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February 9, 2015

Barry F. Mardock, Deputy Director
Office of Regulatory Policy
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102–5090

Re: Proposed rule on Regulatory Capital, Implementation of Tier 1/Tier 2 Framework
Published at 79 FR 52814-52908

Dear Mr. Mardock:

The Farm Credit Administration (FCA) has published the above-mentioned proposed rule to implement Basel III for the Farm Credit System. My biggest disappointment with the proposed rule is that it is intended to implement Basel III for the Farm Credit System.

I am in agreement with Thomas Hoenig, Vice Chairman of the Federal Deposit Insurance Corporation, who has said that Basel III is too complicated and should not be implemented in the United States as currently proposed. For example, see his speech on September 14, 2012: "Back to Basics: A Better Alternative to Basel Capital Rules":

> …the United States should not implement Basel III, but reject the Basel approach to capital and go back to the basics.

Another banking regulator who speaks passionately in favor of simplicity is Andrew Haldane, Executive Director, Financial Stability, Bank of England. For example, see his speech on August 31, 2012: "The dog and the frisbee." Both speeches should be required reading for all financial institution regulators.

The fact that FCA's proposed rule is 95 pages of small print in the Federal Register is *prima facie* evidence that it is too complicated. Capital regulations should be clear and simple. The proposed rule is too long by at least a factor of ten.

And yet, in spite of its length and complexity, there is one factor that the proposed rule does not include that I would endorse. Subsequent to the financial crisis of 2008, there began to be the idea that large financial institutions should be required to hold more capital as a percent of their assets than small financial institutions. Previously the common view was that large institutions were safer—that they were better managed and more diversified. And it may well be that large institutions have a lower probability of default for those reasons.

What we all came to learn in the financial crisis of 2008 is that large financial institutions, when they do fail, have a *much* larger loss given default because of the damage that their failure causes to others. That's why we have a "too big to fail" problem.

This idea was included in a blog post by Prof. Gary Becker of the University of Chicago dated March 9, 2009 titled "Financial Regulations":

> One-way to reduce the likelihood of a too-big-to-fail problem is to impose higher capital requirements relative to assets on larger financial firms. That is, to implement a progressive set of capital requirements relative to assets that would increase as the size of a bank or other financial firm increased.

Dr. Becker won the Nobel prize in economics in 1992.

This idea was noted in a speech by Sheila Bair, then Chairman of the Federal Deposit Insurance Corporation, on March 20, 2009:

> We need to reduce systemic risk by limiting the size, complexity, and concentration of our financial institutions. We need to create regulatory and economic disincentives for systemically important financial firms. For example, we need to impose higher capital requirements on them in recognition of their systemic importance, to make sure they have adequate capital buffers in times of stress.

The principle of greater capital requirements for larger institutions has been adopted by regulators of financial institutions. For example, implementation of this concept in 2014 by the Federal Reserve is documented here (final rule requiring an additional 2% leverage buffer for large financial institutions) and here (proposed rule that would require capital surcharges of 1.0-4.5% on the largest financial institutions).

While Dr. Becker, Ms. Bair and the Federal Reserve are all referring to "systemically important financial institutions" on the scale of Citigroup, etc., the same principle applies within the Farm Credit System. Any System association whose failure could bring down the System is "systemically important" to the System, and I encourage FCA to apply this principle to such associations.

Thank you for this opportunity to comment on FCA's proposed capital rule.

Sincerely,

George S. Putnam
President and CEO

cc: Yankee Farm Credit Board of Directors

Links

Thomas Hoenig, 9/14/12, “Back to Basics: A Better Alternative to Basel Capital Rules”
https://www.fdic.gov/news/news/speeches/archives/2012/spsep1412_2.html

Mr. Hoenig’s speeches, etc. can be found here:
https://www.fdic.gov/about/learn/board/hoenig/index.html

Andrew Haldane, 8/31/12, “The dog and the frisbee”
http://www.bankofengland.co.uk/publications/Documents/speeches/2012/speech596.pdf

Mr. Haldane’s speeches, etc. can be found by searching by author here:
http://www.bankofengland.co.uk/publications/Pages/speeches/default.aspx

Gary Becker, 3/09/09, “Financial Regulations”
http://www.becker-posner-blog.com/2009/03/financial-regulations-becker.html

Sheila Bair, 3/20/09, speech to Independent Community Bankers of America
https://www.fdic.gov/news/news/speeches/archives/2009/spmar2009_2.html

Federal Reserve, 4/08/14, joint press release with FDIC and OCC
http://www.federalreserve.gov/newsevents/press/bcreg/20140408a.htm

Federal Reserve, 12/09/14, press release
http://www.federalreserve.gov/newsevents/press/bcreg/20141209a.htm