Federal Reserve Proposes Significant Changes to Large Firm Prudential Framework

November 1, 2018

Yesterday, the Federal Reserve Board (the "FRB") proposed significant changes to the prudential framework applicable to banking organizations with $100 billion or more in total consolidated assets (the "Proposal").[1] We have set forth below a high-level overview of the Proposal and anticipate publishing a more detailed analysis in the near future. Comments on the Proposal are due by January 22, 2019.

Debevoise & Plimpton

The Proposal would create four categories of prudential standards for U.S. bank holding companies and noncommercial, noninsurance savings and loan holding companies with $100 billion or more in total consolidated assets.

Category I firms include the U.S. global systemically important bank holding companies ("GSIBs").

Category II firms include firms with $700 billion or more in total consolidated assets or $75 billion or more in cross-jurisdictional activity (defined as the sum of cross-jurisdictional liabilities and assets) that are not otherwise subject to Category I standards.

Category III firms include firms that are not subject to Category I or II standards that have $250 billion or more in total consolidated assets or $75 billion or more in any one or more of: (1) nonbank assets; (2) weighted short-term wholesale funding; and (3) off-balance-sheet exposures.

Category IV firms include firms with at least $100 billion in total consolidated assets that are not subject to any other category.

The Proposal's inclusion of noninsurance, noncommercial savings and loan holding companies would represent an expansion of the reach of the full suite of enhanced prudential standards, which at present apply only to bank holding companies.

---

[1] The Office of the Comptroller of the Currency issued a parallel proposal focused on the applicability thresholds for regulatory capital and liquidity requirements. The Federal Deposit Insurance Corporation is expected to issue a similar proposal in the near future.

The standards for the four categories of firms are as follows:

Category I standards. The Proposal would retain the current prudential framework for GSIBs but remove the mid-cycle company-run Dodd-Frank Act stress testing ("DFAST") requirement.

Category II standards. The Proposal would retain the current prudential framework for Category II firms, but remove the mid-cycle company-run DFAST requirement. In addition, these firms would be subject to:

- The qualitative assessment under the FRB's Comprehensive Capital Analysis and Review ("CCAR") program, even if the firm has less than $250 billion in total consolidated assets and less than $75 billion in nonbank assets
- The FRB's single-counterparty credit limits rule (the "SCCL"), even if the firm has less than $250 billion in total consolidated assets (which is the applicability threshold for the SCCL rule as recently finalized by the FRB, see our prior analysis)

Category III standards. The Proposal would change the prudential framework for these firms by:

- Removing the advanced approaches capital requirements (although the supplementary leverage ratio and countercyclical capital buffer requirements would be retained)
- Removing the requirement to recognize most elements of accumulated other comprehensive income ("AOCI") in regulatory capital
- Replacing the most stringent versions of the liquidity coverage ratio (the "LCR") and proposed net stable funding ratio (the "NSFR") with versions that are scaled based on a factor of 70 percent to 85 percent, unless the firm has weighted short-term wholesale funding of $75 billion or more (in which case the full requirements apply)
- Reducing the frequency of company-run DFAST from annually to every two years (although internal stress tests would appear to be required in connection with the annual capital plan submission)

However, these firms would become subject to the following requirements that may not necessarily apply today:

- The qualitative assessment under the FRB's CCAR program, even if the firm has less than $250 billion in total consolidated assets and less than $75 billion in nonbank assets

- The SCCL rule, even if the firm has less than $250 billion in total consolidated assets

- Daily (as opposed to monthly) liquidity reporting, if the firm has $75 billion or more in weighted short-term wholesale funding

Category IV standards. The Proposal would change the prudential framework for these firms by:

- Removing the advanced approaches capital requirements (if they were previously applicable)

- Removing the supplementary leverage ratio requirement

- Removing the requirement to recognize most elements of AOCI in regulatory capital

- Removing the LCR and the proposed NSFR requirements

- Reducing the stringency of liquidity risk management, stress testing and buffer requirements by:

    - Reducing the frequency of required internal liquidity stress testing from monthly to quarterly

    - Reducing the frequency of evaluation of collateral positions from weekly to monthly

    - Limiting liquidity risk limits to activities relevant to the firm

    - Reducing required elements of monitoring of intraday liquidity risk exposures

- Reducing the frequency of the supervisory stress testing requirement from annually to every two years

- Eliminating the requirement to conduct and publicly disclose company-run stress tests

- Reducing the frequency of the CCAR quantitative assessment from annually to every two years, although capital plans would need to be submitted annually

The Proposal does not modify the framework for foreign banking organizations, which will be addressed in a separate forthcoming proposal. Separate proposals also are forthcoming regarding resolution planning requirements, revisions to the FRB's capital planning rule and integration of the proposed stress capital buffer with the Proposal.

Satish M. Kini
Partner, Washington, D.C.
+1 202 383 8190
smkini@debevoise.com

Gregory J. Lyons
Partner, New York
+1 212 909 6566
gjlyons@debevoise.com

David L. Portilla
Partner, New York
+1 212 909 6041
dlportilla@debevoise.com

Chen Xu
Associate, New York
+1 212 909 6171
cxu@debevoise.com