SFAS No. 115's mark-to-market requirements by purchasing or retaining whole loans instead of similar loans that had been securitized and guaranteed by government sponsored enterprises or the private market. This approach could harm associations because many loans have greater credit risk than guaranteed, high-quality mortgage-related securities.

Other commenters submitted that the OTS interest-rate risk model and capital component already capture and address associations' interest rate risk exposure. They argued that adoption of SFAS No. 115 for capital purposes was unnecessary, could conflict with the interest-rate risk model and component, and could result in a double hit to capital for interest rate swings.

Commenters opposing the proposal also argued that its adoption would lead to associations' focusing too much attention on the short-term effects of investment decisions instead of long-term economic viability. Commenters also raised the possibility that adoption of the proposal would make an association reluctant to sell securities from its held-to-maturity portfolio for fear of having its entire held-to-maturity portfolio reclassified as available-forsale, thereby limiting an association's flexibility to manage its investments properly.

Several commenters were critical of the market value accounting approach imposed by SFAS 115 because it includes in capital unrealized gains and losses that might never be realized by an association and so could present a misleading picture of an association's current financial condition.

Commenters also submitted that SFAS 115 is inconsistent in its approach because it requires institutions to account for certain assets at fair market value while liabilities are valued at cost.

B. Comments Supporting a SFAS No. 115 Component

The two commenters supporting the OTS proposed rule believed that the OTS's adoption of SFAS No. 115 for regulatory capital purposes was consistent with GAAP and the Agencies' requirements that institutions comply with SFAS No. 115 for regulatory reporting purposes. These commenters reasoned that the proposal would minimize the reporting and systems burden that would otherwise result if the SFAS No. 115 capital component is treated differently in regulatory capital calculations than in GAAP and regulatory reports. Second, these commenters stated that the OTS's adoption of SFAS No. 115 for regulatory capital purposes would be consistent with Congressional intent as manifested

in section 121 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), which provides that Federal banking agency regulatory accounting policy applicable to reports or statements filed with those agencies be no less stringent than GAAP. One commenter contended that including the SFAS No. 115 equity component in regulatory capital would protect associations and the deposit insurance fund by causing associations to control their interest-rate risk exposure. This commenter believed that SFAS No. 115 gives associations the appropriate incentive to hold shorter duration securities and to limit their interest-rate risk exposure to avoid drops in their capital levels.

Finally, one commenter contended that not adopting SFAS No. 115 for regulatory capital purposes would arguably allow institutions temporarily to hide their losses and to defer appropriate supervisory action. This would be inconsistent with prudent asset liability management and ultimately with protecting the SAIF from losses not otherwise included in regulatory capital. Furthermore, failure to include unrealized losses in regulatory capital would give associations, particularly undercapitalized ones, an incentive to speculate on interest rates by holding unhedged long-term securities.

C. Comments Suggesting Alternative Ways of Incorporating a SFAS No. 115 Component

The majority of commenters opposing the proposal supported excluding the SFAS No. 115 equity component from regulatory capital altogether. Several commenters, however, suggested alternative methods of incorporating SFAS 115 into the OTS's regulatory capital regulation. One commenter recommended that, if SFAS No. 115 was going to affect regulatory capital, that it only be included in supplementary capital or in risk-based capital computations. Commenters also argued that, even if the SFAS No. 115 equity component was included in regulatory capital, it should be excluded from computations and determinations relating to PCA, insurance premiums, lending limits, and other differential regulations based on capital levels. Other commenters recommended that the OTS propose a method for balancing the mark-to-market adjustment for available-for-sale securities with offsetting adjustments to associations' deposits, other liabilities, and hedging instruments. Finally, several

commenters recommended that OTS institute a three-quarter lag similar to that used with the interest-rate risk component to reduce the effects of temporary market fluctuations and to give associations time to take action ameliorating the effects of their unrealized losses.

IV. The Final Rule

After considering all the comments received, the OTS, in consultation with the other Agencies, has decided not to adopt its proposal to include the SFAS No. 115 equity component in computing regulatory capital. Savings associations, however, must follow SFAS No. 115 for regulatory reporting purposes, as required by statute. This decision leaves in effect the OTS's current requirement that nontrading debt securities be valued at amortized cost and nontrading marketable equity securities be valued at the lower of fair value or amortized cost for computing regulatory capital.8 This decision is consistent with the recommendation of the Task Force on Supervision of the FFIEC and the policies of the other Agencies.9

Based on the comment letters received, the OTS determined that adoption of the proposal could potentially have an inappropriate impact on associations' regulatory capital and result in an inaccurate picture of their capital positions. For example, fluctuations in interest rates could cause temporary changes in regulatory capital levels, which in turn could trigger more permanent regulatory intervention and inappropriately affect industry profitability. In addition, including the SFAS No. 115 adjustment in capital could potentially distort an association's capital position by giving the same weight to an association's SFAS 115 component as is given to its common stock, paid-in surplus, and retained earnings. Also, changes in the value of institutions' assets from interest rate changes would not be properly balanced by offsetting changes in the value of institutions' liabilities and hedge positions.

The OTS is also concerned that adoption of the proposal would encourage management to place excessive weight on the accounting implications of their decisions, rather than on their long-term economic impacts. Associations could potentially take actions or make investment

⁷ Pub. L. 102-242 (1991).

⁸ See current 12 CFR 567.1(d) and the OTS's November 28, 1994 interim policy statement, which provided that the SFAS No. 115 capital component could no longer be included in regulatory capital.

⁹ See 59 FR 60552 (November 25, 1994) (OCC), 59 FR 63241 (December 8, 1994) (FRB), and 59 FR 66662 (December 28, 1994) (FDIC).