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M E M O R A N D U M

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To Our Clients and Friends

Re: Proposed Basel II Standardized Approach

The Federal Reserve Board and Federal Deposit Insurance Corporation (the “Agencies”) have issued an interagency proposal to provide banks, bank holding companies and savings associations with the option to adopt an alternative risk-based capital framework based on the standardized approach of the Basel II capital accord. The Office of the Comptroller of the Currency and Office of Thrift Supervision are also expected to complete their approval processes in the near future. Public comments on the proposal will be accepted for 90 days after publication in the *Federal Register*.

The standardized approach would be available to institutions other than the large, internationally active banking organizations that are required to comply with the advanced approaches of Basel II, which took effect in April. The proposal would have no effect on how a banking organization calculates its leverage ratio.

The standardized framework would:

- Add more risk-weight categories to the existing rules
- Expand the use of external ratings to a broader range of exposures
- Expand the recognition of credit risk mitigants, such as collateral and guarantees
- Enhance risk-sensitivity by using loan-to-value ratios to risk weight most residential mortgages
- Increase the capital requirements on certain off-balance sheet exposures, including liquidity lines to asset-backed commercial paper exposures
- Require a capital charge for operational risk using the Basic Indicator Approach under Basel II

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- Emphasize the importance of a bank's risk assessment of its overall risk profile and capital adequacy
- Require comprehensive disclosures to complement the minimum capital requirements and supervisory process through market discipline

The Agencies also seek comment on whether the standardized approach should be made available to banking organizations subject to Basel II.

A copy of the proposed rule can be found on our website at http://www.schwartzandballen.com/whats_new.html.

If you have any questions, please call Gilbert Schwartz, Robert Ballen, Tom Fox or Heidi Wicker at (202) 776-0700.