United States Senate
WASHINGTON, DC 20510

June 19, 2020

The Honorable Randal K. Quarles
Vice Chairman for Supervision
Board of Governors of the Federal Reserve System
20th St and Constitution Avenue NW
Washington, D.C. 20551

The Honorable Jelena McWilliams
Chairman
Federal Deposit Insurance Corporation (FDIC)
550 17th Street, N.W.
Washington, D.C. 20429

The Honorable Brian P. Brooks
Acting Comptroller of the Currency
Office of the Comptroller of the Currency
400 7th St. SW
Washington, DC 20219

Dear Vice Chair Quarles, Chairman McWilliams, and Acting Comptroller Brooks:

We write concerning recent changes implemented by the Federal Reserve Board of Governors (Fed), Federal Deposit Insurance Corporation (FDIC), and Office of the Comptroller of the Currency (OCC) to weaken the Supplementary Leverage Ratio (SLR), a critical regulatory requirement for the largest banks. The SLR is a key component of the regulatory framework that Congress developed to protect Americans from another financial crisis.[1] The interim rule that you jointly released to weaken this requirement amidst an economic crisis is dangerous and puts the economy and hardworking families at risk.

Capital requirements are a critical tool of financial regulators to ensure that banks maintain a cushion against losses and can continue to serve the real economy during periods of financial stress. Almost 500 banks failed as a result of the last banking crisis, resulting in $73 billion in losses to the FDIC's Deposit Insurance Fund,[2] due to banks' failure to maintain adequate levels of capital in the years leading up to the crisis.[3] Following the crisis, financial regulators took steps to strengthen these regulations, and one of the ways they did so was through the SLR. The SLR applies to the largest financial institutions and requires them to fund at least three percent of

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[1] Board of Governors of the Federal Reserve System, "Federal Reserve Board approves final rule to help ensure banks maintain strong capital positions," July 02, 2013, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130702a.htm.
[2] Federal Deposit Insurance Corporation, "Crisis and Response: An FDIC History, 2008-2013," 2017, https://www.fdic.gov/bank/historical/crisis/overview.pdf.
[3] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, "Regulators temporarily change the supplementary leverage ratio to increase banking organizations' ability to support credit to households and businesses in light of the coronavirus response," May 15, 2020, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20200515a.htm.

their total on-balance sheet assets and off-balance sheet exposures with equity capital. [4][5] The SLR rule was finalized in 2014[6], and banks and their lobbyists have opposed it ever since while pushing for its relaxation or removal.[7] Last month, you partially granted their wish.

On May 15, 2020, the Fed, FDIC, and OCC released an interim final rule (IFR), allowing banks to exclude certain assets from the SLR calculation until March 2021.[8] Specifically, banks are allowed to exclude deposits held at Federal Reserve Banks and U.S. Treasuries. This change will lower capital requirements at the largest, riskiest banks by $55 billion.[9]

Instead, the federal financial regulators should be taking action to solidify bank capital requirements, not weakening them amidst an economic crisis. Banks are currently “battening down the hatches to deal with an expected surge in loan losses as the pandemic casts serious doubts over the capacity of consumers and companies to pay their debt.”[10] As banks’ balance sheets continue to come under pressure in the coming months, this is exactly the wrong time to reduce the amount of capital that banks will have to absorb these losses.

We are troubled by the release of this rule for multiple reasons. First, the rule goes well-beyond the purpose stated in the Federal Register. The IFR states that the agencies are making this change “in order to facilitate depository institutions’ significant increase in reserve balances resulting from the Federal Reserve’s asset purchases and the establishment of various programs to support the flow of credit to the economy, as well as the need to continue to accept exceptionally high levels of customer deposits.”[11] In short, the agencies are arguing that this rule is necessary to accommodate changes to banks’ balance sheets resulting from financial market

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[4] *Id.*
[5] Specifically, the SLR applies to all advanced approaches banks, which are defined as banks with at least $250 billion in total consolidated assets or at least $10 billion in total on-balance sheet foreign exposure. Congressional Research Service, “Overview of the Prudential Regulatory Framework for U.S. Banks: Basel III and the Dodd-Frank Act,” Darryl E. Getter, July 27, 2016, https://www.crs.gov/reports/pdf/R44573.
[6] Federal Reserve Board of Governors, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, “Agencies adopt supplementary leverage ratio final rule,” September 03, 2014, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20140903b.htm.
[7] American Banker, “Raising Leverage Ratio Weakens Bank Liquidity,” Hugh Carney, June 28, 2013, https://www.americanbanker.com/opinion/leverage-ratio-harms-banks-role-as-safe-haven-in-a-crisis.
[8] The Fed previously made this change at the bank holding company level in April. Board of Governors of the Federal Reserve System, “Federal Reserve Board announces temporary change to its supplementary leverage ratio rule to ease strains in the Treasury market resulting from the coronavirus and increase banking organizations’ ability to provide credit to households and businesses,” April 01, 2020, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20200401a.htm.
[9] Office of the Comptroller of the Currency , Board of Governors of the Federal Reserve System, and Federal Deposit Insurance Corporation, Federal Register Notice,” Regulatory Capital Rule: Temporary Exclusion of U.S. Treasury Securities and Deposits at Federal Reserve Banks From the Supplementary Leverage Ratio for Depository Institutions,” June 01, 2020, https://www.fdic.gov/news/board/2020/2020-05-14-notational-fr.pdf.
[10] Financial Times, “US banks brace for surge in loan losses,” Laura Noonan, April 18, 2020, https://www.ft.com/content/87189e79-a442-44b9-a699-7bce47b5bc64.
[11] Office of the Comptroller of the Currency , Board of Governors of the Federal Reserve System, and Federal Deposit Insurance Corporation, Federal Register Notice,” Regulatory Capital Rule: Temporary Exclusion of U.S. Treasury Securities and Deposits at Federal Reserve Banks From the Supplementary Leverage Ratio for Depository Institutions,” June 01, 2020, https://www.fdic.gov/news/board/2020/2020-05-14-notational-fr.pdf.

developments associated with the coronavirus disease 2019 (COVID-19) pandemic. However, you exempted *all* of these assets from the SLR calculation,[12] including those that banks held well before the crisis. Therefore, this rule goes far beyond providing institutions relief to accommodate the inflow of deposits and increases in reserve balances as a result of the economic response to the coronavirus crisis.

Second, the rule allows banks, with regulators' permission, to continue to pay out billions of dollars in dividends to shareholders and executives – reducing capital reserves in a way that does nothing to help bank customers or financial stability. Even if one accepts the premise that banks needed to reduce capital buffers in order to support lending to households and businesses, it is unacceptable that regulators have not yet prohibited banks from reducing capital buffers in order to enrich their shareholders and executives. The IFR allows banks that opt into the regulatory rollback to continue to pay dividends, requiring only that they seek preapproval from their primary financial regulator. [13] This weak provision is woefully insufficient.

Every million dollars a bank distributes to its shareholders eliminates tens of millions of dollars[14] that could otherwise be used to support communities in need during this economic crisis. Before the economic implications of COVID-19 were evident, participants in the Federal Reserve's Open Market Committee (FOMC) meeting in January acknowledged that "planned increases in dividend payouts by large banks and the associated decline in capital buffers might leave those banks with less capacity to weather adverse shocks—which could have negative implications for the economy—or that lower bank capital ratios could be associated with greater tail risks to GDP [Gross Domestic Product] growth."[15]

There is no justifiable reason to relax a key safety and soundness restraint by arguing that it is necessary for banks to support lending while simultaneously allowing banks to distribute capital to enrich their shareholders. And multiple former financial regulators, including former Federal

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[12] Center for American Progress, "Bank Capital and the Coronavirus Crisis," Gregg Gelzinis, May 12, 2020, https://www.americanprogress.org/issues/economy/reports/2020/05/12/484722/bank-capital-coronavirus-crisis/.

[13] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, "Regulators temporarily change the supplementary leverage ratio to increase banking organizations' ability to support credit to households and businesses in light of the coronavirus response," May 15, 2020, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20200515a.htm.

[14] At current capital ratios, an extra dollar in capital can be leveraged to support more than $15 in lending. Center for American Progress, "Bank Capital and the Coronavirus Crisis," Gregg Gelzinis, May 12, 2020, https://www.americanprogress.org/issues/economy/reports/2020/05/12/484722/bank-capital-coronavirus-crisis/.

[15] Federal Reserve System, "Minutes of the Federal Open Market Committee," January 28-29, 2020, https://www.federalreserve.gov/monetarypolicy/files/fomcminutes20200129.pdf.

Reserve officials Chairman Ben Bernanke[16], Chair Janet Yellen[17], Governor Dan Tarullo[18], and FDIC Board Member Tom Hoenig[19] have spoken out regarding your failure to enact this common-sense requirement.

Third, and most importantly, this change, by reducing the amount of capital at the largest banks, makes our financial system weaker and could harm our recovery from this crisis. Banks entered this crisis in a stronger financial position compared to the last crisis – in large part because of the post-2008 reforms.[20] It is perplexing that you are weakening banks' financial positions just as "financial sector vulnerabilities are likely to be significant in the near term."[21] Not only are banks that enter into a financial crisis with strong capital buffers more likely to be able to withstand losses, they are also in a better position to lend to businesses and consumers.[22] According to former FDIC Vice Chair Hoenig, "having a stronger capital base actually provides a better base for lending…for every dollar of capital [banks] retain, there's approximately $15 of loans that they can make."[23] But your proposed changes could reduce bank capital by tens of

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[16] "We didn't do that in 2008. I think in retrospect, you know, that might have been a mistake because obviously in the end many banks were short of capital and putting out dividends reduces the amount of capital. So I think there is a case for asking banks generally to be very cautious about dividend payouts and share buybacks."–*Ben Bernanke, Member (2002-05) and Chairman (2006-2014), Board of Governors of the Federal Reserve System,* The Brookings Institution, "Former Fed Chair Ben Bernanke Weighs in on the Economic Response to COVID-19," April 7, 2020, https://www.brookings.edu/wp-content/uploads/2020/04/20200407_covid19_bernanke_transcript.pdf.

[17] "We learned that we let way too much money out the door in that crisis…We don't know where this is going, this is really a tail event and a great threat to the country." - Janet Yellen, *Vice Chair (2010-14) and Chair (2014-2018), Board of Governors of the Federal Reserve System,* The New York Times, "Fed Gives Banks a Break to Keep Markets Calm, Asking for Little in Return," Jeanna Smialek, April 15, 2020, https://www.nytimes.com/2020/04/15/business/economy/fed-banks-dividends-virus.html.

[18] "Allowing some banks to continue dividends in 2008 further eroded their capital just when it was needed most." - Dan Tarullo, *Member (2009-2017) Board of Governors of the Federal Reserve System,* Wall Street Journal, "Fed Unlikely to Order Big U.S. Banks to Suspend Dividends," Andrew Ackerman and Nick Timiraos, April 3, 2020, https://www.wsj.com/articles/fed-unlikely-to-order-big-u-s-banks-to-suspend-dividends-sources-11585941449.

[19] "I would encourage them to delay dividends or cease dividends temporarily. There are some benefits. People say it's not enough to make a difference, but I think perhaps it is enough to matter." - *Tom Hoenig, Vice Chairman (2012-2018), Federal Deposit Insurance Corporation,* Mercatus Center, "Thomas Hoenig on Bank Capitalization and Fed Policy after COVID-19," David Beckworth, May 25, 2020, https://www.mercatus.org/bridge/podcasts/05252020/thomas-hoenig-bank-capitalization-and-fed-policy-after-covid-19.

[20] Board of Governors of the Federal Reserve System, " Financial Stability Report," May 2020, https://www.federalreserve.gov/publications/files/financial-stability-report-20200515.pdf.

[21] *Id.*

[22] Mercatus Center, "Thomas Hoenig on Bank Capitalization and Fed Policy after COVID-19," David Beckworth, May 25, 2020, https://www.mercatus.org/bridge/podcasts/05252020/thomas-hoenig-bank-capitalization-and-fed-policy-after-covid-19.

[23] Mercatus Center, "Thomas Hoenig on Bank Capitalization and Fed Policy after COVID-19," David Beckworth, May 25, 2020, https://www.mercatus.org/bridge/podcasts/05252020/thomas-hoenig-bank-capitalization-and-fed-policy-after-covid-19.

billions of dollars.[24] Both of the former Chairs of the FDIC Sheila Bair[25] and Marty Gruenberg[26], who saw firsthand the devastation caused by the bank failures during the last crisis, have vocally opposed the IFR.

We are baffled that the federal financial regulators granted a long-desired piece of deregulation to the nation's largest banks without sufficient justification to do so, and despite the risks to economic growth and financial stability. There will no doubt be calls to extend this relaxation of a key capital requirement beyond its current expiration date of March 2021. Given the lack of justification and analysis in issuing the IFR, we are concerned that you could similarly extend it without justification when it is set to expire. We are also troubled by requests for Congress to pass legislation to allow regulators to similarly relax the Tier 1 leverage ratio.[27] Unlike the SLR, the Tier 1 leverage ratio applies to all insured depository institutions.[28] Removing this safeguard for the financial system would be a grave error. Congress should not grant this change, and regulators should not try to find a loophole to do it themselves.

To the families who were affected by the last financial crisis, capital requirements were not some abstract ratio found in the pages of the Federal Register: they represented the difference between families and workers losing their homes, jobs, and livelihoods. The same is true as the country faces a new economic crisis caused by the COVID-19 pandemic. You should reverse this rule and immediately take action to preserve capital at financial institutions to ensure that these institutions are stable and can provide needed assistance to their customers and to the economy as a whole.

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[24] Office of the Comptroller of the Currency , Board of Governors of the Federal Reserve System, and Federal Deposit Insurance Corporation, Federal Register Notice," Regulatory Capital Rule: Temporary Exclusion of U.S. Treasury Securities and Deposits at Federal Reserve Banks From the Supplementary Leverage Ratio for Depository Institutions," June 01, 2020, https://www.fdic.gov/news/board/2020/2020-05-14-notational-fr.pdf.

[25] "Very disappointed that the FDIC and OCC followed the Fed to weaken the supplementary leverage ratio, a key constraint on mega-banks use of excessive leverage… Allowing banks to reduce capital minimums now is the wrong move. The Fed itself has warned of dire economic conditions that could result in significant losses for banks. They should be building, not reducing, capital, to remain solvent and lending through this crisis." –S*heila Bair, Chairman (2006-2011), Federal Deposit Insurance Corporation*, Tweets from Sheila Bair, May 17, 2020, https://twitter.com/SheilaBair2013/status/1262186239953862656.

[26] "Now is not the time to reduce significantly the capital of the most systemically important U.S. banks in order to facilitate financial market liquidity. Both are essential to the stability of the financial system and the functioning of the economy. We learned the hard way during the 2008 financial crisis the importance of preserving loss absorbing leverage capital at systemically important banks. The capital of U.S. banks may look strong today, but that profile may change drastically over the next 12 months as credit losses mount"- *Martin Gruenberg, Board Member (2005-present) and Chairman (2005-06, 2011-2018) Federal Deposit Insurance Corporation,* Statement by Martin J. Gruenberg on the Interim Final Rule: Temporary Exclusion of U.S. Treasury Securities and Deposits at Federal Reserve Banks from the Supplementary Leverage Ratio, May 15, 2020, https://www.fdic.gov/news/news/speeches/spmay1520.html.

[27] Letter from Vice Chair for Supervision Randal Quarles to Chairman Crapo, April 22, 2020, https://www.banking.senate.gov/imo/media/doc/Fed%20Response%20to%20Crapo%204.8.20%20Letter.pdf.

[28] Congressional Research Service, "Enhanced Prudential Regulation of Large Banks," Marc Labonte, May 6, 2019, https://www.crs.gov/reports/pdf/R45711,

Sincerely,

Elizabeth Warren
United States Senator

Sherrod Brown
United States Senator