Federal Reserve and OCC Propose Changes to the Enhanced Supplementary Leverage Ratio Standard

May 7, 2018

On April 11, 2018, the Federal Reserve Board ("FRB") and the Office of the Comptroller of the Currency ("OCC") proposed to amend the enhanced supplementary leverage ratio ("eSLR") standards for U.S. global systemically important bank holding companies ("GSIBs") and their insured depository institution ("IDI") subsidiaries.
Under the proposal, the eSLR would change from a fixed amount to 50% of the percentage that applies pursuant to the FRB's GSIB surcharge methodology. The FRB also proposed several changes to the FRB's total loss-absorbing capacity ("TLAC") and long-term debt requirements. The comment period for the proposed changes closes on May 21, 2018.

IMPACT OF PROPOSED MODIFICATIONS

Currently, the eSLR is the binding constraint for four of the eight U.S. GSIBs. Under the proposal, the FRB and OCC (the "agencies") believe only one of the eight U.S. GSIBs would have the eSLR as its most binding capital requirement. Further, the agencies believe there would be a $9 billion aggregate decrease in the amount of tier 1 capital that GSIBs would have to hold to avoid limitations on capital distributions and discretionary bonus payments under the agencies' regulatory capital rules. Despite this significant decrease, the agencies estimate that the amount of tier 1 capital required across the GSIBs to meet requirements under both the capital plan rule and the capital rules would fall only by $400 million.

For covered IDIs, the eSLR currently is the most binding tier 1 capital requirement for all eight lead IDI subsidiaries of the GSIBs; the agencies believe this will be the case for only three lead IDIs under the proposed changes. The agencies also believe there would be a $121 billion aggregate decrease in the amount of tier 1 capital required under the proposed rule to be considered "well capitalized" under the agencies' prompt corrective action ("PCA") framework.

OVERVIEW OF PROPOSED CHANGES

Current Capital Rules

At present, all subject banking organizations must maintain a minimum tier 1 leverage ratio of 4%. In addition, banking organizations required to calculate risk-based capital under the advanced approaches[1] must maintain a supplementary leverage ratio ("SLR") of 3%. Unlike the tier 1 leverage ratio, which measures the ratio of tier 1 capital to total consolidated assets, the SLR is the ratio of tier 1 capital to total leverage exposure, a measure that includes both on- and off-balance sheet items. In addition to the SLR, the eight U.S. GSIBs and their IDI subsidiaries must maintain an eSLR.

At the holding company level, a GSIB must maintain a buffer of 2% on top of the 3% minimum SLR in order to avoid restrictions on capital distributions and certain discretionary bonus payments. IDI subsidiaries of U.S. GSIBs must maintain an SLR of 6% in order to be considered "well capitalized" under the PCA framework.[2]

Modifications to eSLR

The agencies propose to recalibrate the eSLR requirements by changing the fixed eSLR to 50% of the percentage that applies pursuant to the GSIB surcharge methodology.[3]

Under the proposed rule, GSIBs would be subject to the following SLR and eSLR standards:

- A GSIB holding company would be required to maintain the minimum 3% SLR, plus a leverage buffer equal to 50% of the firm's GSIB surcharge, in order to avoid limitations on distributions and certain discretionary bonus payments.
- An FRB- or OCC-regulated IDI would be required to maintain an SLR of 3% plus 50% of its holding company's GSIB surcharge to be considered "well capitalized" under the PCA framework.

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[1] A banking organization is subject to the advanced approaches capital requirements if it has $250 billion or more total consolidated assets or $10 billion or more in on-balance sheet foreign exposures, or is a banking organization subsidiary of a depository institution, bank holding company, savings and loan holding company or intermediate holding company subject to the advanced approaches.

[2] Under the PCA framework, an IDI may be subject to limits on its activities, or to closure, if its level of capitalization falls below certain thresholds.

[3] GSIBs must hold additional capital—that is, a risk-based surcharge—based on the FRB's methodology, which is intended to measure a GSIB's systemic footprint.

The agencies request comment on whether the new eSLR standard for IDIs should be a capital buffer requirement instead of being incorporated into the PCA framework. Under this alternative, an IDI also would have to maintain an SLR of 3% plus a leverage buffer of 50% of its holding company's GSIB surcharge in order to avoid limitations on distributions and certain discretionary bonus payments.

Modifications to TLAC Standards

The proposed rule also would amend the TLAC requirements: (a) to replace the 2% TLAC leverage buffer with a buffer set to 50% of the firm's GSIB surcharge; and (b) to make parallel changes to the TLAC rule's long-term debt requirements by making such requirement equal to total leverage exposure multiplied by 2.5% plus 50% of the GSIB's surcharge (rather than total leverage exposure multiplied by 4.5%).

The proposed rule also makes a number of technical amendments to the TLAC rule as applied to the U.S. intermediate holding companies of foreign GSIBs, including by correcting a technical error in the applicability provisions of the TLAC rule to clarify that foreign banking organizations have at least three years after initial applicability before they become subject to the substantive requirements of the TLAC rule.

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