Indexing Regulatory Thresholds

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Issue Update

For decades, many regulatory thresholds have stayed fixed in nominal terms, even as the economy has grown. These thresholds were typically set during very different economic conditions and have not been updated to reflect changes in the banking sector. As a result, thresholds that once reflected meaningful distinctions in size, complexity, or risk now capture institutions that were never intended to be subject to more burdensome regulatory requirements.

For example, heightened audit requirements established by the FDIC kick in when a bank's assets reach $500 million. When this threshold was set in 1993, the more stringent requirements applied to only 7 percent of banks. Today, it applies to 41 percent. Dozens of thresholds, from stress testing to resolution planning, have drifted the same way.

Why It Matters

This regulatory "drift" creates three problems:

1. **Burdens institutions never meant to be captured.**
   Over time, economic growth and inflation erode the real value of thresholds, pulling more institutions into regulatory regimes that were never intended to apply to them. Banks with limited complexity or risk profiles may be forced to shoulder costs and reporting burdens designed for much larger entities.
2. **Discourages organic growth.**
   Institutions manage their balance sheets defensively to avoid crossing arbitrary thresholds. In some cases, this distortion discourages organic growth and instead encourages consolidation as the only viable means to absorb new regulatory burdens.
3. **Dilutes regulatory resources.**
   An expanding pool of covered banks beyond the intended scope dilutes regulatory efforts and the ability of agencies to focus on the largest sources of risk. These outcomes run counter to the policy objectives Congress and regulators have set.

Recommended Action Items

The solution is indexing. ABA recommends, ***after a one-time adjustment to correct for past inaction***, ***linking asset-based thresholds to nominal GDP***, which reflects the size of the economy and the scale of the banking sector. Indexing is a low-cost, high-impact reform. It improves transparency, reduces arbitrary burdens, and allows regulators to focus on where the risk really is.

Policy makers should prioritize this issue like the FDIC, which has a proposal to index some of its thresholds. Indexing is particularly important for Congress to consider, since some thresholds are set by statute.

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