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Portfolio

[tag] Checks and Balances

[hed] ICBA Avengers unite: Basel III Endgame proposals targeted at large banks

[dek] With legislation like the Interagency Proposal to Amend Regulatory Capital Requirements for Large Banks, it’s as important as ever for community bankers to share their opinions on why “too big to fail” banks and community banks should be regulated differently.

[byline] By Chris Cole

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ICBA’s efforts to encourage policymakers to differentiate community banks from larger institutions when proposing regulations is paying dividends—and the proposed “Basel III Endgame” is proof positive.

For years, ICBA has effectively highlighted the difference between community banks and those traditionally viewed as “too big to fail” banks. Even before the failure of Silicon Valley Bank (SVB) in March, ICBA led the community banking industry in its campaign to show how community banks serving local communities are vastly different from large, super-regional or national banks.

In a post-SVB world, this mission has taken on increasing importance as policymakers look to shore up oversight of these institutions. As they reconsider capital standards and the impact a potential failure could have on the financial system, new rulemaking and guidance is on the horizon—and ICBA is speaking out for community banks to ensure they are not subject to new onerous capital rules.

Community banks have many high-ranking allies on this front. Federal Reserve chairman Jerome Powell, Federal Deposit Insurance Corp. (FDIC) chairman Martin Gruenberg, Federal Reserve governor Michelle Bowman and Fed vice chair of supervision Michael Barr have all publicly stated that new regulatory capital and debt requirements should not affect community banks. ICBA commends each of these leaders for their pragmatic approach.

Support from policymakers has been key in ensuring any regulatory change in this area focuses exclusively on large banks. Of the three related proposals released by the Office of the Comptroller of the Currency (OCC), the FDIC and the Fed in July and August, all three limit their focus to institutions with $100 billion or more in assets (with one focused on institutions with $250 billion or more in assets).

**[subhed] A closer look at large bank proposals**

**Basel III Endgame.** In July, the agencies released their Interagency Proposal to Amend Regulatory Capital Requirements for Large Banks (often referred to as Basel III Endgame). It would make significant changes to the regulatory capital framework for U.S. banking organizations with $100 billion or more in assets or significant trading activity. The proposal would also ensure the capital requirements applicable to large banking organizations are tiered based on the complexity and size of the institution.

Large banks would be required to:

* Include accumulated other comprehensive income (AOCI) in the calculation of regulatory capital
* Better capture credit risk exposure by using the “expanded risk-based approach,” which calculates total risk-weighted assets using credit risk, equity risk, operational risk, market risk and credit valuation adjustment (CVA) risk
* Calculate common equity tier 1 capital ratio, tier 1 capital ratio and total capital ratio using the risk-weighted asset amounts under the current standardized approach <i>*and*<i> the expanded risk-based approach. The higher of the two risk-weighted asset amounts will be used to satisfy minimum capital requirements.
* Follow market risk rules for trading activity, including CVA risk and market risk requirements, when total trading assets and liabilities exceed 10% of total assets. The dollar threshold for trading assets and liabilities would be raised from $1 billion to $5 billion.

Banks with $100 billion to $250 billion in assets would also be subject to the supplementary leverage ratio and the countercyclical capital buffer.

**Enhanced resolution plans.** In August, the FDIC and Fed proposed guidance that would help banks with $250 billion or more in assets further their resolution plans, also known as “living wills,” which are required under the Dodd-Frank Act. These plans detail how a bank holding company would rapidly resolve the bank when facing bankruptcy due to financial distress or failure. The guidance is focused on areas of potential vulnerability, including capital, liquidity and operational capabilities. In August, the FDIC also proposed stricter resolution plans for banks with $100 billion or more in assets and informational filings for banks with assets between $50 billion and $100 billion. ICBA has serious concerns with both FDIC proposals.

**Financial stability through long-term debt.** In August, the agencies also proposed a rule that would require large banks with $100 billion or more in assets to maintain a layer of long-term debt. This would improve financial stability by increasing the resolvability and resiliency of such institutions. The proposal also limits complex activities, discouraging large banks from interbank long-term debt holdings to reduce system interconnectedness and contagion.

**[subhed] The way forward for proportionate regulation**

ICBA maintains that regulatory reforms aimed at increasing oversight and reforming capital frameworks must be tailored to differentiate community banks from large banks that pose systemic risk.

While the proposals are out, victory is not assured until final rules and guidance are released. Community bankers need to keep momentum in our favor throughout the comment period, which ends Nov. 30. Comments supporting the proposal’s focus on large banks is invaluable along with involvement in the turnkey ICBA National Campaign to educate the American public on the benefits of community banking and why their choice of bank matters.

ICBA will continue working with policymakers to ensure Washington’s policy response does not affect the community banks that continue to appropriately manage risk and do right by their customers and communities.

Chris Cole (<i>*chris.cole@icba.org*<i>) is executive vice president, senior regulatory counsel

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