Public Comments on Resolution of Systemically Important Financial Institutions: Single Point of Entry Strategy

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Comment: OCC, you cannot cover for “unexpected losses” by using the perceptions of “expected losses” Banks already cover reasonably well for the perceived risks of “expected losses”, by means of interest rates, size of exposure and other terms. And so capital requirements are there primarily to create a reasonable buffer against any “unexpected losses”. What does not make any sense though is, as is done, to base the risk-weights which determine those capital requirements on the same perceptions of expected losses. That causes the risk perceptions for “expected losses” to be considered twice and the risks of unexpected losses being ignored. And this is especially wrong when the capital requirements are portfolio invariant, as this ignores the benefits of diversification for what is perceived as “risky”, and the dangers of excessive concentration for what is perceived as “safe”. With this risk-weighting, banks are allowed to obtain much higher risk-adjusted returns on their equity when lending to The Infallible than when lending to The Risky. And that introduces a serious distortion that affects the allocation of bank credit in the real economy and carries grave consequences. It also introduces a discrimination that does not seem to be compatible with the Equal Credit Opportunity Act (Regulation B)