Opening Statement by Governor Daniel K. Tarullo

Thank you, Chair Yellen.

As you just noted, the *final rule* on enhanced supplementary leverage ratio standards for the largest, most systemically important banking organizations in the United States is part of our program to establish, consistently with Section 165 of the Dodd-Frank Act, a set of enhanced prudential standards for firms whose failure or material distress would pose the greatest risk to the stability of the financial system. The *final rule* would strengthen our multi-pronged capital framework of complementary requirements and standards that focus on different vulnerabilities and therefore compensate for potential shortcomings in any single capital measure.

With our adoption of the Basel III capital reforms and our intention to implement risk-based capital surcharges for globally systemic firms, we must raise the required leverage ratio for these firms if we are to maintain the traditional relationship between the risk-based capital and leverage ratios. The leverage ratio serves as a critical backstop to the risk-based capital requirements--particularly for the most systemic banking firms--and moderates some of the pro-cyclicality in the risk-based capital regime. It helps compensate for the possibility that risk-weighted measures understate the risk that large holdings of assets that are very safe in normal times may, as we observed during the financial crisis, become considerably less so in periods of serious financial market stress.

Numerous commenters have noted the potential for skewing the incentives of the largest financial firms if the leverage ratio becomes the binding capital requirement in ordinary times. Board staff estimates do suggest that this rule would make the leverage ratio more binding, relative to the risk-based capital ratios, for certain U.S. systemic banking organizations. However, the impact would vary substantially among firms, depending on their business models, and analysis suggests that these organizations could manage their capital structures to help meet the standards through certain low-cost, systemic-risk-reducing actions. It is also worth noting that, if we increase the risk-based capital surcharge for U.S. systemically important firms to a higher level than the minimum agreed to internationally, such as by reference to dependence on runnable short-term wholesale funding, the supplemental leverage ratio would be less likely to bind in normal times.

The *proposed rule* before us would revise the definition of total leverage exposure in the supplementary leverage ratio--that is, the denominator of the ratio. This proposal would implement the recent international agreement on this definition. To help ensure global financial stability, it is important that all internationally active banking organizations meet a minimum leverage requirement. I should note that staff estimates that the aggregate amount of tier 1 capital needed to meet the supplementary leverage ratio would increase modestly as a result of the proposal, though again with potentially different impacts on different firms.

With that, I turn to Connie Horsley, who will provide a more detailed explanation of both the final and the proposed rules.