

Statement by FDIC Chairman Jelena McWilliams on the Final Rule: Capital Simplification for Qualifying Community Banking Organizations

September 17, 2019

One of the great strengths of the U.S. financial system is its diversity of institutions – we have thousands of banks of varying sizes and business models. The overwhelming majority of U.S. banks are small and less complex relative to their larger peers. It is important that the regulatory framework applicable to our nation’s community banks be commensurate with this reality. At the same time, it is also important that community banks remain well-capitalized so that they can continue to serve their communities.

In May of 2018, Congress passed the Economic Growth, Regulatory Relief and Consumer Protection Act (the “Act”), which requires the banking agencies to develop a simple leverage ratio for qualifying community banks. The Act recognizes that the existing risk-based capital framework is very complex, and that there should be a simpler way for community banks to demonstrate their capital adequacy. For this reason, I am pleased to support the final rule before us today.

The agencies received a number of constructive comments on the proposal approved by the Board last November. In response to comments, the banking agencies made several changes to the proposal while keeping other parts of the proposal intact.

Many commenters recommended that agencies lower the community bank leverage ratio (CBLR) to 8 percent rather than the proposed 9 percent. At 9 percent, approximately 85 percent of insured institutions currently would qualify for the CBLR. At the same time, a 9 percent threshold ensures that banks that adopt the CBLR maintain strong levels of capital. The agencies estimated that a threshold of 8 percent could allow a material number of community banks to operate with less capital than is required today. The final rule maintains the 9 percent threshold.

Among the changes made to the proposal in response to comments, two I will briefly highlight are the definition of tangible equity and the so-called “Prompt Corrective Action (PCA) proxies.”

First, the final rule adopts the existing definition of tier 1 in the numerator of the community bank leverage ratio. Using the existing tier 1 definition provides more consistency with the existing framework, and it was clear that the overwhelming majority of commenters preferred this approach rather than the proposed simpler definition of tangible equity. Second, the so-called “PCA proxies” that were included in the proposed rule are not adopted in the final rule. Instead, the final rule allows for a grace period during which a community bank that has fallen below the 9 percent CBLR can work toward the 9 percent requirement before being classified as less than well-capitalized under the PCA framework, or can undertake necessary steps to return to the risk-based system.

When Basel III was introduced in the United States in 2013, the stated goal was to improve the quality and quantity of capital in the banking system. Basel III made the risk-based framework significantly more complex, and unduly so for community banks. The CBLR is an important step in the simplification and tailoring of our regulatory framework.

The final rule is responsive to many comments received and supports the goals of reducing regulatory burden for as many community banks as possible while also ensuring that community banks continue to be well-capitalized. Additionally, this framework will allow community banks to significantly reduce the regulatory reporting associated with capital adequacy on the Call Report.

I would like to conclude by thanking the staff of the Office of the Comptroller of the Currency and the Federal Reserve who worked with our staff on this final rule. In particular, I would like to thank the staff of the FDIC for all of their hard work.