

Capital Simplification

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Issue Update

Many banks today maintain capital levels far in excess of any amounts that would be required by the Basel III risk-based capital rules. For those banks, the risk-based capital rules yield no additional supervisory or safety and soundness benefits.

Section 201 of the recently enacted Economic Growth, Regulatory Relief, and Consumer Protection Act requires all three banking regulators to issue a rule creating a “Community Bank Leverage Ratio” and setting it between 8% and 10%. If a community bank is above that ratio, they will be deemed in compliance with risk-based capital requirements, such as Basel III. The fundamental idea is that it is superfluous for a bank with high levels of capital to go through the complex risk-based calculations if the results do nothing more than confirm that the bank has sufficient capital.

On November 20, 2018, the banking agencies issued a proposal that would treat “qualifying” banks as “well capitalized” if they hold a Community Bank Leverage Ratio of greater than 9%. As proposed, qualifying institutions would be limited to banks with less than \$10 billion in assets that meet various other criteria.

Why it Matters To Your Community

The Basel III risk-based capital standards are complex and burdensome. Section 201 will reduce regulatory burden at qualifying institutions by creating an exception to the risk-based capital standards. Moreover, Section 201 could shield qualifying institutions from future changes to the risk-based capital standards. As a result, qualifying banks will be able to dedicate fewer resources towards compliance and more resources to meeting customer needs.

Recommended Action Items

- Regulators should recognize that an 8% threshold is appropriate. Data shows that banks with 8% capital clearly meet—in fact exceed—the various risk-based capital requirements. In effect this proves the premise on which the provision in law was based and shows that an 8% threshold meets the purpose of the law. Any exceptions can be dealt with through the supervisory process.
- The Community Bank Leverage Ratio must remain optional. The Community Bank Leverage Ratio must remain optional and not be converted into a new—*higher*—minimum capital standard for community banks.
- Regulators should not limit relief to “qualifying” banks. The proposal limits the institutions that qualify for the Community Bank Leverage Ratio election through various criteria including asset size, size of off-balance sheet exposures, and mortgage servicing assets concentrations. These limits risk adding unnecessary complexity to proposal.