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News release

11 July 2014

Bank of England Consultation Paper: The Financial Policy Committee's review of the leverage ratio

The Financial Policy Committee is today launching a consultation on the design of a leverage ratio framework for the UK. This forms part of the FPC's review of the role of the leverage ratio within the capital framework for banks, as requested by the Chancellor of the Exchequer in November 2013.

This consultation paper sets out the FPC's analysis of the policy choices that would determine the role of the leverage ratio within this framework. The responses to this paper will inform the final review, intended to be published in November 2014.

The review and this paper will not determine appropriate numerical values for the leverage ratio framework. These will be considered by the FPC at the point when the capital framework and too-big-to-fail priorities are concluded next year.

The FPC views the leverage ratio as an integral part of the capital framework and an effective complement to the existing framework of risk-weighted capital requirements and buffers. Adding a leverage ratio requirement would mean that the UK's capital requirement framework for banks would comprise:

- A risk-weighted capital framework, in which capital requirements are set in proportion to an assessment of risk in each asset class.
- A stress-testing framework, exploring banks' resilience to future adverse scenarios.
- A leverage ratio framework, set in proportion to exposures regardless of their risk, to guard against under-statement of risk.

In combination, these measures can enhance the safety and soundness of firms and improve the resilience of the financial system as a whole by ensuring that institutions fund their activities with sufficient capital.

The consultation paper published today considers a range of issues, including the following:

Whether the leverage framework should mirror features of the existing risk-weighted framework. The main components of the risk-weighted framework include a minimum requirement, a capital conservation buffer, supplementary buffers for systemically important firms and a time-varying countercyclical capital buffer.

The case for introducing a supplementary leverage ratio component to a subset of firms, for example ring-fenced banks and/or systemically important institutions, and whether this should be varied in proportion to the associated supplementary risk-weighted ratio.

The merits of a time-varying leverage ratio component, which would be varied in a countercyclical manner as system-wide risks evolve over the cycle.

The quality of capital needed to meet the possible components of the leverage framework.

The consultation paper sets out the possible costs and benefits of applying a leverage ratio to different types of firms, as well as some high-level considerations related to a cost-benefit analysis of a leverage ratio framework.

The paper also considers the allocation of responsibilities over the leverage ratio framework. Based on the analysis so far, the FPC is minded to recommend to HMT that it be granted powers of Direction over all components of the leverage ratio framework.

Notes to Editors

1. Consultation Paper: The Financial Policy Committee's review of the leverage ratio
http://www.bankofengland.co.uk/financialstability/Pages/fpc/fscp.aspx

2. Leverage Ratio review - Terms of Reference
http://www.bankofengland.co.uk/publications/Pages/news/2014/062.aspx

Key Resources

pdf Consultation Paper (319KB)