

Board of Governors of the Federal Reserve System  
Federal Deposit Insurance Corporation  
Office of the Comptroller of the Currency



# Community Bank Leverage Ratio Framework

Community Bank Compliance Guide

October 2019

## Introduction

This guide<sup>1</sup> is intended to help community banking organizations understand the optional community bank leverage ratio framework recently adopted by the federal banking agencies. The framework provides for a simple measure of capital adequacy for certain community banking organizations, consistent with section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act. Depository institutions and depository institution holding companies that have less than \$10 billion in total consolidated assets and meet other qualifying criteria, including a tier 1 leverage ratio of greater than 9 percent, are considered qualifying community banking organizations and are eligible to opt into the community bank leverage ratio framework.

This guide summarizes the community bank leverage ratio framework and therefore does not carry the effect of law or regulation. In addition to using this guide, community banking organizations should review the final rule implementing the community bank leverage ratio framework.

## Overview of the Community Bank Leverage Ratio Framework

- The community bank leverage ratio framework is an **optional framework** that is designed to reduce burden by removing the requirements for calculating and reporting risk-based capital ratios for qualifying community banking organizations that opt into the framework.
- Qualifying community banking organizations that elect to use the community bank leverage ratio framework and that maintain a leverage ratio of greater than 9 percent are considered to have satisfied the risk-based and leverage capital requirements in the agencies' generally applicable capital rule. Additionally, such insured depository institutions are considered to have met the well-capitalized ratio requirements for purposes of section 38 of the Federal Deposit Insurance Act.
- The main components and requirements of the community bank leverage ratio framework are as follows:

Community Bank Leverage Ratio Framework	
<b>Qualifying Community Banking Organization</b>	<ul style="list-style-type: none"><li>• Leverage ratio greater than 9 percent</li><li>• Less than \$10 billion in average total consolidated assets</li><li>• Off-balance-sheet exposures of 25 percent or less of total consolidated assets</li><li>• Trading assets plus trading liabilities of 5 percent or less of total consolidated assets</li><li>• Not an advanced approaches banking organization</li></ul>
<b>Calculation of the Leverage Ratio</b>	$\frac{\text{Tier 1 capital}}{\text{Average total consolidated assets}}$
<b>Leverage ratio Requirement</b>	Greater than 9 percent

<sup>1</sup> This small entity compliance guide is issued in accordance with Section 212 of the Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. No. 104-121, 110 Stat. 857, reprinted in 5 U.S.C.A. § 601, note.

<b>Community Bank Leverage Ratio Framework</b>	
<b>Grace Period</b>	<p>A two-quarter grace period (which begins as of the end of the calendar quarter in which the electing banking organization ceases to satisfy any of the qualifying criteria) to either meet the qualifying criteria again or to comply with the generally applicable capital rule.</p> <ul style="list-style-type: none"> <li>• Grace period applies when a banking organization’s leverage ratio is 9 percent or less but greater than 8 percent.</li> <li>• A banking organization that fails to maintain a leverage ratio greater than 8 percent would not be permitted to use the grace period and must comply with the generally applicable capital rule and file the appropriate regulatory reports.</li> <li>• Grace period does not apply in the case of a merger or acquisition.</li> </ul>

## **Details of the Community Bank Leverage Ratio Framework**

### Calculation of the Leverage Ratio

The leverage ratio required for purposes of the community bank leverage ratio framework is calculated as tier 1 capital divided by average total consolidated assets, consistent with how banking organizations calculate their leverage ratio under the generally applicable capital rule.

The calculation of tier 1 capital includes the modifications made in relation to the capital simplifications final rule<sup>2</sup> and current expected credit losses methodology (CECL) transitions final rule.<sup>3</sup>

Note: 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. The community bank leverage ratio 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 under the generally applicable capital rule.

### Qualifying Community Banking Organization

The community bank leverage ratio framework is optional for a banking organization that meets the following qualifying criteria:<sup>4</sup>

<sup>2</sup> Banking organizations electing to use the community bank leverage ratio framework would incorporate the changes made by the capital simplifications final rule when calculating tier 1 capital, which include an increase in the individual regulatory limit for mortgage servicing assets and certain deferred tax assets from 10 percent to 25 percent of a non-advanced approaches banking organization’s common equity tier 1 capital. In addition, the capital simplifications final rule removed the aggregate 15 percent common equity tier 1 capital threshold deduction, streamlined the treatment for investments in the capital of unconsolidated financial institutions, and simplified the calculation for minority interest limitations for non-advanced approaches banking organizations. For more information on the capital simplifications final rule, see 84 FR 35234 (July 22, 2019). The agencies also have adopted a final rule that permits non-advanced approaches banking organizations to implement the capital simplifications final rule in the quarter beginning January 1, 2020, or wait until the quarter beginning April 1, 2020.

<sup>3</sup> See 84 FR 4222 (February 14, 2019)

- 1) *A leverage ratio of greater than 9 percent.*
- 2) *Total consolidated assets of less than \$10 billion:* Total consolidated assets are calculated in accordance with the reporting instructions to Schedule RC of the Call Report or Schedule HC of Form FR Y-9C, as applicable.
- 3) *Total off-balance-sheet exposures (excluding derivatives other than sold credit derivatives and unconditionally cancellable commitments) of 25 percent or less of total consolidated assets:* The off-balance sheet qualifying criterion incorporates off-balance sheet exposures currently required to be captured and reported by banking organizations in the Call Report or Form FR Y-9C. The following exposures are included in the calculation:
  - a. The unused portions of commitments (except for unconditionally cancellable commitments);
  - b. Self-liquidating, trade-related contingent items that arise from the movement of goods;
  - c. Transaction-related contingent items (*i.e.*, performance bonds, bid bonds, and warranties);
  - d. Sold credit protection in the form of guarantees and credit derivatives;
  - e. Credit-enhancing representations and warranties;
  - f. Off-balance-sheet securitization exposures (to the extent that they are not captured in other off balance-sheet exposures);
  - g. Letters of credit;
  - h. Forward agreements that are not derivative contracts; and
  - i. Securities lending and borrowing transactions.
- 4) *Total trading assets plus trading liabilities of 5 percent or less of total consolidated assets:* Total trading assets and trading liabilities are calculated as the sum of those exposures, in accordance with the reporting instructions for these items in the Call Report or Form FR Y 9C, as applicable.
- 5) *Non-advanced approaches institution:* An advanced approaches banking organization is not eligible to use the community bank leverage ratio framework.

### Opting into and out of the community bank leverage ratio framework

A qualifying community banking organization may opt into the community bank leverage ratio framework by completing the associated reporting line items that are required for such firms on its Call Report and/or Form FR Y-9C, as applicable. A qualifying community banking organization becomes subject to the community bank leverage ratio framework when it makes an election.

A banking organization may opt out of the community bank leverage ratio framework and become subject to the generally applicable capital rule by completing the associated reporting requirements on its Call Report and/or Form FR Y-9C, as applicable. A banking organization can opt out of the community bank leverage ratio framework between reporting periods by providing its capital ratios under the generally applicable capital rule to its appropriate regulators at that time.

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<sup>4</sup> A non-advanced approaches subsidiary depository institution may opt into the community bank leverage ratio framework if the institution meets all qualifying requirements—even if its parent holding company is not a qualifying banking organization, and vice versa.

A banking organization that opts out of the community bank leverage ratio framework can subsequently opt back into the community bank leverage ratio framework if it meets the qualifying criteria listed above.

### Grace Period

If an electing banking organization fails to satisfy one or more of the qualifying criteria but maintains a leverage ratio of greater than 8 percent, that banking organization would have a “grace period” of up to two quarters during which it could continue to use the community bank leverage ratio framework and be deemed to meet the “well capitalized” capital ratio requirements. As long as the banking organization is able to return to compliance with all the qualifying criteria within two quarters, it continues to be deemed to meet the “well capitalized” ratio requirements and be in compliance with the generally applicable capital rule.

A banking organization is required to comply with and report under the generally applicable capital rule and file the relevant regulatory reports if the banking organization (i) is unable to restore compliance with all qualifying criteria during the two-quarter grace period (including reporting a leverage ratio greater than 9 percent), (ii) has a leverage ratio of 8 percent or less, or (iii) ceases to satisfy the qualifying criteria due to consummation of a merger transaction.