JEB HENSARLING, TX, CHAIRMAN

United States House of Representatives
Committee on Financial Services
Washington, D.C. 20515

MAXINE WATERS, CA, RANKING MEMBER

September 20, 2018

The Honorable Jerome Powell
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave, NW
Washington, D.C. 20551

Dear Chairman Powell,

It has come to our attention that many of our colleagues from across the aisle on the Financial Services Committee wrote to the Board of Governors of the Federal Reserve System ("Federal Reserve") expressing concerns that the Global Systemically Important Banks ("G-SIBs") currently face "unwarranted capital burdens" through the G-SIB capital surcharge, and urge the Federal Reserve to "recalibrate" or otherwise reduce the surcharge.[1] They argue – without providing empirical evidence – the G-SIB capital surcharge allegedly puts U.S. banks at a competitive disadvantage and is duplicative of other post-crisis reforms. We urge you to reject their advice.

The Dodd-Frank Wall Street Reform and Consumer Protection Act and related regulatory reforms, including the G-SIB capital surcharge, have made the financial system much safer following the 2007-2009 financial crisis. Vice Chairman for Supervision Randal Quarles testified before our Committee in April that the largest banks have more than doubled their loss-absorbing capital, increasing it by more than $700 billion.[2] While other post-crisis reforms, like stronger leverage limits and resolution planning, have improved the regulatory framework, the G-SIB capital surcharge is an important complement to, not duplicative of, these reforms to address the complex set of risks posed by G-SIBs. The Basel Committee on Banking Supervision previously explained, "[t]here is no single solution to the negative externalities posed by G-SIBs. Hence the official community is addressing the issues through a multipronged approach."[3]

In addition, the G-SIB capital surcharge helps level the playing field for thousands of community banks as it only applies to eight of the largest banks, which have a combined $10.7 trillion of assets, or approximately half of total U.S. depository assets.[4] As former Chair Janet Yellen explained when the Federal Reserve finalized the G-SIB capital surcharge rule with your support, "[a] key purpose of the capital surcharge is to require the firms themselves to bear the costs that their failure would impose on others... they must either hold substantially more capital, reducing the likelihood that they will fail, or else they must shrink their systemic footprint, reducing the harm that their failure would do to our financial system. Either outcome would enhance financial stability."[5]

The evidence shows that higher capital standards and related regulatory improvements are not harming U.S. banks. In fact, banks are making record profits, on average of $167 billion annually the last three years. And that was before Congressional Republicans slashed the corporate tax rate for U.S. G-SIBs, giving the largest banks a windfall of more than $15 billion this year, and billions more to come in the years to follow.[6] In fact, the industry made a record $60 billion in profits in just the second quarter of 2018.[7]

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[1] https://www.americanbanker.com/news/house-republicans-ask-fed-to-lower-capital-requirements-for-megabanks
[2] https://financialservices.house.gov/uploadedfiles/hhrg-115-ba00-wstate-rquarles-20180417.pdf
[3] https://www.bis.org/publ/bcbs207cn.pdf
[4] https://www.treasury.gov/press-center/press-releases/Documents/A%20Financial%20System.pdf
[5] https://www.federalreserve.gov/newsevents/pressreleases/bcreg20150720a.htm
[6] https://thinkprogress.org/goldman-report-tax-plan-759ec84f8eee/
[7] https://www.fdic.gov/bank/analytical/qbp/

As banks have increased capital and earned record profits, their lending to businesses has increased by 80 percent since 2010,[8] and the economy has had 101 consecutive months of private sector job growth since 2010.[9] U.S banks are also competing well internationally. One headline in the *Financial Times* read, "European banks fall further behind their US rivals."[10] Similarly, you observed a few months ago, "[a]s you look around the world, U.S. banks are competing very, very successfully. They're very profitable. They're earning good returns on capital.... So I'm looking for the case, for some kind of evidence that... regulation is holding them back, and I'm not really seeing that case as made at this point."[11]

Finally, it is worth noting Federal Reserve Governor Brainard, the Federal Deposit Insurance Corporation ("FDIC"), community banks, and experts from across the political spectrum have voiced strong objections to the Federal Reserve's proposed rule to reduce the leverage limitation on the depository institutions of G-SIBs.[12] The last thing the Federal Reserve should do is ignore these concerns and weaken G-SIB requirements that help protect the broader U.S. economy from another financial crisis. As Governor Brainard has cautioned, "[a]t 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."[13]

Strong capital requirements are the cornerstone of an effective regulatory regime that promotes financial stability while supporting stable economic growth. The financial crisis a decade ago taught a painful lesson about how damaging an undercapitalized financial system can be—a recent Federal Reserve study estimated the crisis cost every American about $70,000.[14] Thus, we urge the Federal Reserve not to forget that costly lesson and maintain the appropriately tough capital requirements on G-SIBs.

Sincerely,

Maxine Waters

Ed Perlmutter

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[8] https://fred.stlouisfed.org/series/BUSLOANS

[9] https://www.bls.gov/news.release/empsit.nr0.htm.

[10] https://www.ft.com/content/4962c1c8-4f9f-11e8-a7a9-37318e776bab. Also see https://www.economist.com/special-report/2017/05/06/american-banks-have-recovered-well-many-european-ones-much-less-so.

[11] https://subscriber.politicopro.com/financial-services/whiteboard/2018/04/powell-doesnt-see-need-to-loosen-rules-on-biggest-banks-967593. Furthermore, the Federal Reserve's own research has indicated capital rules are generally on the lower end of requirements that best balances benefits associated with mitigating systemic risk with a bank's funding costs (e.g., see https://doi.org/10.17016/FEDS.2017.034).

[12] https://www.fdic.gov/news/news/speeches/spapr1218.html, https://www.wsj.com/articles/relaxing-bank-capital-requirements-would-risk-another-crisis-1524784371, https://www.icba.org/docs/default-source/icba/advocacy-documents/letters-to-regulators/18-06-012_gsibltr.pdf?sfvrsn=0&sfvrsn=0, and https://www.mercatus.org/publications/comment-proposed-rulemaking-regulatory-capital-rules.

[13] https://www.federalreserve.gov/newsevents/speech/brainard20180403a.htm

[14] https://www.frbsf.org/economic-research/publications/economic-letter/2018/august/financial-crisis-at-10-years-will-we-ever-recover/

CC: The Honorable Randal Quarles, Vice Chairman for Supervision
The Honorable Lael Brainard, Governor