

August 6, 2020

MEMORANDUM TO: Board of Directors

FROM: Doreen R. Eberley, Director

SUBJECT: Regulatory Capital Rule: Temporary Changes to and Transition for the Community Bank Leverage Ratio Framework and Transition

SUMMARY: Staff is presenting for approval of the Federal Deposit Insurance Corporation (FDIC) Board of Directors (FDIC Board) a request to adopt and publish the attached interagency final rule (final rule) to finalize, with no changes, the revisions to the community bank leverage ratio framework made under two interim final rules issued by the FDIC, the Office of the Comptroller of the Currency (OCC), and the Board of Governors of the Federal Reserve System (FRB) (together, the agencies) in the Federal Register on April 23, 2020. Under the final rule, the community bank leverage ratio will remain 8 percent through calendar year 2020, will be 8.5 percent through calendar year 2021, and will be 9 percent thereafter. The final rule also maintains a two-quarter grace period for a qualifying community banking organization whose leverage ratio falls no more than 1 percentage point below the applicable community bank leverage ratio requirement.

Recommendation: Staff requests that the FDIC Board approve the final rule and authorize its publication in the *Federal Register* with an effective date of October 1, 2020.

Concur:

Nicholas J. Podsiadly
General Counsel

Discussion:

I. Background on the Community Bank Leverage Ratio Framework

The community bank leverage ratio framework provides a simple measure of capital adequacy for community banking organizations that meet certain qualifying criteria. The community bank leverage ratio framework implements section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA), which requires the agencies to establish a community bank leverage ratio of not less than 8 percent and not more than 10 percent for a qualifying community banking organization.¹ Under section 201(c) of EGRRCPA, a qualifying community banking organization whose leverage ratio exceeds the community bank leverage ratio, as established by the agencies, shall be considered to have met the generally applicable risk-based and leverage capital requirements in the capital rule (generally applicable rule), any other applicable capital or leverage requirements, and, if applicable, the “well capitalized” capital ratio requirements for purposes of section 38 of the Federal Deposit Insurance Act. Section 201(b) of EGRRCPA also requires the agencies to establish procedures for the treatment of a qualifying community banking organization whose

¹ Pub. L. 115-174, 132 Stat. 1296, 1306–07 (2018) (codified at 12 U.S.C. 5371 note). The authorizing statutes use the term “qualifying community bank,” whereas the regulation implementing the statutes uses the term “qualifying community banking organization.” The terms generally have the same meaning. Section 201(a)(3) of EGRRCPA provides that a qualifying community bank is a depository institution or depository institution holding company with total consolidated assets of less than \$10 billion that satisfies such other factors, based on the banking organization’s risk profile, that the agencies determine are appropriate. This determination shall be based on consideration of off-balance sheet exposures, trading assets and liabilities, total notional derivatives exposures, and any such factors that the agencies determine appropriate.

leverage ratio falls below the community bank leverage ratio requirement as established by the agencies.

In November 2019, the agencies issued a final rule establishing the community bank leverage ratio framework, which became effective January 1, 2020 (2019 final rule).² Under the 2019 final rule, the agencies established a community bank leverage ratio of 9 percent using the existing leverage ratio calculation. A qualifying community banking organization that maintains a leverage ratio of greater than 9 percent and elects to use the community bank leverage ratio framework will be considered to have satisfied the generally applicable rule, any other applicable capital or leverage requirements, and, if applicable, the capital ratio requirements to be considered well capitalized.³

Under the 2019 final rule, a qualifying community banking organization is any depository institution or depository institution holding company that has less than \$10 billion in total consolidated assets, off-balance sheet exposures (excluding derivatives other than sold credit derivatives and unconditionally cancelable commitments) of 25 percent or less of total consolidated assets, and trading assets and liabilities of 5 percent or less of total consolidated assets. The banking organization also cannot be an advanced approaches banking organization.⁴

² 84 FR 61776 (November 13, 2019).

³ Under existing prompt corrective action requirements applicable to insured depository institutions, to be considered “well capitalized” an insured depository institution must demonstrate that it is not subject to any written agreement, order, capital directive, or as applicable, prompt corrective action directive, to meet and maintain a specific capital level for any capital measure. See 12 CFR 6.4(b)(1)(iv) (OCC); 12 CFR 208.43(b)(1)(v) (FRB); 12 CFR 324.403(b)(1)(v) (FDIC). The same legal requirements continue to apply under the community bank leverage ratio framework.

⁴ A banking organization is an advanced approaches banking organization if it (1) is a global systemically important bank holding company, (2) is a Category II banking organization, (3) has

In addition, the 2019 final rule established a two-quarter grace period during which a qualifying community banking organization that temporarily fails to meet any of the qualifying criteria, including the leverage ratio requirement, generally would still be considered well capitalized so long as the banking organization maintains a leverage ratio of greater than 8 percent during that grace period. A banking organization that either fails to meet all the qualifying criteria within the grace period or fails to maintain a leverage ratio of greater than 8 percent is required to comply with the generally applicable rule and file the appropriate regulatory reports.

II. Interim Final Rules

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) became law.⁵ Section 4012 of the CARES Act directs the agencies to issue an interim final rule providing that, for purposes of section 201 of EGRRCPA, the community bank leverage ratio shall be 8 percent, and a qualifying community banking organization whose leverage ratio falls below the community bank leverage ratio requirement established under the CARES Act shall have a reasonable grace period to satisfy that requirement. Section 4012 of the CARES Act specifies that the interim final rule is effective during the period beginning on the date on which the agencies issue the interim final rule and ending on the sooner of the termination date of the national emergency concerning the coronavirus disease (COVID-19) outbreak declared by the

elected to be an advanced approaches banking organization, (4) is a subsidiary of a company that is an advanced approaches banking organization, or (5) has a subsidiary depository institution that is an advanced approaches banking organization. See 12 CFR 3.100 (OCC); 12 CFR 217.100 (FRB); 12 CFR 324.100 (FDIC).

⁵ Pub. L. 116-136, 134 Stat. 281.

President on March 13, 2020, under the National Emergencies Act, or December 31, 2020 (termination date).

Accordingly, the agencies issued an interim final rule that implements a temporary 8-percent community bank leverage ratio requirement, as mandated under section 4012 of the CARES Act (statutory interim final rule).⁶ In addition, under the statutory interim final rule, a community banking organization that temporarily fails to meet any of the qualifying criteria, including the 8-percent community bank leverage ratio requirement, generally will still be considered well capitalized provided that the banking organization maintains a leverage ratio equal to 7 percent or greater. A banking organization that fails to meet the qualifying criteria after the end of the grace period or reports a leverage ratio of less than 7 percent must comply with the generally applicable rule and file the appropriate regulatory reports.

Since the statutory interim final rule could cease to be effective at any time before December 31, 2020, the agencies issued a separate interim final rule pursuant to section 201(b) of EGRRCPA that provides a graduated transition from the temporary 8-percent community bank leverage ratio requirement to the 9-percent community bank leverage ratio requirement as established under the 2019 final rule (transition interim final rule).⁷ Specifically, the transition interim final rule provides that, once the statutory interim final rule ceases to apply, the community bank leverage ratio will be 8 percent in the second quarter through fourth quarter of calendar year 2020, 8.5 percent in calendar year 2021, and 9 percent thereafter.⁸ The transition

⁶ 85 FR 22924 (April 23, 2020).

⁷ 85 FR 22930 (April 23, 2020).

⁸ Section 201 of EGRRCPA requires a qualifying community banking organization to exceed the community bank leverage ratio established by the agencies in order to be considered to have met the generally applicable rule, any other applicable capital or leverage requirements, and, if

interim final rule also modifies the two-quarter grace period for a qualifying community banking organization to account for the graduated increase in the community bank leverage ratio requirement. The interim final rules do not make any changes to the other qualifying criteria in the community bank leverage ratio framework.

Consistent with section 201(c) of EGRRCPA, under the transition interim final rule, a qualifying community banking organization that temporarily fails to meet any of the qualifying criteria, including the applicable community bank leverage ratio requirement, generally would still be deemed well capitalized during a two-quarter grace period so long as the banking organization maintains a leverage ratio of the following: greater than 7 percent in the second quarter through fourth quarter of calendar year 2020, greater than 7.5 percent in calendar year 2021, and greater than 8 percent thereafter.⁹ A banking organization that fails to meet the qualifying criteria by the end of the grace period or reports a leverage ratio of equal to or less than 7 percent in the second through fourth quarters of calendar year 2020, equal to or less than 7.5 percent in calendar year 2021, or equal to or less than 8 percent thereafter, would be required to comply immediately with the generally applicable rule and file the appropriate regulatory reports.

applicable, the “well capitalized” capital ratio requirements, whereas section 4012 of the CARES Act requires that a qualifying community banking organization meet or exceed an 8 percent community bank leverage ratio to be considered the same.

⁹ While the statutory interim final rule is in effect, a qualifying community banking organization that temporarily fails to meet any of the qualifying criteria, including the applicable community bank leverage ratio requirement, generally would still be deemed well capitalized so long as the banking organization maintains a leverage ratio of 7 percent or greater during a two-quarter grace period. Similarly, while the statutory interim final rule is in effect, a banking organization that fails to meet the qualifying criteria by the end of the grace period or reports a leverage ratio of less than 7 percent must comply with the generally applicable rule and file the appropriate regulatory reports.

III. Public Comment and Final Rule

The agencies received one public comment that addressed the substance of the interim final rules. The commenter urged the agencies to revert to a 9 percent community bank leverage ratio by January 1, 2022, which is consistent with the transition interim final rule. Accordingly, the final rule would finalize, without change, the interim final rules.

Conclusion:

Staff requests that the FDIC Board approve the final rule and authorize its publication in the *Federal Register* with an effective date of October 1, 2020.

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