

(OCC) Docket ID OCC-2013-0008, (FED) Docket No. R-1460, and (FDIC) RIN 3061-AE01  
DRAFT Public Comment by Cody Hiatt

October 20th, 2013

Office of the Comptroller of the Currency  
Legislative and Regulatory Activities Division  
400 7th Street SW., Suite 3E-218, Mail Stop 9W-11  
Washington, DC 20219

Federal Deposit Insurance Corporation  
Attention: Comments  
550 17th Street NW  
Washington, DC 20429

Board of Governors of the Federal Reserve System  
Attention: Robert de V. Frierson, Secretary  
20th Street and Constitution Avenue NW  
Washington, DC 20551

**RE: Regulatory Capital: Enhanced Supplementary Leverage Ratio Standards for Certain Bank  
Holding Companies, etc. (OCC-2013-0008)**

Dear Members of the OCC, FED, FDIC, and to whom it may concern:

Thank you for the opportunity to respond to the proposed recommendations regarding Enhanced Supplementary Leverage Ratio Standards for Certain Bank Holding Companies (Proposal) issued jointly by the Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (FED), and the Federal Deposit Insurance Corporation (FDIC). The efforts of the Fed, FDIC, and OCC (regulatory community) to mitigate risks to the financial stability of the United States should be applauded. The regulatory community is performing its' duty mandated by the American public as expressed through the Dodd-Frank Act (Public Law 111-203, 2010) to improve accountability in the financial system for the efficient functioning of our economy. The Dodd-Frank Act set ambitious deadlines for finalizing the new rules to address systemic deficiencies in our financial sector because Congress saw spill-over effects on Americans and the global economy.

The parallel trends of deregulation and excessive risk taking by firms culminated in a financial crisis whose consequences resulted in a \$19 trillion loss in household wealth from Q2-2007 to Q1-2009, 8.7 million lost jobs from Dec-07 to Feb-10, and 6.3 million more Americans fell into poverty from 2007-2009 (Treasury, 2012). The subsequent Eurozone crisis further emphasized the need for minimum global standards to be set among the central banks in advanced economies. The minimum standard is represented by the Basel III framework (BCBS, 2011). The final rule implementing Basel II on July 9<sup>th</sup>, 2013, by the Fed and OCC is a milestone that factors in community banks and recognizes the need for a supplementary leverage ratio (Docket ID OCC-2012-0008).

The proposed supplementary leverage ratio rule is a complex topic that may not draw the interest or attention of the general public. It is disheartening to see so many public comments in the regulations.gov dockets originate from special interest groups with an institutional responsibility to increase shareholder value rather than private citizens participating in a democratic process. From the Tea Party movement to the Occupy Wall Street movement, there is a common objection to privatized benefits and socialized costs. My belief is that the general public wants to believe the community of regulators is overhauling the rules to prevent inadequately capitalized systemically important financial institutions (G-SIBs) from having adverse impacts on the global economy.

I am submitting my comments from the perspective of a stakeholder in the broader economy; an economy that relies on the effective design and operation of financial markets. Professionally, I am an Internal Auditor at a diversified manufacturer, Crane Co. (NYSE: CR), with over a decade of accounting experience. Policy makers' response to the financial crisis has been the focus of my studies over the past two years towards a Masters of Public Administration at Seattle University. Admittedly I am not a banker, lawyer, regulator, or paid researcher. This public comment represents a capstone research project that draws on research and conclusions from more informed sources as well as my informed opinion on the proposals.

### **Criteria for proposed rules**

**Objective:** Success is measured by how well the proposed rules accomplish the intended policy objectives. The BASEL Committee on Banking Supervision (BCBS, 255) stated the broad aim of their policies is to:

- reduce the probability of failure of G-SIBs by increasing their going-concern loss absorbency; and
- reduce the extent or impact of failure of G-SIBs, by improving global recovery and resolution frameworks.

**Risk:** As stated in the background of the Proposal,

• **No incentive for risk mitigation:** First, the existence of the “too big to fail” problem reduces the incentives of shareholders, creditors and counterparties of these companies to discipline excessive risk-taking by the companies.

• **Further market consolidation in G-SIBs:** Second, it produces competitive distortions because companies perceived as “too big to fail” can often fund themselves at a lower cost than other companies. This distortion is unfair to smaller companies, damaging to fair competition, and tends to artificially encourage further consolidation and concentration in the financial system.

**Control: Strong Capital base:** “In the agencies' experience, strong capital is an important safeguard that helps financial institutions navigate periods of financial or economic stress. Maintenance of a strong base of capital at the largest, systemically important institutions is particularly important because capital shortfalls at these institutions can contribute to systemic distress and can have material adverse economic effects.” – Docket OCC-2013-0008

The proposed supplemental leverage ratio is designed to be a detective control to evaluate the adequacy of capital in relation to a G-SIBs risk exposure. For this metric to be meaningful it must have the following characteristics:

**-Simple:** The ratio should be non-risk based to avoid complex risk weights for different capital in the numerator.

**-Transparent:** Can the metric be recalculated by information already available/required in financial statements?

**-Useful to inform investors & regulators:** The denominator should be measured in a manner that is internationally consistent among GSIBs to facilitate investment decisions and assessing global stability.

Answering the agencies questions will necessitate a referral back to this criterion.

*Question 1: How would proposed strengthening of the supplementary leverage ratio for covered BHCs and their subsidiary IDIs contribute to financial stability and thus economic growth?*

There is a positive correlation between financial stability and economic growth. Some Eurozone countries have been slow to emerge from a recession because of financial instability. Some commenters on the proposed rules argue that credit availability will be reduced and in turn, economic growth will slow, and ignore the increased financial stability realized from the proposal.

If GSIBs could provide a single metric or ratio that could be consolidated to indicate overall global financial stability then everyone's job would be a lot easier. This has led to a wide range of metrics that when combined provide a more comprehensive assessment of the complexities inherent in global financial stability.

The proposed supplemental leverage ratio adds another dimension to help GSIB stakeholders monitor risk. The Oct 11, 2013 final rule on Implementation of BASEL III (12 CFR Parts 208, 217, and 225) contains provisions for a conservation buffer, counter cyclical buffer, and supplemental leverage ratio but not a capital surcharge that BASEL III proposed for G-SIBs. The supplemental leverage ratio in excess of 3% (6% for well capitalized) would compensate for the lack of G-SIB surcharge not currently implemented in the US.

*Question 2: Would the proposed strengthening of the leverage ratio mitigate public-policy concerns about the regulatory treatment of banking organizations that may pose risks to the broader economy?*

Maybe the largest public-policy concern is "Should we allow G-SIBs to exist, given the concentration of financial assets/liabilities pose a systemic risk to the broader economy?" yet we have come to accept that "too big to fail" is here to stay. For many commentators, including myself think this risk is greater than our risk appetite. I am skeptical that the resolution authority framework and "living wills" will be enacted in the event of another financial crisis, given the extraordinary measures taken by the Fed and Treasury during the last crisis.

In context of the new tools implemented by BASEL III (risk based leverage ratio, etc.), BCBS speaks to the public policy concerns as well:

*“These policy measures are significant, but they are not sufficient to address the negative externalities posed by G-SIBs or to protect the system from the wider spillover risks of G-SIBs. The rationale for adopting additional policy measures for G-SIBs is based on the cross-border negative externalities created by systemically important banks, which current regulatory policies do not fully address.*

*The negative externalities associated with institutions that are perceived as not being allowed to fail due to their size, interconnectedness, complexity, lack of substitutability or global scope are well recognised. In maximising their private benefits, individual financial institutions may rationally choose outcomes that, on a system-wide level, are suboptimal because they do not take into account these externalities. Moreover, the moral hazard costs associated with implicit guarantees derived from the perceived expectation of government support may amplify risk-taking, reduce market discipline and create competitive distortions, and further increase the probability of distress in the future. As a result, the costs associated with moral hazard add to any direct costs of support that may be borne by taxpayers.*

*In addition, given the potential cross-border repercussions of a problem in any of the G-SIBs on the financial institutions in many countries and on the global economy at large, this is not uniquely a problem for national authorities, and therefore requires a global minimum agreement.” - Basel Committee on Banking Supervision, Global systemically important banks: updated assessment methodology and the higher loss absorbency requirement (July, 2013)*

The global minimum agreement from BASEL II gave a false indication of banks' capital available to absorb losses (BCR, 2011). A minimum global agreement doesn't represent an optimal agreement. Many banks engaged in regulatory capital arbitrage, rendering the minimum agreement ineffective. I will offer an alternative to the supplemental leverage ratio calculation as well as a method to improve the existing proposal in responding to the other questions.

*Question 3: The agencies solicit commenters' views on what economic data suggest about leverage ratios and risk-based capital ratios as predictors of bank distress and thus tools to prevent the failure of large systemically-important banking organizations.*

Preparing an answer to this question required me to conduct limited research before asserting my views on leverage ratios. I will defer to the *BIS Committee on Global Financial System (Apr, 2009 CGFS Papers, No 34, Page 16)* regarding tools to prevent a G-SIB's failure.

### **Quantitative constraints on leverage**

*A leverage ratio is defined by the total amount of nominal (non-risk-weighted) assets, possibly augmented by certain off-balance sheet items that a financial institution holds relative to its capital. Maximum leverage ratios have been implemented in some countries for many decades, and were introduced recently in Switzerland.*

#### **Pros:**

- *Transparency. Leverage ratios are easy to measure and timely.*
- *Relevance in times of stress. In circumstances when risk measures become highly uncertain, leverage ratios provide a gauge of the magnitude of exposures an institution has to manage.*

- *Complementary indicator. Leverage ratios can usefully complement risk-weighted capital requirements and act as a check on the viability of individual institutions in extreme circumstances.*
- *Controls the build-up of leverage during the boom.*

**Cons:**

- *Differences in accounting standards and methodology limit their comparability across jurisdictions.*

*CGFS – The role of valuation and leverage in procyclicality*

- *Binding constraints on balance sheet leverage may encourage regulatory arbitrage through the expansion of off-balance sheet activities. One area of future research might be the coverage of off-balance sheet exposures in regulatory policies.*
- *Limits on nominal balance sheet leverage may encourage exposure to more risky assets to enhance the return on equity.*
- *Constant caps on leverage ratios may force banks to deleverage in the downturn of the cycle.*

*As indicators of potential vulnerabilities, leverage ratios could play the role of a precautionary backstop in macroprudential supervision, for both systemically important financial institutions and the system as a whole. For instance, leverage ratios exceeding certain ranges (at the level of individual institutions or the whole system) could trigger a process of surveillance and review followed, if necessary, by corrective interventions.*

*Another option could be to use leverage ratios as a tool to link balance sheet adjustments directly to the financial cycle. For instance, minimum capital requirements as implied by a leverage ratio (or the Basel II Tier 1 ratio) could be combined with a long-term target level. Financial institutions would be required to raise buffers to at least this target level in good times and reduce them to the minimum requirement during downturns. Thus, the range between these two levels would provide scope to accommodate countercyclical movements.*

*A prerequisite for the effective monitoring of aggregate leverage in the economy by authorities is adequate information. The extent of leverage accumulated over the last years – especially in off-balance sheet vehicles and in the form of embedded leverage – has only recently become apparent. Hence, authorities may consider which information on the positions and activities of financial institutions would be needed to identify such a build-up of leverage.*

*Question 4: Would the proposal create any risk-reducing incentives and around what specific activities? Would the proposal create incentives for subject banking organizations to take additional risk and if so, would this effect be expected to limit the safety-and-soundness benefits of the proposal?*

Requiring a G-SIB to hold tier 1 capital in a reasonable proportion to their total on & off balance sheet exposure is not a radical idea, it is sound business practice for an on-going concern. It is unreasonable conclude that quantifying total exposure would compel G-SIBs to take on more exposure.

Scott Roger and Jan Vlček describe in International Monetary Fund Working Paper (2011) actions banks may take in order to meet the higher capital adequacy ratio requirements.

- Increase retained earnings by:
- Raising average lending margins, while keeping dividends unchanged;
- Reducing dividend payments and/or return on equity;
- Increasing operating efficiency while keeping dividends unchanged;
- Reduce risk-weighted assets by:
- Cutting the overall size of their loan portfolios;
- Shifting the composition of loan portfolios towards less risky assets.
- Issue new equity, implying a dilution of existing shareholder rights and a permanent increase in payments to shareholders.

*The results indicate that the size of the macroeconomic impact of a tightening of capital requirements varies substantially according to how banks respond to the regulatory change. The lowest costs are incurred if capital is raised through cutting bank dividends and the target rate of return on equity. However, raising capital through cutting dividends alone may not be sufficient if the timetable for raising capital is fairly short. In this case, faster, but more costly measures may also be needed. In particular, banks can also raise capital by widening interest spreads. The most costly means of raising capital ratios is found to be through adjustment in the level of assets (the denominator of the ratio).*

Commenters that claim banks will be forced to go to the “shadow banking system” shows willingness for G-SIBs to rely on the government safety net rather than prudential risk management. Should we entertain this claim, it calls into question if we should permit unregulated “shadow banking” activity without a regulated sponsor. At any rate, the claim that measuring a leverage ratio will compel G-SIBs to assume greater risks can be flatly dismissed.

*Question 5: What are commenters' views on the proposed calibration of the leverage standards? Is the proposed 6 percent well-capitalized standard for subsidiary IDIs and the proposed 5 percent minimum supplementary leverage ratio plus leverage buffer for covered BHCs appropriate or should these requirements be higher or lower? In particular with regard to covered BHCs, what are the advantages and disadvantages of establishing the minimum supplementary leverage ratio plus leverage buffer at 5 percent for all covered BHC's versus establishing the amount between 4 and 5.5 percent according to each covered BHC's risk-based capital surcharge (that is, to reflect the minimum supplementary leverage ratio of 3 percent plus between 1 and 2.5 percent depending upon each covered BHC's risk-based capital surcharge)? With respect to the subsidiary IDIs of covered BHCs, the agencies seek commenters' views on what, if any, specific challenges these institutions would face in meeting the proposed well-capitalized threshold of 6 percent beginning on January 1, 2018.*

I believe the leverage standards should be higher; 8% well-capitalized standard for subsidiary IDI and 7% minimum supplementary leverage ratio plus leverage buffer for covered BHCs under the proposed rule. Admittedly, I was not able to identify a study or research to support my assertion for a higher leverage standard. Convincing research from Adamati, DeMarzo, Hellwig, and Pfleiderer (2013) supports the conclusion that increasing bank equity requirements imposes no significant social cost.

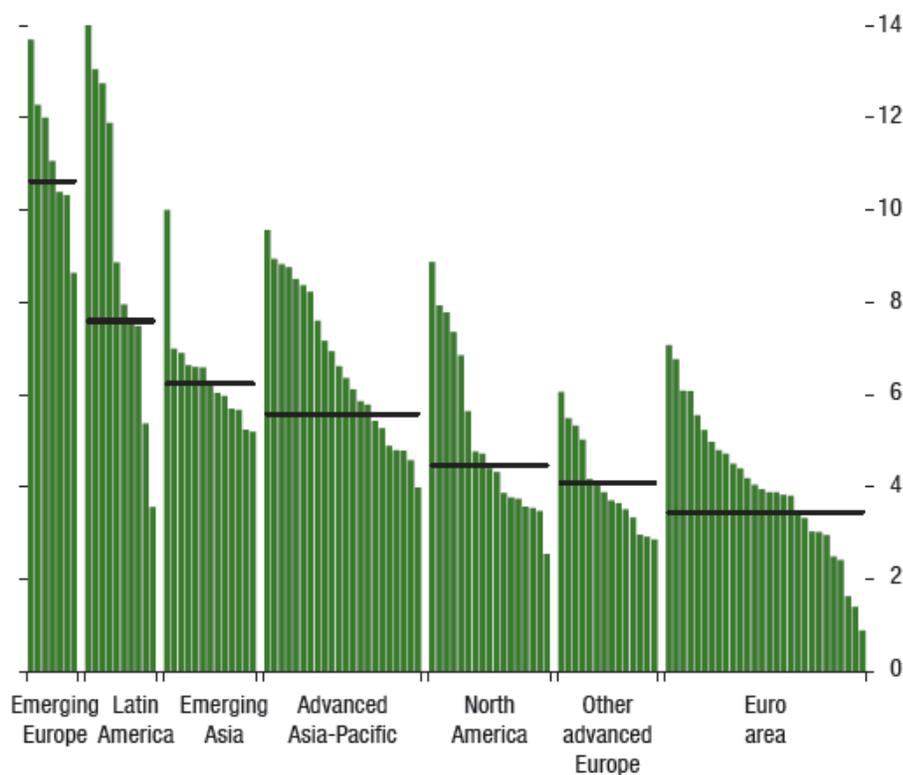
The risk based capital surcharge as presented in question 5 (1-2.5% range) conflicts with our initial criteria for a simple, transparent and useful metric. I support the proposed 5% minimum if my only

alternative is a risk based capital surcharge. Please refer to the citation in question 4 on how G-SIBs can raise the required capital by January 1<sup>st</sup>, 2018. The excerpt below adds context to this discussion.

**International Monetary Fund - Global Financial Stability Report (Oct 2013) Transition Challenges to Stability**

*In addition to risk-weighted capital ratios, investors are increasingly using unweighted leverage ratios to assess bank capitalization. This is partly in anticipation of new rules: the Basel Committee on Banking Supervision has finalized its leverage ratio proposal, and the United States has proposed new leverage standards. But it also reflects lingering concerns about the consistency of approaches used by banks in different jurisdictions for calculating risk-weights, an issue that is being examined by the Basel Committee and by the European Banking Authority. Because the data on netting and off-balance-sheet positions, which are needed to calculate the Basel III leverage ratio, are not published by all banks, investors often use tangible leverage ratios—such as the ratio of tangible equity to tangible assets—to gauge the relative strength of banks (Figure 1.55).*

**Figure 1.55. Large Bank Tangible Leverage Ratios, 2012:Q4**  
(Percent)



Sources: Bloomberg, L.P.; company reports; Federal Deposit Insurance Corporation; and IMF staff estimates.

Note: The tangible leverage ratio is the ratio of adjusted tangible equity to adjusted tangible assets. The adjustment is made by subtracting goodwill, other intangibles, and deferred tax assets. For U.S. banks, these numbers also include adjustments for accounting differences in derivatives netting, in line with the methodology used in Hoenig (2013). However, some differences in accounting definitions may remain. The horizontal lines show the asset-weighted average ratio for the banks in each region. See footnote in text for makeup of regions.

*For some banks, these simple tangible leverage ratios and Tier 1 ratios appear to give conflicting signals about the strength of bank balance sheets. This tension is illustrated in Figure 1.56 (Not shown in excerpt, see original report) which shows a number of banks in either the bottom-right or top-left quadrants of the figure; these quadrants are where the two ratios give different signals about bank balance sheet strength. This apparent conflict reflects, in part, differences in business models and regulatory environments.*

*The “universal banking” model, which tends to be used more in Europe, will naturally lead to a larger balance sheet when compared with a bank with the originate-to-distribute model, more commonly used in North America.*

*The conflicting signals also highlight the importance of restoring investor confidence in the accuracy and consistency of bank risk weights. This also suggests that risk-weighted capital ratios should be supplemented by leverage ratios, as proposed in the Basel III framework.*

**Table 1.3.1. Comparison of Bank Regulations across Jurisdictions**

Regulation	Basel Minimum Standard	United States	European Union
<b>Capital</b>			
Quality of Capital	Common equity to compose CET1, conservation and countercyclical buffers, and G-SIB surcharge Full compliance by 2018	Common equity to compose CET1, conservation and countercyclical buffers; no G-SIB surcharge (separately treated) Full compliance by 2018	Common equity to compose CET1, conservation and countercyclical buffers, and G-SIB surcharge Full compliance by 2018
Quantity of Capital	CET1 4.5% Conservation buffer 2.5% Countercyclical buffer 2.5%	CET1 4.5% Conservation buffer 2.5% Countercyclical buffer 2.5%	CET1 4.5% Conservation buffer 2.5% Countercyclical buffer 2.5%
G-SIB Buffer Leverage Ratio	Surcharge 1.0–3.5% BCBS has set minimum requirement at 3% for leverage ratio to complement risk-based capital ratio.	Not part of U.S. Basel III U.S. has revised its existing leverage ratio to require 4% (minimum) for all banking organizations. Supplementary ratio (BCBS format) was adopted at 3% (minimum) for internationally active banking organizations. Enhanced supplementary ratio has been proposed for bank holding companies (with over \$700 bn in assets or \$10 tm in assets under custody) at 5%. Further, insured depository subsidiaries of these firms will have to meet 6% leverage ratio to be well capitalized under the prompt corrective action regime.	Surcharge 1.0–3.5% EU is expected to adopt leverage ratio within Basel III proposed framework. CRR/CRDIV includes the calculation and reporting of a leverage ratio but does not yet establish it as a pillar 1 requirement.
<b>Liquidity</b>			
Liquidity Supervision		U.S. Dodd-Frank Act, Section 165, requires banks with assets of more than \$50 billion to hold liquidity buffers of highly liquid assets; this is broadly consistent with the objective of Basel III liquidity ratios.	The EU plans to adopt LCR and Net Stable Funding Ratio. LCR implementation phased in beginning in January 2015 at 60%, with full compliance by 2019. EU member states are to carry out supervision and monitor reporting of LCR compliance progress.
Liquidity Coverage Ratio	BCBS has identified the list of eligible Level 1 and Level 2 assets to constitute High Quality Liquid Assets. BCBS has proposed phase-in period starting in January 2015 and lasting through 2019.	No proposals.	The EU has outlined outflows and inflows in Capital Requirements Regulation. Further refinements to come from EBA on regulatory standards and to be adopted by the European Commission.
Net Stable Funding Ratio	BCBS intends to review NSFR. The objective is to ensure that banks maintain stable asset-liability profiles over a one-year horizon.	No proposals but expected at later date.	EU plans to adopt NSFR once the BCBS has finalized it.

Source: IMF staff.

Note: BCBS = Basel Committee on Banking Supervision; CET1 = common equity Tier 1; EU = European Union; G-SIB = global systemically important bank; LCR = Liquidity Coverage Ratio; NSFR = Net Stable Funding Ratio. U.S. leverage ratio is defined as Tier 1 capital over on-balance-sheet assets, whereas the U.S. supplementary leverage ratio is defined as Tier 1 capital over total leverage exposure, which includes both on-balance-sheet and certain off-balance-sheet exposures.

*Question 6: The agencies solicit commenters' views on whether a strengthened leverage ratio requirement would enhance the competitive position of U.S. banking organizations relative to foreign banking organizations by enhancing the relative safety of the U.S. banking system. Alternatively, could the proposed strengthened leverage ratio requirement place U.S. banking organizations at a competitive disadvantage relative to foreign banking organizations and if so, in what areas?*

Referring to the IMF's Table 1.3.1 on Bank Regulations across Jurisdictions shows a comparison of the US and EU implementation of the Basel minimum standard. The epicenter of the global financial crisis began in the United States so it is incumbent on the US to be a global leader in strengthening our financial system. The proposed leverage ratio would reduce the risk premium associated with investing in US G-SIBs, thereby making us more competitive internationally.

G-SIBs already enjoy a competitive advantage relative to smaller banks by having access to financing at much lower rates. This unfair competitive advantage hurts smaller banks that are already disadvantaged in international markets. Additionally, it inhibits the diversification of systemic risk that policy makers are trying to encourage.

*Question 7: How would this proposal affect counterparty incentives and behavior?*

I have no comment at this time.

*Question 8: The agencies seek commenters' views on the macroeconomic implications of the proposal, particularly the potential effects the proposal could have on the allocation of credit and the volume of lending. For example, could a strengthened leverage ratio requirement as proposed cause a shift in favor of lending to individuals and businesses as opposed to markets-based activity by banking organizations? If covered BHCs were better capitalized as a group, to what extent would this improve their ability to serve as a source of credit to the economy during periods of economic stress? Conversely, to what extent would the proposal create incentives for banking organizations to shrink or otherwise modify their activities?*

If G-SIBs had to increase their equity requirements as a means to improving their leverage ratio they have a few alternatives; (A) asset liquidation by reducing loans outstanding, (B) recapitalize by replacing liabilities with equity, and (C) asset expansion financed by raising new equity. (Adamati, 2013) Some commenters assert that a G-SIB's only or most likely option is to shrink their balance sheet and reduce credit availability. Why don't banks lend?

*The surveys ask loan officers for the reasons behind tightened lending standards, which allows the construction of a variable that reflects mostly supply constraints. Responses on the tightness of lending conditions may not necessarily reflect "pure" constraints on the supply of credit, such as bank liquidity and capital. The responses could also reflect effects on the standards from changes in borrowers' creditworthiness, the economic outlook, economic uncertainty, and the like. (IMF, 2013)*

Better capitalized banks as a group are in a better position to increase lending in a period of economic stress because they can take advantages of opportunities untenable by inadequately capitalized banks. Such opportunities include acquisitions of weaker banks or capturing a greater market share by banks that retreat from lending in times of economic stress.

*Question 9: What are the incremental costs to banking organizations of the proposed rule compared to the costs of currently anticipated and planned capitalization initiatives?*

Quantifying the incremental costs for BHCs to comply is outside the scope of my graduate studies. I would defer to the Potential Costs section in Docket ID OCC-2013-0008.

I respectfully assert that the cost for banks to comply with the proposal should not carry greater weight when scaled to the benefits of reduced risk to the broader economy. I realize that the benefits of a more stable financial system are hard to quantify. The effects of an unstable financial system have led many Eurozone countries to pursue an aggressively austere fiscal policy. The US had a glimpse of an austerity agenda with the 2011 Budget Control Act; resulting in a measurable effect in reducing US GDP over the next ten years. The long term effects of decreased economic growth pale in comparison to incremental costs for eight US G-SIBs. Banks stand to benefit from a growing US economy as well.

*Question 10: The agencies are interested in comment on the appropriate measure of capital that should be used as the numerator of the supplementary leverage ratio. Among the many measures of capital used by banks, regulators and the market, the agencies considered the following measures: (1) Common equity tier 1 capital, (2) tier 1 capital, (3) total capital, and (4) tangible equity (as these terms are defined in the agencies' capital regulations as of the date of the issuance of this proposed rule, including the 2013 revised capital approaches). What are the advantages and disadvantages of each of these as well as alternative measures?*

The tangible equity measure is preferable because it is the most simple, transparent, and useful measure of capital available to absorb losses as compared to the other measures.

*Question 11: What, if any, alternatives to the definition of total leverage exposure should be considered and why?*

The agencies should strongly consider using the IFRS method to include off-balance sheet derivatives exposure into the total leverage calculations. This will lead to greater consistency internationally and provides a more transparent view of a firm's position. See (Hoenig, 2013) and Appendix A (Table 1 of Hoenig's research) on the differences between GAAP and IFRS rules have on leverage ratios.

*Question 12: In light of the proposed enhanced leverage requirement and ongoing standardized risk-based capital floors, should the agencies consider, in some future regulatory action, simplifying or eliminating portions of the advanced approaches rule if they are unnecessary or duplicative? Are there opportunities to simplify the standardized risk-based capital framework that would be consistent with safety and soundness or other policy objectives?*

I have no comment at this time. I will be following this issue to provide more substantive comments at a later date.

*Question 13: The proposed scope of application is U.S. top-tier BHCs with more than \$700 billion in total assets or more than \$10 trillion in assets under custody and their subsidiary IDIs. Should the proposed requirements also be applied to other advanced approaches banking organizations? Why or why not? Should all IDI subsidiaries of a covered BHC be subject to the proposed well-capitalized*

*standard, and if not, why? Please provide specific factors and the associated rationale the agencies should consider in establishing any exemption from the proposed well-capitalized standard.*

I have no comment at this time. I will be following this issue to provide more substantive comments at a later date.

## **References (please excuse the draft format)**

DEPARTMENT OF TREASURY Office of the Comptroller of the Currency  
12 CFR Parts 6 [Docket ID OCC-2013-0008] RIN 1557-AD69  
Regulatory Capital Rules: Regulatory Capital, Enhanced Supplementary Leverage Ratio Standards for Certain Bank Holding Companies and Their Subsidiary Insured Depository Institutions

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Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Risk-weighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule, and Market Risk Capital Rule

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<http://www.gsb.stanford.edu/sites/default/files/fallacies-facts-myths-admati.pdf>

Global Financial Stability Report (October 2013) Transition Challenges to Stability  
International Monetary Fund <http://www.imf.org/External/Pubs/FT/GFSR/2013/02/pdf/text.pdf>  
Page 54: The authors of this box are Ana Carvajal, Marc Dobler, Ellen Gaston, Eija Holttinen, Fabiana Melo, Mala Nag, Oana Nedelescu, Nobuyasu Sugimoto, and Mamoru Yanase. 1For details, see the August 2013 BCBS progress report on Basel III implementation (www.bis.org/publ/bcbs260.pdf ).

(IMF, 2013) Global Financial Stability Report (October 2013) Transition Challenges to Stability  
International Monetary Fund, Page 107 <http://www.imf.org/External/Pubs/FT/GFSR/2013/02/pdf/text.pdf>

Hoenig, Thomas (2013) Basel III Capital: A Well-Intended Illusion April 9, 2013  
<http://fdic.gov/news/news/speeches/spapr0913.pdf>

Table 1 in the Appendix is originally found in Hoenig, Thomas (2013) Basel III Capital: A Well-Intended Illusion presentation at the International Association of Deposit Insurers – 9-APR-13

# Table 1: Capitalization Ratios for Global Systemically Important Banks

Data as of Fourth Quarter 2012

Institution <sup>1</sup>	Basel Risk-Based Capital			Tangible Capital				Components of Tangible Capital				Price-to-Book	
	Tier 1 Capital <sup>2</sup> (\$Billions)	Risk-Weighted Assets (\$Billions)	Tier 1 Capital Ratio <sup>3</sup> (Percent)	GAAP		IFRS ESTIMATE <sup>4</sup>		Total Equity <sup>6</sup> (\$Billions)	Goodwill (\$Billions)	Other Intangibles (\$Billions)	Deferred Tax Assets (\$Billions)	Price-to-Book Ratio <sup>7</sup> (Percent)	Price-to-Adjusted Tangible Book Ratio <sup>7</sup> (Percent)
				Total Assets (\$Billions)	Leverage Ratio <sup>5</sup> (Percent)	Total Assets (\$Billions)	Leverage Ratio <sup>5</sup> (Percent)						
<b>U.S. G-SIBs</b>													
Bank of America	155	1,206	12.89	2,212	5.79	3,540	3.55	237	70	13	33	0.57	1.22
Bank of New York Mellon	17	111	15.02	359	4.02	381	3.77	36	18	5	0	0.85	2.40
Citigroup	137	971	14.06	1,865	5.61	2,878	3.57	189	26	8	56	0.64	1.24
Goldman Sachs	67	400	16.75	939	7.07	1,707	3.87	76	4	1	5	0.88	1.03
JPMorgan Chase	160	1,270	12.59	2,359	5.89	3,947	3.48	204	48	10	11	0.86	1.33
Morgan Stanley	54	307	17.72	781	5.79	1,749	2.55	62	7	4	8	0.62	0.89
State Street	14	72	19.13	222	5.78	228	5.64	21	6	3	0	1.06	1.82
Wells Fargo	127	1,077	11.75	1,423	8.13	1,485	7.78	158	26	20	0	1.24	1.82
<b>Average U.S. G-SIBs</b>	<b>730</b>	<b>5,415</b>	<b>13.49</b>	<b>10,160</b>	<b>6.17</b>	<b>15,914</b>	<b>3.88</b>	<b>983</b>	<b>204</b>	<b>63</b>	<b>113</b>	<b>0.85</b>	<b>1.28</b>
<b>Foreign G-SIBs</b>													
Banco Santander (Spain)	80	716	11.17			1,631	2.97	108	32	4	25	0.84	2.35
Bank of China Limited (China)	121	1,149	10.54			2,009	6.53	136	0	2	3	0.94	0.98
Barclays (UK)	82	611	13.35			2,354	3.08	89	8	4	5	0.60	0.75
BBVA (Spain)	46	423	10.77			819	4.04	56	9	3	13	0.91	1.67
BNP Paribas (France)	97	709	13.63			2,451	3.47	111	14	3	10	0.67	0.92
BPCE Group (France)	60	491	12.17			1,474	4.27	70	5	2	0	...	...
Crédit Agricole Group (France)	79	617	12.85			2,580	2.72	98	19	2	7	...	...
Deutsche Bank (Germany)*	65	458	14.19			2,734	1.47	72	20	0	12	0.50	0.92
HSBC (UK)	151	1,124	13.44			2,693	5.16	175	21	8	8	1.13	1.44
ING Bank (Netherlands)	51	358	14.35			1,074	4.11	48	2	1	2	...	...
Nordea bank (Sweden)	31	276	11.17			870	3.65	36	3	1	0	1.03	1.18
Royal Bank of Scotland (UK)	90	726	12.43			2,073	3.72	103	0	21	5	0.53	0.71
Société Générale (France)	52	416	12.50			1,607	2.84	61	7	2	7	0.48	0.66
Standard Chartered (UK)	41	302	13.45			637	5.77	44	7	1	1	1.36	1.65
UBS (Switzerland)	44	205	21.29			1,343	2.52	49	6	1	9	1.17	1.71
UniCredit (Italy)	63	549	11.44			1,191	5.57	85	15	5	n/a	0.34	0.46
<b>Average Foreign IFRS</b>	<b>1,151</b>	<b>9,129</b>	<b>12.61</b>			<b>27,540</b>	<b>3.70</b>	<b>1,342</b>	<b>168</b>	<b>61</b>	<b>106</b>	<b>0.84</b>	<b>0.98</b>
<b>Other Foreign G-SIBs</b>													
Credit Suisse (Switzerland; CHF, U.S. GAAP)	37	239	15.56	986	3.69			45	9	0	n/a	...	...
Mitsubishi UFJ FG (Japan; JPY, Local GAAP)	136	1,114	12.22	2,672	5.07			151	0	13	4	0.68	0.79
Mizuho FG (Japan; JPY, Local GAAP)	81	633	12.75	2,064	3.66			86	0	6	5	0.85	1.06
Sumitomo Mitsui FG (Japan; JPY, Local GAAP)	84	654	12.81	1,692	4.76			95	0	10	5	0.81	1.06
<b>Average All Foreign G-SIBs</b>	<b>1,489</b>	<b>11,769</b>	<b>12.65</b>	<b>34,954</b>	<b>3.85</b>			<b>1,719</b>	<b>177</b>	<b>90</b>	<b>121</b>	<b>0.83</b>	<b>1.02</b>
<b>Average U.S. BHC by Size Group<sup>8</sup></b>													
U.S. G-SIBs	730	5,415	13.49	10,160	6.17	15,914	3.88	983	204	63	113	0.85	1.28
Ten Largest Non-G-SIBs <sup>9</sup>	171	1,499	11.41	1,913	8.21	1,927	8.15	226	57	12	6	0.94	1.59
Ten Largest Less Than \$50 Billion <sup>10</sup>	24	191	12.85	293	7.91	293	7.91	33	8	1	2	1.07	1.51
Ten Largest Less Than \$1 Billion <sup>10</sup>	1	7	13.40	10	8.67	10	8.67	1	0	0	0	...	...

Source: Bankscope (Data updated as of April 4, 2013), Bloomberg LP, Federal Reserve Y-9C Reports, International Monetary Fund, and 10-Q reports.

# Table 1 (continued): Capitalization Ratios for Global Systemically Important Banks

## Notes:

<sup>1</sup> Global systemically important banks (G-SIBs) are defined by the Financial Stability Board and include eight U.S. bank holding companies (BHC).

<sup>2</sup> Tier 1 Capital is equity capital less unrealized gains on available-for-sale debt securities, unrealized losses on available-for-sale equity securities, disallowed preferred stock, disallowed goodwill, disallowed servicing assets, disallowed deferred tax assets, and other tier 1 capital components.

<sup>3</sup> Tier 1 capital ratios and underlying data are calculated and reported under Basel I standards for U.S. Banks, under the China Banking Regulation Commission regulations for the Bank of China, under Basel II for Banco Santander, BBVA, ING Bank, Mitsubishi UFJ FG, Mizuho FG, Nordea Bank, Royal Bank of Scotland, Standard Chartered, Sumitomo Mitsui FG, and Unicredit, and under Basel 2.5 for Barclays, BNP Paribas, BPCE Group, Credit Agricole, Credit Suisse, Deutsche Bank, HSBC, Societe Generale and UBS.

<sup>4</sup> Differences in accounting requirements for netting and offsetting of assets and liabilities result in significant differences in banks' total assets. The ability to offset under International Financial Reporting Standards (IFRS) is limited in comparison with Generally Accepted Accounting Principles (GAAP), especially for derivatives traded with the same counterparty under an International Swaps and Derivatives Association (ISDA) Master Netting Agreement. U.S. GAAP permits the netting of derivative receivables and payables, and the related cash collateral received and paid when a legally enforceable master netting agreement exists between a firm and a derivative counterparty. U.S. GAAP discloses gross derivative assets and liabilities and the offset amount applied to derivatives in the notes to the consolidated financial statements rather than in the consolidated balance sheet. To narrow the difference in total assets between IFRS and U.S. GAAP reporting institutions, the U.S. G-SIBs IFRS estimates follow the methodology used by ISDA in its Netting and Offsetting Report (May 2012, <http://www2.isda.org/functional-areas/research/studies/>) and adds the disclosed offsetting amount applied to derivatives back to total assets in order to calculate total assets. Total assets are as reported in the consolidated balance sheet while the offset applied to derivatives is as reported in the notes to the consolidated financial statements on derivatives in each firm's 10-Q report.

<sup>5</sup> The Leverage Ratio is the ratio of adjusted tangible equity to adjusted tangible assets. Adjusted tangible equity, adjusted tangible assets, and adjusted tangible book subtract goodwill, other intangibles, and deferred tax assets.

<sup>6</sup> Equity Capital is the basic GAAP measure of net worth, defined as total assets minus total liabilities.

<sup>7</sup> Median price-to-book ratios and price-to-adjusted tangible book ratios are used instead of averages for subgroups and for U.S. BHC size groups. Data are not available for six bank holding companies with assets less than \$1 billion, as well as for BPCE Group, Credit Agricole Group, and ING Bank.

<sup>8</sup> Bank holding companies that are owned by a foreign parent or reported a net loss in fourth quarter 2012, and thrift holding companies that did not file a full FRY-9C report as of fourth quarter 2012 were excluded.

<sup>9</sup> Six of the ten largest non-G-SIB (American Express, KeyCorp, Northern Trust, PNC, Suntrust and U.S. Bancorp) reported the fair value of their derivative positions in their 10-Q reports. The leverage ratio for these six banks is 8.53 percent under U.S. GAAP and 8.47 percent under the IFRS estimate. The 6 basis point difference is used to adjust the leverage ratio for the entire group from 8.21 percent to 8.15 percent and to estimate total assets under the IFRS estimate. The remaining four bank holding companies reported minimal derivative exposure.

<sup>10</sup> The ten largest U.S. bank holding companies with assets less than \$50 billion and the ten largest U.S. bank holding companies with assets less than \$1 billion reported de minimis derivative exposures. We assume that total assets and the adjusted tangible equity to adjusted tangible assets ratio are essentially the same under U.S. GAAP and the IFRS estimate.