#)