

# What's Working

## AN OVERVIEW OF THE PROPOSED COMMUNITY BANK LEVERAGE RATIO REGULATIONS

On November 21, 2018, the federal banking regulatory agencies (collectively, "the Agencies") released their proposal for the implementation of the community bank leverage ratio ("CBLR") that was mandated in the Economic Growth, Regulatory Relief, and Consumer Protection Act that was signed into law by President Trump on May 24, 2018. Under the proposed regulations, eligible community banking organizations would be able to elect the CBLR framework if their CBLR is greater than 9%, meaning that if they so choose, they would not be required to calculate existing risk-based and leverage capital requirements. Furthermore, they would be deemed to be "well-capitalized" if their CBLR exceeds 9%. The proposal's highlights are shown below.

- Non-advanced approaches banking organizations (bank or holding company) with assets less than \$10 billion that meet these additional requirements are eligible to use the CBLR framework:
  - Off-balance sheet exposures less than 25% of total consolidated assets, excluding derivatives that are not credit derivatives, such as interest rate swaps and foreign exchange swaps
  - Trading assets equal to, or less than, 5% of total consolidated assets
  - MSAs equal to, or less than, 25% of CBLR tangible equity
  - Temporary difference deferred tax assets equal to, or less than, 25% of CBLR tangible equity
- CBLR tangible equity equals a banking organization's total equity capital less:
  - Minority interests
  - AOCI
  - All intangible assets other than MSAs
  - Temporary difference deferred tax assets

Disclosures are contained on the last page of this report.

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- The Agencies appear to be considering allowing CBLR banks to use the proposed optional three-year transition arrangement for any day-one adverse regulatory capital effects of CECL adoption.
- Of particular interest was the inclusion of **cumulative**, perpetual preferred stock as an eligible tangible capital element for purposes of the CBLR. Cumulative perpetual preferred is excluded as a Tier 1 capital element under standard capital ratios.
- Average total consolidated assets would be the same as under the current Tier 1 leverage ratio calculation.
- The proposed Prompt Corrective Action levels are as follows:
  - CBLR > 9% — well capitalized
  - CLBR >= 7.5% — adequately capitalized
  - CLBR < 7.5% and >= 6.0% — undercapitalized
  - CLBR < 6% — significantly undercapitalized
- There would be a two-consecutive-quarter grace period for banks failing to meet the CBLR qualifying criteria before they would be required to use the standard capital ratios.
- Banking organizations would be allowed to switch between the CBLR and standard capital ratios but the Agencies believe such switches should be rare and driven by significant changes in business activities.

The federal banking regulatory agencies proposed simplifying changes for community banks through the use of the community bank leverage ratio. This proposal appears to reduce the regulatory filing burden on smaller banks. The final rule, the amount of actual relief provided, and the adoption rate by banking organizations remains to be seen. The Agencies suggest that 83% of banks and 56% of holding companies will be able to comply with the 9% CBLR proposal. The proposal is subject to a 60-day comment period that ends in January 2019.

View the proposal: <https://www.fdic.gov/news/news/press/2018/pr18088.html>

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