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June 22, 2018

Federal Reserve Board
Office of the Comptroller of the Currency
c/o Legislative and Regulatory Activities Division
400 7th Street SW, Suite 3E–218
Washington, DC 20219
Submitted via email to: regs.comments@occ.treas.gov

Re: Docket ID OCC–2018–0002, Regulatory Capital Rules: Regulatory Capital, Enhanced Supplementary Leverage Ratio Standards for U.S. Global Systemically Important Bank Holding Companies and Certain of Their Subsidiary Insured Depository Institutions; Total Loss-Absorbing Capacity Requirements for U.S. Global Systemically Important Bank Holding Companies

Dear Officers,

On behalf of more than 400,000 members and supporters of Public Citizen, we offer the following comments on proposed rules to relax the enhanced Supplementary Leverage Ratio (eSLR).

The 2008 financial crisis revealed drastic deficiencies in bank capital since as the value of assets fell, it essentially eliminated the margin between banks' assets and liabilities. Congress and regulators understood the danger that posed, and established improved capital requirements. These have come in two forms: a basic leverage requirement, which does not distinguish between the risk of assets; and a risk-based capital requirement, which does distinguish based on risk, identifying some asserts as safer than others. For example, a Treasury bond is considered safer than a construction loan. When determining risk-based capital, regulators require less capital for the ownership of Treasuries than for construction loans. The eSLR does not distinguish between assets based on risk.

The current eSLR rule requires the largest banks, namely those designated as Global Systemically Important Banks (GSIBs), to maintain a supplementary leverage ratio greater than 3 percent. Leverage ratios refer to the amount of capital, or the difference between assets and liabilities, in relation to total assets held by a financial institution. In addition to the three percent baseline, GSIBs must maintain an "enhanced" leverage ratio buffer of 2 percent in order to avoid limitations on firms' distributions and certain discretionary bonus payments.

The Federal Reserve Board (Board) and the Office of the Comptroller of the Currency (OCC) now propose to roll back this critical systemic risk protection by reducing the eSLR that banks must hold. The proposal would replace each GSIB's enhanced 2 percent leverage buffer with a leverage buffer set equal to 50 percent of the firm's risk-based surcharge, which is determined by the Board's GSIB risk-based surcharge rule. If allowed to move forward, this proposal would result in a significant reduction in capital requirements. For depository institutions among the GSIBs, it would reduce capital by a substantial amount. According to estimates from the Federal Deposit Insurance Corp, the figure is $121 billion.[1]

More specifically, here is the FDIC analysis of likely future supplementary capital requirements for GSIBs under the proposed rule:

- JPMorgan Chase & Co.: $34.597 billion (20.83% reduction in tier 1 capital);
- Citigroup: $26.978 billion (23.3% reduction);
- Bank of America: $22.838 billion (18.5% reduction);
- Wells Fargo: $20.406 billion (16.9% reduction);
- Bank of New York Mellon: $5.911 billion (33.65% reduction);
- State Street: $5.346 billion (37.5% reduction);
- Morgan Stanley: $2.507 billion (25% reduction); and
- Goldman Sachs: $1.93 billion (9.49% reduction).

The Board and OCC contend that the current leverage ratio requirements represent a bias in favor of riskier assets. That is, a bank may decide to hold riskier assets (that pay a better return) than less risky assets, because the capital would be the same under a straight leverage ratio. By relying more on risk-based capital ratios tied to specific GSIB surcharges, and less on a simple leverage ratio, the regulators contend that banks would operate more safely.

We believe this is problematic for three reasons. First, banks should be adding capital, not reducing capital. Major banks already operate perilously close to insolvency. Federal Reserve Board Governor Lael Brainard dissented from this proposal and in a subsequent speech she explained, "At a time when valuations seem stretched and cyclical pressures are building, I would be reluctant to see our large banking institutions releasing the capital and liquidity buffers that they have built so effectively over the past few years, especially since credit growth and profitability in the U.S. banking system are robust."[2]

The Board found that losses of some of major financial institutions during financial crises reached 19 percent of their assets.[3] Based on this, we believe capital levels should be higher than this, namely 20 percent. In one of his final speeches as Fed governor, Daniel Tarullo observed, the "capital requirement that best achieves this [stability] is somewhere in the range of 13 percent to 26 percent."[4] As of now, according to FDIC estimates, capital at JP Morgan, Bank of America, Wells Fargo and Citigroup are below 9 percent.[5] These figures are not much different than what the banks reported before the crash. Commented then FDIC Chair Martin Gruenberg, "Strengthening leverage capital requirements for the

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[1] Jonathan Heltman, Fed, OCC back proposal to ease big bank capital measure—without FDIC, AMERICAN BANKER, (April 11, 2018) https://www.americanbanker.com/news/fed-occ-back-proposal-to-ease-big-bank-capital-measure

[2] Gov. Lael Brainard, *An Update on the Federal Reserve's* Financial Stability Agenda, FEDERAL RESERVE, (April 3, 2018) https://www.federalreserve.gov/newsevents/speech/brainard20180403a.html

[3] ''The Supervisory Capital Assessment Program: Overview of Results.'', Federal Reserve, (May 7, 2009), available at http://www.federalreserve.govnewsevents/press/bcreg/bcreg20090507a1.pdf.

[4] Daniel Tarullo, Departing Thoughts, FEDERAL RESERVE, (April 4, 2017) https://www.federalreserve.gov/newsevents/speech/tarullo20170404a.htm

[5] Press Statement, Federal Deposit Insurance Corporation, Director Thomas Hoenig , Release of Fourth Quarter 2014 Global Capital Index (April 2, 2015), http://1.usa.gov/1SNutf7.

largest, most systemically important banks in the United States was among the most important post crisis reform."[6] Yet, this proposal would have the effect of double-digit percentage reductions in capital held by some of the world's biggest banks.

Second, regulators should not reduce capital based on judgments about risk. These judgments can be wrong, as evinced by the regulatory assessment that mortgages were less risky than other investments, which proved woefully wrong in the years leading to the financial crash. A more robust across-the-board leverage ratio would better ensure bank safety than greater reliance on risk-based capital ratios that invite a bank to select assets based on risk-weighted capital requirements as opposed to making reasonable funding decisions based on risk and return.

Finally, current capital requirements are not hindering bank lending. Bank lending, and bank profits, are at near records. There is little evidence that increasing bank capital requirements stifles lending. Even Fed Chair Jay Powell, while advancing this proposal, acknowledges that current bank capital requirements are not stifling: "As you look around the world, U.S. banks are competing very, very successfully. They're very profitable. They're earning good returns on capital. Their stock prices are doing well. So I'm looking for the case, for some kind of evidence that — and I'm open to this — some kind of evidence that regulation is holding them back, and I'm not really seeing that case as made at this point."[7] Indeed, the agencies proffer no argument about how this would help promote either industry safety or even greater lending.

It is telling that the Federal Deposit Insurance Corp declined to join this joint rule-making.[8] As noted, Gov. Brainard opposed this proposal.[9] Thomas Hoenig and Sheila Bair, both former officers of the Federal Deposit Insurance Corp., also warn against this proposal.[10]

We urge the Board and the OCC to heed these concerns and withdraw this proposal.

For questions, please contact Bartlett Naylor at bnaylor@citizen,.org

Sincerely,

Public Citizen

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[6] Jonathan Heltman, Fed, OCC back proposal to ease big bank capital measure—without FDIC, AMERICAN BANKER, (April 11, 2018) https://www.americanbanker.com/news/fed-occ-back-proposal-to-ease-big-bank-capital-measure

[7] Victoria Guida, *Powell doesn't see need to loosen rules* on biggest banks, POLITICO, (Nov. 28, 2017) https://www.politico.com/newsletters/morning-money/2018/02/28/powell-aces-hill-test-118527

[8] Peter Eavis, Washington Wants to Ease Bank Rules. Not Every Regulator Agrees, NEW YORK TIMES (April 24, 2018) https://www.nytimes.com/2018/04/24/business/dealbook/bank-rules-leverage-ratio.html?rref=collection%2Fbyline%2Fpeter-eavis&action=click&contentCollection=undefined&region=stream&module=stream_unit&version=latest&contentPlacement=1&pgtype=collection

[9] Lael Brainard, Safeguard Financial Resilience through the Cycle, FEDERAL RESERVE BOARD (April 19, 2018) https://www.federalreserve.gov/newsevents/speech/brainard20180419a.htm

[10] Thomas Hoenig, Sheila Bair, Relaxing Bank Capital Requirements Would Risk Another Crisis, WALL STREET JOURNAL (April 26, 2018) https://www.wsj.com/articles/relaxing-bank-capital-requirements-would-risk-another-crisis-1524784371