United States Senate
WASHINGTON, DC 20510

April 9, 2013

The Honorable Daniel K. Tarullo
Governor
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

The Honorable Thomas J. Curry
Comptroller
Office of the Comptroller of the Currency
250 E Street SW, Room 9048
Washington, DC 20219

The Honorable Martin J. Gruenberg
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Dear Governor Tarullo, Comptroller Curry, and Chairman Gruenberg:

As you know, the debate over ending too-big-to-fail continues to draw public attention and concern. In this regard, we urge you to proceed deliberately and expeditiously with the following measures:

Bank Capital: Numerous studies have shown that regulator reliance on the internal models of large banks to determine the riskiness of the banks' assets has led to wide variations in the amount of capital held by banks with similar portfolios. Internal models can be inherently unreliable, and, of course, they rest on assumptions that often prove to be false, such as, most recently, the assumption that OECD member country debt is entirely risk free.

The Basel Committee agreed to an international leverage ratio in its 2010 Basel III capital accord to address weaknesses in the use of risk-based standards. But this leverage ratio will only have meaning if it is sufficiently strong. And just as importantly, while the use of asset risk weights makes some sense, we should not rely on them completely. An appropriate minimum overall capital ratio in exchange for a reduced reliance on models would make sense.

There is widespread, bipartisan agreement that excessive leverage played a major role in the 2008 financial crisis and ensuing need for taxpayer bailouts. Constraining leverage through the use of a simple and effective leverage ratio would go a long way toward correcting deficiencies in the capital regulation of large, complex financial institutions that proved to be seriously over leveraged prior to the crisis.

In addition, we believe that we should not move forward with an overly complicated capital regime for smaller institutions. As you know, community banks, for example, have very different business models than globally active financial institutions, and while there may be merit in improving the capital framework applicable to them, this should be a secondary priority to constraining leverage at the largest firms. The new Basel III capital standards were designed for large, internationally active banks, as was appropriate. We urge you to complete work on capital standards for the largest banks before turning to the smaller institutions. Then, devise a simpler framework that, unlike the current proposals, will be within the reach and capabilities of community institutions.

Enhanced Prudential Standards: Even with tougher capital standards, there is no guarantee that a large bank failure can be prevented in the future. As a consequence, it is imperative that you ensure that should a large institution fail, the losses associated with the failure can be absorbed by its own shareholders and creditors. These losses should not be forced on other members of the industry through special assessments, as DFA would require, or worse, despite the prohibition in DFA, on taxpayers. The FDIC, working in consultation with the Federal Reserve Board and international regulators, is developing a new strategy for the orderly resolution of a large, internationally active bank which involves seizing control of its holding company. However, to be successful, it is imperative that the holding company issue enough equity and long-term unsecured debt to absorb losses. For this reason, commentators, including FDIC and Federal Reserve Board officials, have acknowledged the wisdom and need for requiring complex financial institutions to issue an appropriate amount of equity and long-term, unsecured debt at the holding company level, where investors and creditors clearly understand there is a risk of loss in the event of a failure. We urge you to consider the vital step of having loss absorption capacity at the holding company level, as you draft rules for the regulation of large systemically risky firms.

We understand that the financial regulators have had a daunting task in promulgating and finalizing the numerous regulatory provisions required by Dodd-Frank. Given the many demands on your time and resources, some prioritization is obviously necessary. As such, we ask that you move expeditiously in these two areas, given continued public concern over the dangers that large financial institutions pose to our banking system and to the overall economy. By acting to substantially strengthen capital requirements and to ensure that future losses of a large bank failure will be absorbed by its shareholders and unsecured creditors, you will further your statutory mandate to protect the public against financial instability and go a long way toward ending too-big-to-fail.

Sincerely,

Senator Bob Corker

Senator Sherrod Brown

Senator David Vitter

Senator Elizabeth Warren

Senator Susan Collins