BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

BEN S. BERNANKE
CHAIRMAN

April 11, 2011

The Honorable Sherrod Brown
United States Senate
Washington, D.C. 20510

Dear Senator:

This is in response to your letter dated March 18, 2011, in which you raised concerns about the largest 19 bank holding companies (BHCs) that received assistance through the Troubled Asset Relief Program (TARP) being permitted to increase dividends based on results of the Comprehensive Capital Analysis and Review (CCAR).

Attached, please find responses to the questions posed in your letter. I hope this information is helpful to you.

Sincerely,

Enclosure

ATTACHMENT

1. Will you make available to the public the details, methodology, and institution-by-institution results of the stress tests?

On March 18, 2011, the Federal Reserve issued a press release and published a detailed "white paper" that describes the objectives, context, component assessments, disclosure issues, as well as similarities and differences between the Comprehensive Capital Analysis and Review (CCAR), the Supervisory Capital Assessment Program (SCAP), and the stress-testing provisions of Dodd-Frank Act (DFA)[1]. The white paper also includes a summary of the key macroeconomic variables used in the supervisory stress scenario, which provides useful information to market participants about the severity of the CCAR exercise.

In contrast to the SCAP, the Federal Reserve does not intend to disclose firm-specific results from the CCAR. This reflects the different nature and purpose of the two exercises. As outlined in the white paper, the CCAR differs from the SCAP in that it was not only an evaluation of the stressed capital levels, but also an assessment of the process used by the firms to manage capital and assess risk. In addition, the Federal Reserve focused on assessing the sensitivity of the firms' projections of capital under alternative assumptions, rather than generating complete, independent estimates as in the SCAP and required under DFA. As a result, the CCAR stress test results do not lend themselves to direct comparisons across firms.

2. Why, in this time of economic uncertainty, is it necessary for the largest TARP recipients to issue dividends, when those institutions are most prone to moral hazard?

Since the conclusion of the SCAP in May 2009, the quantity and quality of bank capital has improved substantially, many large banks have repaid TARP capital (in large part from proceeds of common issuance) and large U.S. banks are better positioned to withstand unanticipated stresses. Since the third quarter of 2008, the largest bank holding companies (BHCs) have raised more than $300 billion in common equity capital. The 19 largest BHCs added $36 billion in retained earnings to common equity since the end of 2009 as earnings have improved, while distributions to shareholders have been limited, in accordance with Federal Reserve guidance regarding such distributions.[2] In addition to general improvements in their financial condition, these firms also have greater clarity about the future regulatory environment following the completion of the Basel III agreement and the adoption of the DFA.

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[1] The press release and white paper is available on the Board's public website at http://www.federalreserve.gov/newsevents/press/bcreg/20110318a.htm.

[2] These data are derived from the Federal Reserve Y-9C reports, which contain quarterly balance sheet and income statement data for bank holding companies. Guidance is referring to SR Letter 09-4 and its addendum. Available at: http://www.federalreserve.gov/boarddocs/srletters/2009/SR0904_Addendum.pdf

The ability of firms to return capital to shareholders in an appropriate manner is consistent with well-functioning, private capital markets that improve the overall allocation of capital in our economy. However, given continued uncertainty around the pace and strength of the economic recovery in the United States and abroad, and the extraordinary circumstances of the recent crisis, the Federal Reserve took a measured and conservative approach in considering capital distributions by the largest BHCs. Requests for increased capital distributions in 2011 were considered as one element of the comprehensive capital plans submitted by these firms. This process is intended to ensure the firms have thorough and robust processes for managing their capital resources and will continue to hold adequate capital and serve as credit intermediaries, even under adverse conditions.

3. If the international community is moving toward increased capital requirements under the Basel III framework, shouldn't the United States do the same?

Federal banking agencies are currently developing proposals for the implementation of Basel III in the U.S. The CCAR was designed to be consistent with the proposed Basel III framework to ensure U.S. firms have sufficient capital for safety and soundness purposes, while maintaining a competitive landscape internationally. The Federal Reserve critically examined the credibility of each firm's capital plan and the firms' assumptions regarding their ability to take the steps necessary to meet the more stringent capital requirements proposed under Basel III.

4. What capital requirements will you apply to Systemically Important Financial Institutions under the Dodd-Frank Act?

Section 165 of the DFA directs the Federal Reserve to impose enhanced risk-based capital and leverage requirements on BHCs with consolidated assets of $50 billion or more and nonbank financial companies supervised by the Federal Reserve. The requirements must be more stringent than the risk-based capital and leverage requirements for firms that do not pose similar risk to U.S. financial stability, and the requirements increase in stringency based on the systemic footprint of the firm. The Federal Reserve is in the process of developing a proposed rule to implement these enhanced risk-based capital and liquidity requirements, which is expected to be issued in mid-2011.