FDIC unveils long-awaited community bank leverage ratio

By **Rachel Witkowski**
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WASHINGTON — The Federal Deposit Insurance Corp. on Tuesday voted to release a proposal that is designed to provide a simpler capital regime for small banks, a long-anticipated product of the regulatory relief law enacted earlier this year.

The plan would create a community bank leverage ratio for institutions with less than $10 billion of assets which smaller banks could comply with in lieu of more complicated Basel risk-based capital standards. Under the proposal, the ratio was set at 9% of tangible equity to total assets, striking a middle ground from the 8% and 10% that regulators were considering.

The FDIC estimated that more than 80% of the country's 5,400 community banks could qualify for the simplified leverage ratio.

"This was a key priority in designing the proposal — to ensure that the simple ratio would be available broadly," said FDIC Chairman Jelena McWilliams in remarks Friday at a banking conference prior to the proposal's release.

"The proposal recognizes that, while strong liquidity buffers are critical, the liquidity standards can be better tailored among institutions," said FDIC Chairman Jelena McWilliams, speaking of a proposal to change big bank capital requirements.
Bloomberg News

But the plan immediately drew criticism from some bank groups, which said the 9% threshold is too high.

"ICBA is disappointed that regulators have proposed capital standards that are higher than necessary for main street community banks," said Rebeca Romero Rainey, president and CEO of the Independent Community Bankers of America, in a press release.

Rob Nichols, the head of the American Bankers Association, agreed.

"Unfortunately, the 9% leverage ratio proposed by regulators will still leave too many well-capitalized community banks forced to follow capital rules always intended for more complex institutions," he said in a press release.

In a briefing with reporters after the meeting, McWilliams said the FDIC decided to set the ratio at 9% as a "compromise" because an 8% threshold would have more requirements to qualify and the max 10%.

“Here is the bottom line: you could potentially set it at 8%, 9% or 10% but each of those would have caveats where we feel the community banks would have to be,” McWilliams said. “So it seemed to be the right approach to give us some flexibility moving forward. Most of the community banks are well above that.”

The FDIC board voted unanimously to release the community bank proposal without discussion. But that move took place against the backdrop of a more controversial plan that would reduce capital and liquidity requirements for some big banks. That proposal, which had already been released by the Federal Reserve Board, would establish four categories for banks with more than $100 billion of assets, with the biggest institutions facing the strictest requirements.

Regulators largely support the changes, including McWilliams who said Tuesday that the proposal would ease unnecessary compliance burdens for the less complex big banks. But former FDIC Chairman Martin Gruenberg, who was the only opposing FDIC board vote against the big-bank plan, argued it undermines heightened standards put in place to hedge against another financial crisis.

“The current requirements are tailored appropriately to the size, complexity and risk profile of the institutions to which they apply,” Gruenberg said. “They provide a crucial prudential safeguard in the event of a rapid liquidity failure by one or more of these large institutions, they have not impeded the strong performance by these institutions since the requirements were adopted, and they have not yet even been tested through a full economic cycle. I see no reason to weaken these requirements at this time.”

Fed Gov. Lael Brainard also voted against the big-bank proposal, during an Oct. 31 Fed meeting.

But McWilliams said Tuesday that the proposal does not mean regulators are loosening standards for the riskiest banks.

“The proposal recognizes that, while strong liquidity buffers are critical, the liquidity standards can be better tailored among institutions,” she said. “Additionally, all firms subject to the rule would still be subject to — and would still need to hold sufficient highly liquid assets to satisfy — liquidity stress-testing and liquidity risk management requirements at the holding company level."

Rachel Witkowski