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March 25, 2019

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Via Email: comments@FDIC.gov

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Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
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Re: RIN 3064-AE91; Docket ID OCC-2018-0040; Docket No. R-1638

Ladies and Gentlemen:

The following comments are submitted on behalf of the Independent Bankers Association of Texas ("IBAT"), a trade association representing more than 350 independent, community banks domiciled in Texas.

IBAT submits these comments in response to the notice of proposed rulemaking (proposal) that would provide 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 ("EGRRCPA").

Section 201 of EGRRCPA directs the Federal Banking Agencies ("FBA") to develop a Community Bank Leverage Ratio ("CBLR") of not less than 8 percent and not more than 10 percent and defines the CBLR as a tangible leverage ratio. Section 201 of the Act defines the components and potential levels of the CBLR, limits eligibility for compliance with the CBLR and sets out regulatory consequences for compliance with the CBLR.

Under the current proposal, most depository institutions and depository institution holding companies that have less than $10 billion in total consolidated assets, meet risk-based qualifying criteria for designation as a Qualifying Community Bank ("QCB") and have a CBLR of greater than 9

percent would be eligible to opt into a CBLR framework. Banks that elect to use the CBLR framework would be exempt from the current regulatory capital rules and associated reporting requirements.

The proposed rule allows a QCB to elect to use the CBLR framework or to use the current regulatory capital requirements without penalty, effectively an 'opt-out'. A QCB electing to 'opt-out' of the CBLR may do so before falling below the 9 percent tangible leverage ratio but must notify the FBAs of that election. A bank that is a QCB may 'opt-in' and 'opt-out' of the CBLR by notifying the FBAs without limitation provided it maintains its status as a QCB.

Under Section 201(c) a QCB with a CBLR greater than 9 percent shall be considered to have met —

> *(A) the generally applicable leverage capital requirements and the generally applicable risk-based capital requirements;*
>
> *(B) in the case of a qualifying community bank that is a depository institution, the capital ratio requirements that are required in order to be considered well capitalized under section 38 of the Federal Deposit Insurance Act (12 U.S.C. 1831o) and any regulation implementing that section; and*
>
> *(C) any other capital or leverage requirements to which the qualifying community bank is subject.*

While IBAT appreciates the agencies' proposal to provide community banks with regulatory relief, the relief intended in Section 201 appears unduly complicated by that same proposal. While deciding how exactly to determine and calculate appropriate capital levels is a difficult if not impossible task, we believe this proposal for "simplification" adds additional complexity and uncertainty.

Calculation of the CBLR Ratio - Section 201 allows the agencies to define the numerator of the CBLR as Tier 1 Capital as currently defined under the regulatory capital rules and, consequently, the CBLR should be a bank's Tier 1 Leverage Ratio as currently calculated. Banks should not have to calculate yet another ratio to determine if they meet the CBLR. A QCB would simply report the information necessary to calculate its Tier 1 Capital on Schedule RC-R of the Call Report and divide its Tier 1 Capital by its adjusted average total consolidated assets to calculate its Tier 1 Leverage Ratio.

Creation of New Prompt Corrective Action ("PCA") Framework – Prompt corrective action is a big deal to say the least. Guidelines are in effect today with substantially lower levels of required equity capital, and IBAT strongly believes those guidelines should be followed under the proposal. As proposed, a bank that elects to use CBLR and falls below the 9 percent level would be subject to a proposed CBLR PCA framework. Section 201 does not mandate the creation of a separate PCA framework within the CBLR framework as the agencies propose. IBAT believes that a separate PCA framework is especially punitive and may subject those banks not opting to participate to "regulatory creep" wherein the CBLR threshold becomes the "new normal" for minimum equity capital levels regardless of risk-based capital. As discussed below, a regulatory tool as lethal as PCA is not necessary to ensure compliance with this simplified capital regime.

We are hopeful this will be seriously reconsidered prior to issuance of a final rule.

Nine Percent CBLR – IBAT supports strong capital requirements for banks of all sizes. We also recognize that the opportunity to avoid the tedious and complex calculations of the present risk-based capital adequacy determinants is worth in some instances maintaining a marginally higher equity capital ratio.

While exceptions exist, the fact is that bankers are generally fine with lower capital levels than regulators would like to see.

A number of our members have indicated they would prefer an 8 percent floor, which remains well above the new (2019) capital requirements of 7 percent for community banks, including the capital conservation buffer. These banks would, under that particular capital adequacy matrix, be considered “well-capitalized”. As discussed below, the rule as proposed will likely not result in banks at or near the CBLR threshold opting to take advantage of this alternative.

Regulators should continue to have the ability to assess capital adequacy on a bank-by-bank basis dependent upon a variety of factors and respond accordingly. Lowering the CBLR threshold to 8 percent would add more than 50 Texas banks and approximately 600 community banks across the country that could at least consider a simplified capital regime.

Clarification of Grace Period – Based on our understanding of the proposed rule, a QCB that fails to meet the criteria as a QCB after electing to use the CBLR framework has a two-quarter grace period to reestablish qualifications before being deemed ineligible for the CBLR framework. The proposed rule should clearly address what the grace period is if a bank fails to qualify as a QCB, and specifically at what point in the process PCA becomes applicable.

IBAT strongly urges the regulatory authorities to reconsider their approach when a bank falls below the 9 percent (or wherever that threshold is ultimately set) CBLR, or otherwise fails to qualify as a QCB. It would seem intuitive to simply require a bank falling below the CBLR threshold to revert to current risk-based capital requirements. While we remain skeptical of the appropriate nature of risk-based capital requirements for community banks, we believe that in virtually all cases the banks that fall below the CBLR threshold will still meet those requirements. It would be appropriate for the regulators to revisit risk-based capital requirements for community banks at the earliest possible opportunity.

Further, given the complexity of the proposed rule and the risk of PCA looming under this proposal, we would be surprised if banks with a CBLR within 100 basis points (or perhaps more) of the threshold would even consider availing themselves of this important and potentially welcome regulatory relief. The stakes are simply too high.

Applicability to Capital Requirements at Bank and Holding Company - Additionally, language should be added to the proposal clarifying that CBLR applies to either a bank or a holding company that qualify as a QCB separately and individually. In other words, a bank (that is a QCB) may meet the CBLR while the parent holding company (also a QCB) does not meet the CBLR, or vice versa. In theory, based upon various leverage scenarios, that is distinctly possible. While this appears to be the intent of the proposal, clarification would be appreciated.

Impact of CECL Implementation - While we do not anticipate significant adjustments to the balance sheets or income statements of the majority of community banks subsequent to the implementation of CECL, a three-year phase-in is appropriate. We would be remiss to not again express our strong opinion that the CECL methodology is another textbook example of regulatory overkill for the community banking sector and is a solution in search of a problem for the vast majority of our banks. Community banks should have a thorough understanding of the risk inherent in both sides of their balance sheet and maintain

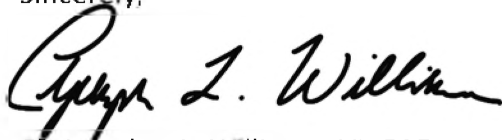
appropriate allowances based upon that risk assessment and in consultation with their regulatory agencies.

While obviously a FASB initiative, we urge the regulators to consider recommending either an outright exemption for community banks or an alternative “minimum” ALLL to avoid the burdensome analysis required to comply with CECL. For example, and in the same spirit as the CBLR, a QCB with an asset quality component of 1 or 2 would be considered adequately reserved with maintenance of a 150 basis points (or whatever level is deemed appropriate) ALLL. It appears counterintuitive to require banks with a conservative lending philosophy, appropriate loan administration and negligible loss experience to jump through the hoops necessary to comply with CECL.

While IBAT is very appreciative of the significant efforts made by the agencies to develop a simple leverage ratio that makes sense for the traditional community bank business model, we believe this proposal goes well beyond what was contemplated in Section 201 and should be revisited on a number of levels.

As always, thank you for consideration of our comments and concerns. We are happy to discuss further or provide additional information.

Sincerely,



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