

Community Bank Leverage Ratio Framework

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Introduction

- On November 13, 2019, the federal banking agencies issued a final rule, which provides for a simple measure of capital adequacy for qualifying community banking organizations, consistent with Section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act.
- During today's webinar, staff from the Board of Governors (Board) will provide an overview of the final rule and answer questions.

Key Aspects of the Final Rule

- The Community Bank Leverage Ratio (CBLR) framework provides an *optional* simple leverage capital measure, which is generally calculated the same as the generally applicable capital rule's leverage ratio.
- A banking organization (depository institution or depository institution holding company) that has less than \$10 billion in total consolidated assets can elect to opt into the framework if its leverage ratio is greater than 9 percent and the banking organization meets the framework's qualifying criteria.
- If a CBLR banking organization fails to satisfy one of the qualifying criteria but has a leverage ratio of greater than 8 percent, the banking organization can continue to apply the CBLR framework and be considered "well capitalized" for a grace period of up to two quarters.

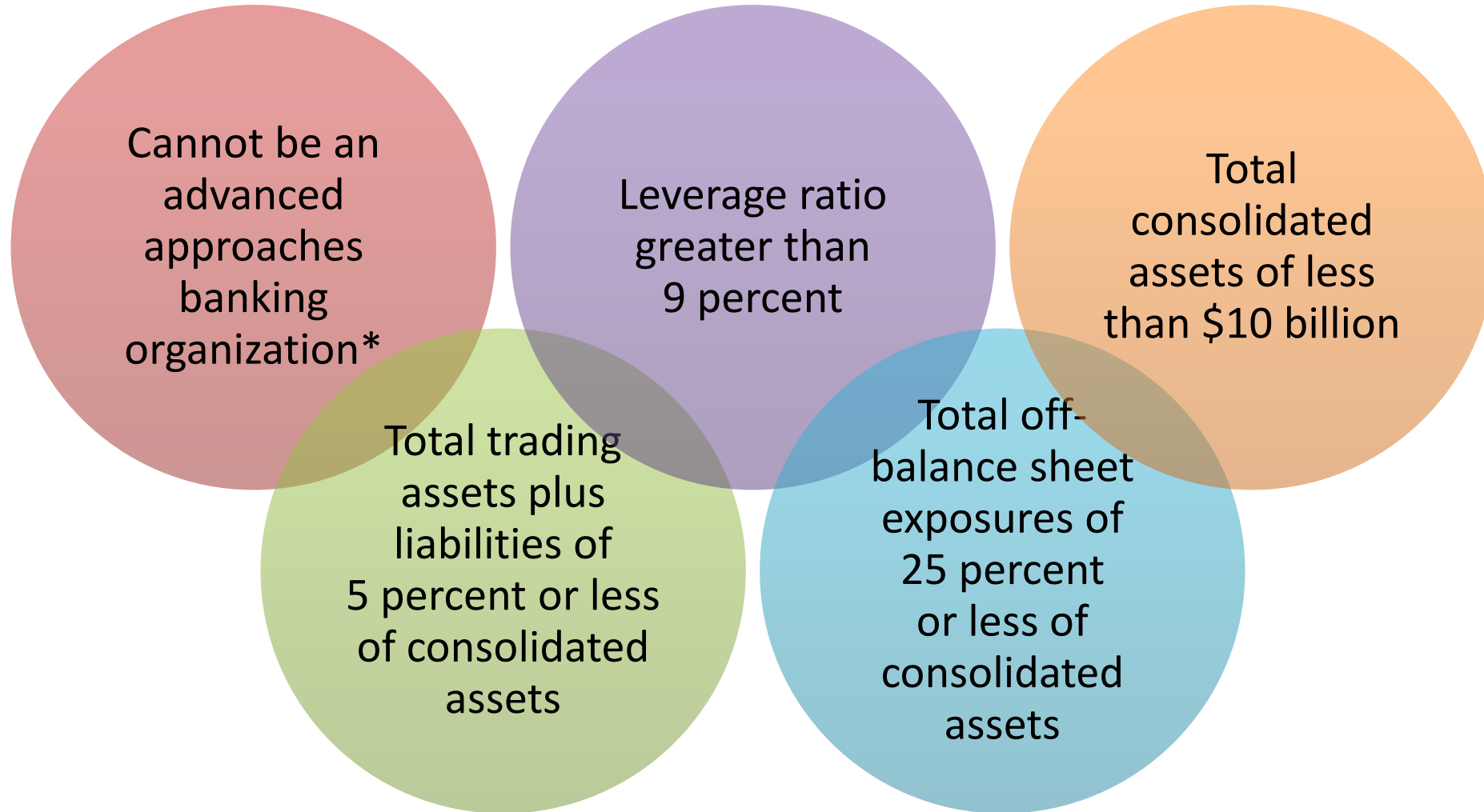
Key Aspects of the Final Rule (continued)

- If all qualifying criteria are met, the banking organization will be considered to have met the “well capitalized” ratio requirements under the Prompt Corrective Action (PCA) framework and the generally applicable capital rule’s requirements.
- Banking organizations electing to use the CBLR framework will not be required to calculate risk-based capital ratios, including complying with High Volatility Commercial Real Estate requirements or applying heightened risk weights to mortgage servicing assets (MSAs), deferred tax assets (DTAs), or investments in unconsolidated financial institutions.
- Reporting requirements will be simplified for banking organizations using the CBLR framework.

Key Changes from Proposed Rule

- Using tier 1 capital as the CBLR numerator:
 - The proposal would have introduced a definition of tangible equity for the numerator of the CBLR.
 - The final rule uses tier 1 capital as the numerator for the CBLR.
 - Public commenters favored this approach, as it enhances the ability of banks to opt in and out of the framework, is already calculated by banking organizations, increases comparability of ratios across firms, and is significantly simpler to calculate after the changes from the Capital Simplifications Final Rule.
- Allowing for the use of a two-quarter transition period instead of using “proxy” PCA thresholds:
 - The proposal would have implemented proxy PCA thresholds for firms that opt into the CBLR framework such that the framework would be self-contained.
 - The final rule provides a firm a two-quarter grace period if the firm’s CBLR falls to between 8 percent and 9 percent.

Eligibility Requirements for the CBLR



*Including a subsidiary of an advanced approaches banking organization

Qualifying Criteria: Off-balance Sheet Exposures

Total Off-balance Sheet Exposures of 25 Percent or Less

- Calculated as the sum of the following items, consistent with the off-balance sheet items that attract a capital charge under the generally applicable rule, as a percentage of total consolidated assets:
 - The unused portions of commitments (except for unconditionally cancellable commitments)
 - Self-liquidating, trade-related contingent items that arise from the movement of goods
 - Transaction-related contingent items, including performance bonds, bid bonds, warranties, and performance standby letters of credit
 - Sold credit protection through:
 - Guarantees
 - Credit derivatives
 - Credit-enhancing representations and warranties
 - Securities lent and borrowed, calculated in accordance with the reporting instructions to the Call Report or to the FR Y-9C, as applicable
 - Off-balance sheet securitization exposures
 - Financial standby letters of credit
 - Forward agreements that are not derivative contracts

Qualifying Criteria: Trading Assets Plus Trading Liabilities

Trading Assets Plus Trading Liabilities of 5 Percent or Less

- Total trading assets plus trading liabilities, calculated in accordance with the reporting instructions to the Call Report or form FR Y-9C, as applicable,
of 5 percent or less of the banking organization's total consolidated assets,
each as of the end of the most recent calendar quarter

Calculation of the CBLR

CBLR

=

Tier 1 capital (includes changes related to simplifications final rule and CECL*)
Average total consolidated assets as of the current quarter**
and less deductions from tier 1 capital

- The CBLR is generally calculated in the same manner as the leverage ratio currently calculated by banks.
- The CBLR framework does not have a total capital requirement.
- Therefore, an electing banking organization is not required to calculate tier 2 capital or make any tier 2 capital deductions.
- The generally applicable capital rule requires deductions from tier 2 capital related to investments in capital instruments of unconsolidated financial institutions when such investments exceed certain limits; such deductions can affect the calculation of tier 1 capital.

*Current expected credit loss

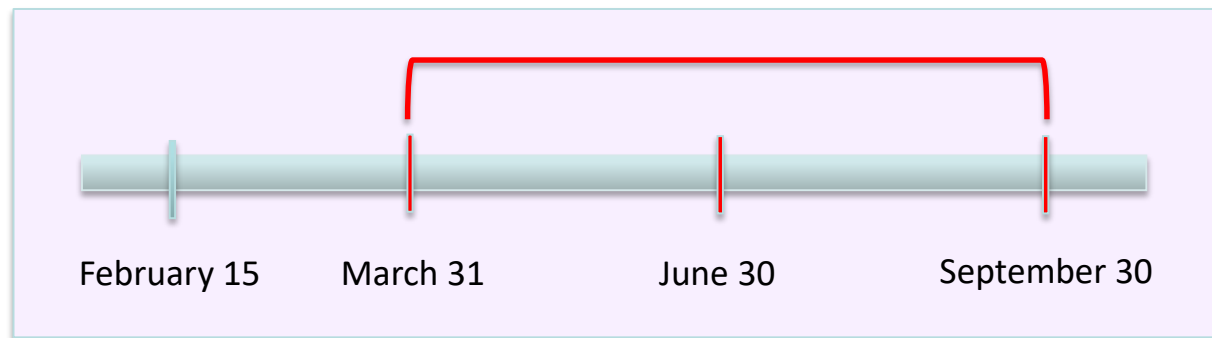
**Reported on FR Y-9C, Schedule HC-K, line item 5

Optionality of the CBLR Framework

- A banking organization can opt into the CBLR framework at any time by completing the associated reporting line items that are required on its Call Report and/or form FR Y-9C, as applicable. The banking organization becomes subject to the CBLR framework when it makes an election.
- CBLR banking organizations may opt out of the framework and become subject to the generally applicable capital rule by completing those reporting requirements on its Call Report and/or form FR Y-9C, as applicable.
- A banking organization can opt out of the CBLR framework between reporting periods by providing its risk-based capital ratios under the generally applicable capital rule to its appropriate regulators at that time.
- After a banking organization opts out of the CBLR framework, it can subsequently opt back in if it meets the qualifying criteria.

Two-quarter Grace Period

- A CBLR firm with a leverage ratio greater than 8 percent that fails to satisfy at least one of the qualifying criteria can continue to apply the CBLR framework for up to two reporting quarters.
- During that two-quarter grace period, the firm would be considered to have met the “well capitalized” capital ratio requirements.
- A banking organization with a leverage ratio of 8 percent or less must comply with the risk-based requirements under the generally applicable capital rule.
 - For example, if a firm fails to meet a qualifying criterion intra-reporting quarter (e.g., on February 15), it has the following two reporting quarters (e.g., until September 30) to return to full compliance with the qualifying criteria.



Capital and Leverage Requirements Fulfilled by Electing to Use the CBLR Framework

- Qualifying banking organizations that elect to use the CBLR framework and maintain a leverage ratio of greater than 9 percent will be considered to have met:
 - The generally applicable risk-based and leverage capital requirements
 - If applicable, the well-capitalized ratio thresholds under the PCA framework
 - Any other capital or leverage requirements to which the bank is subject
- Therefore, CBLR banks will not be subject to the risk-based capital requirements or the capital conservation buffer under the generally applicable rule.

Other Affected Regulations

- The CBLR final rule amends other regulations referencing:
 - “Total capital,” so that an electing banking organization uses tier 1 capital instead
 - “Risk-weighted assets,” so that an electing banking organization uses average total consolidated assets (i.e., the denominator of the leverage ratio) instead
 - “Capital stock and surplus” (or similar items), so that an electing banking organization uses tier 1 capital plus allowances for loan and lease losses (or adjusted allowance for credit losses, as applicable) instead

Effective Dates

- CBLR final rule: Qualifying banking organizations can opt into the CBLR framework on their March 31, 2020, regulatory reporting forms.
- Capital simplifications final rule: Eligible banking organizations will be permitted to apply the final rule on the effective date of April 1, 2020, or can choose to early adopt as of January 1, 2020.
 - Banking organizations choosing to early adopt will have the option to report the simplified tier 1 capital calculation on their March 31, 2020, regulatory reporting forms.

CBLR: Proposed Call Report Revisions

- The Board also plans to issue an information collection proposal in the near future to amend the FR Y-9C to include a section for banks that opt into the CBLR.
- The Board anticipates this section of the FR Y-9C will generally be consistent with the proposed Call Report CBLR collection, as shown in this slide.

The leverage ratio calculation would be moved up and after the tier 1 numerator calculation.



If the bank has a leverage ratio of 9 percent or above or is within the grace period, it would complete this section, collecting applicable information for the qualifying criteria.



The last section would be for informational purposes. It would quantify CECL impacts and CBLR-specific issues.



Total Assets for the Leverage Ratio

27. Average total consolidated assets¹.....
 28. LESS: Deductions from common equity tier 1 capital and additional tier 1 capital (sum of items 6, 7, 8, 10.b, 13 through 15, 17, and certain elements of item 24 - see instructions).....
 29. LESS: Other deductions from (additions to) assets for leverage ratio purposes.....
 30. Total assets for the leverage ratio (item 27 minus items 28 and 29).....

RCOA	Amount
KW03	
P875	
B596	
A224	
RCOA	Percentage
7204	

Leverage Ratio*

31. Leverage ratio (item 26 divided by 30)

Items 32 through 34.d are to be completed only by qualifying institutions that have a leverage ratio that exceeds 9 percent or are within the grace period and have elected to adopt the community bank leverage ratio (CBLR) framework.

Qualifying Criteria for Using the CBLR Framework*

32. Total assets (Schedule RC, item 12) (must be less than \$10 billion).....
 33. Trading assets and trading liabilities (Schedule RC, sum of items 5 and 15). Report as a dollar amount in Column A and as a percentage of total assets (item 32 above) (5% limit) in Column B.....
 34. Off-balance sheet exposures:
 a. Unused portion of conditionally cancellable commitments.....
 b. Securities lent and borrowed (Schedule RC-L, sum of items 6.a and 6.b).....
 c. Other off-balance sheet exposures.....
 d. Total off-balance sheet exposures (sum of items 34.a through 34.c). Report as a dollar amount in Column A and as a percentage of total assets (item 32 above) (25% limit) in Column B.....

Column A		Column B	
RCOA	Amount	RCOA	Percentage
2170			
XXX1		XXX2	
RCFA			
XXX3			
XXX4			
XXX5		XXX6	

Items 35 through 38.c are to be completed only by qualifying institutions that have a leverage ratio that exceeds 9 percent or are within the grace period and have elected to adopt the CBLR framework.

35. Unconditionally cancellable commitments.....
 36. Investments in the tier 2 capital of unconsolidated financial institutions.....
 37. Allocated transfer risk reserve.....
 38. Amount of allowances for credit losses on purchased credit-deteriorated assets:²
 a. Loans and leases held for investment.....
 b. Held-to-maturity debt securities.....
 c. Other financial assets measured at amortized cost.....

RCOA	Amount
S540	
XXX7	
3128	
JJ30	
JJ31	
JJ32	

*Report each ratio and criterion as a percentage, rounded to four decimal places, e.g., 12.3456.

¹Institutions that have adopted ASU 2016-13 and have elected to apply the CECL transition provision should include the applicable portion of the CECL transitional amount.

²Items 38.a through 38.c should be completed only by institutions that have adopted ASU 2016-13.

Summary of Tier 1 Capital Calculation under the Capital Simplifications Final Rule

Tier 1 Capital*	Simplified Tier 1 Capital
Individual threshold deduction of 10 percent of common equity tier 1 capital for MSAs, certain DTAs, and investments in common stock of unconsolidated financial institutions.	Individual deduction thresholds increased to 25 percent of common equity tier 1 capital for MSAs and DTAs. Separate treatment of investments in common stock of unconsolidated financial institutions eliminated.
Aggregate threshold deduction of 15 percent of common equity tier 1 capital for MSAs, certain DTAs, and investments in common stock of unconsolidated financial institutions.	Eliminates the aggregate 15 percent common equity tier 1 capital deduction threshold.
Deduction treatments for (i) significant investments in the capital of unconsolidated financial institutions in the form of common stock, (ii) significant investments in the capital of unconsolidated financial institutions that are not in the form of common stock, and (iii) non-significant investments in the capital of unconsolidated financial institutions.	Eliminates distinction between significant and non-significant investments in the regulatory capital of unconsolidated financial institutions. Applies a deduction threshold of 25 percent of common equity tier 1 to the aggregate of all investments in the capital of unconsolidated financial institutions.
Limitation on minority interest*	Simplified limitation on Minority Interest
Based on the calculation of the capital ratios of the subsidiary.	Removes allocation based on the subsidiary's capital ratios. Limited to 10 percent of the bank's relevant tier of capital. For example, tier 1 minority interest included in tier 1 capital would be limited to 10 percent of the bank's tier 1 capital.

*As of the effective date of the Capital Simplifications Final Rule, this calculation of tier 1 capital and limitation of minority interest is only applicable to advanced approaches banking organizations.

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