STATE STREET.

Stefan M. Gavell
Executive Vice President and Head of
Regulatory and Industry Affairs

State Street Corporation
1 Lincoln Street
P.O. Box 5225
Boston, MA 02206-5225

Telephone: 617-664-8673
Facsimile: 617-664-4270
smgavell@statestreet.com

October 30, 2008

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 1-5
Washington, DC 20219
E-mail: regs.comments@occ.treas.gov
Docket Number OCC-2008-0014

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
E-mail: comments@FDIC.gov
RIN 3064-AD32

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
E-mail: regs.comments@federalreserve.gov
Docket Number R-1329

Regulation Comments, Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
E-mail: reg.comments@ots.treas.gov
Attention: OTS-2008-0010

Capital Adequacy Guidelines: Deduction of Goodwill Net of Associated Deferred Tax Liability

Dear Sir or Madam,

Thank you for providing State Street Corporation ("State Street") the opportunity to comment on the joint notice of proposed rulemaking published by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision (collectively, "the Agencies") on September 30, 2008 to reduce the amount of goodwill that a banking organization must deduct from tier 1 capital by the amount of any deferred tax liability associated with that goodwill.

State Street is the world's leading provider of financial services to institutional investors, including investment servicing, investment management and investment research and trading. With $14.0 trillion in assets under custody and $1.7 trillion in assets under management at September 30, 2008, State Street operates in 26 countries and more than 100 geographic markets worldwide.

Goodwill

State Street strongly supports allowing banking organizations to deduct goodwill from capital net of associated deferred tax liabilities. As the Agencies note, the relief provided by the proposal has been requested by banking organizations for a number of years. We particularly support the Agencies' clear articulation that deductions from tier 1 capital should "reflect a banking organization's maximum exposure to loss if the goodwill becomes impaired or derecognized under GAAP."

We believe the proposal to allow banking organizations to deduct goodwill from tier 1 capital net of associated deferred tax liabilities is an important change, and we urge the Agencies to work expeditiously to issue a final rule, hopefully in time to allow the new treatment to be adopted in the December 2008 Call Report.

Other Intangible Assets

As the Agencies note in their commentary on the proposed rule, existing practice allows banking organizations to deduct certain identifiable intangibles acquired in nontaxable business combinations net of associated deferred tax liabilities. We believe this treatment is appropriate, and consistent with the Agencies' goal of excluding intangibles from tier 1 capital only to the maximum extent impairment of these intangibles could lead to losses to the banking organization.

While the Agencies' current practice of limiting such netting to intangibles acquired in nontaxable business combinations appropriately addressed the issues raised in 1992 by FAS 109 changes, we believe there is strong justification for extending this treatment to all intangible assets required to be deducted from tier 1 capital, regardless if acquired through a taxable or nontaxable business combination. In both taxable and nontaxable acquisitions, such intangible assets give rise to book/tax differences which lead to associated deferred tax liabilities. These differences may be for an indefinite period, as with goodwill or indefinite-lived assets such as trademarks, or short-term timing differences, as might arise with a customer list or other identifiable intangible. In each of these cases, the potential maximum exposure to loss for the banking organization should give account to the tax consequences of loss; the tax effects are best expressed by allowing banking institutions to deduct from capital net of deferred tax liabilities in a manner similar to the treatment provided under current law for nontaxable combinations, and under the Agencies' pending proposal for goodwill.

We suggest the Agencies amend the proposed rule to permit all intangibles disallowed as tier 1 capital to be deducted from capital net of any associated deferred tax liabilities.

Calculation of "maximum exposure to loss"

The Agencies propose to revise their capital rules to permit a banking organization to reduce the amount of goodwill it must deduct from tier 1 capital by the amount of any deferred tax liability associated with that goodwill. The proposed change is intended to permit the organization to reduce its regulatory capital deduction for goodwill to the maximum exposure to loss that could occur were the goodwill to become completely impaired.

As noted above, we support the Agencies' proposal, and recommend expanding such treatment to all intangibles disallowed as tier 1 capital. We suggest, however, that the Agencies permit an alternative netting process which we believe more fully achieves the Agencies' goal.

Consider the example provided by the Agencies:

> *For example, assume that goodwill in the amount of $9,000 arises from a taxable business combination. For income tax purposes, this goodwill is amortized over 15 years at a rate of $600 per year ($9,000/15 years). However, the banking organization cannot recognize the $600 annual tax deduction for goodwill amortization in current income for financial reporting purposes. Assuming an income tax rate of 30 percent, each year the banking organization would have an income tax reduction of $180 ($600 X 30%) and would recognize this amount as a deferred tax liability. Under GAAP, at the end of the first year, the banking organization would report a deferred tax liability of $180. At the end of the 15-year tax amortization period, it would report a cumulative deferred tax liability of $2,700 ($180 X 15 years).*
>
> *Under the Agencies' existing regulatory capital rules, the full carrying amount of goodwill ($9,000) is deducted from tier 1 capital. However, since the amortization of this asset for income tax purposes reduces income taxes by $2,700 over the 15-year period, the maximum amount of reduction in tier 1 capital that the banking organization could experience in the event of total impairment of the goodwill at the end of the 15-year period is $6,300 ($9,000 minus $2,700), not $9,000. Under this proposed rule, the total deduction from tier 1 capital at the end of the first year would be $8,820 ($9,000 minus $180) and, at the end of the fifteenth year, the deduction from tier 1 capital would be $6,300.*

The Agencies correctly note that the deferred tax liability will increase over time, as the goodwill is amortized for tax (typically, ratably over 15 years) but not for GAAP. The Agencies' proposal would allow the banking organization to reduce its deduction for goodwill by the cumulative amount of deferred tax liability at the report date. While we agree the Agencies' proposal is an improvement over current rules, which prohibit any netting of goodwill acquired in a taxable transaction by associated deferred tax liabilities, we believe this approach still overstates the maximum exposure to loss that could result from complete impairment of the goodwill.

The Agencies' proposal does not reflect the full tax effect realized by a complete impairment of the goodwill. Using the Agencies' example, on the date the goodwill becomes completely impaired, the organization would charge off the entire goodwill amount ($9,000) against earnings and record a reduction to tax expense of $2,700. Depending on the timing, some portion of this reduction in tax expense would reflect the deductions already taken for tax, but not book, purposes. The balance of the reduction in tax expense would reflect the remaining tax amortization of the hypothetically impaired goodwill, in the form of either an immediate tax deduction or a deferred tax asset.

In either case, the potential maximum exposure to loss that could occur as a result of impairment of goodwill in year one would be only $6,300 ($9,000 - $2,700), not the $8,820 resulting from the methodology offered in the Agencies' proposal. While the deferred tax liability referred to in the Agencies' example increases throughout the tax amortization period, the hypothetical reduction in tax expense resulting from goodwill impairment is constant – in this example, $2,700 in each year.

If circumstances surrounding the hypothetical impairment of goodwill gave rise to a creation of a deferred tax asset, rather than an immediate deduction, we would expect the resulting deferred tax asset to be subject to the Agencies' rules related to deferred tax assets. In such a case, should a banking organization choose to avail itself of the methodology we suggest here, and a

hypothetical deferred tax asset is created, a parallel exercise would need to be conducted to determine and reflect any impact on tier 1 capital due to the Agencies' normal tier 1 deferred tax asset limitations.

In conclusion, we support the Agencies' proposal to allow goodwill be deducted from capital net of associated tax liability, and suggest that this treatment be extended to all intangible assets required to be deducted from tier 1 capital. In addition, we recommend the Agencies adopt a netting procedure that fully reflects the tax effect of impairment of these intangibles.

Sincerely,

Stefan M. Gavell