

Back to the Future: FSOC Once Again Proposes a Higher Bar for Nonbank Financial Company Designations

April 9, 2026

The Financial Stability Oversight Council (“FSOC”) has proposed once again to recalibrate its approach to nonbank financial company designations. On March 25, 2026, FSOC released proposed interpretive guidance (the “Proposed Guidance”) that would rescind the existing guidance (the “2023 Guidance”)¹ and analytic framework (the “2023 Analytic Framework”) adopted by the Biden administration and largely reinstate the 2019 framework (“2019 Guidance”) from the first Trump administration. The Proposed Guidance would restore the primacy of an activities-based approach and reintroduce procedural and analytical features that would raise the threshold for designation. Comments are due by May 14, 2026.

For nonbank financial companies, the Proposed Guidance would reduce the threat of designation. By restoring the activities-based approach as the presumptive first step, reinstating cost-benefit analysis and an assessment of the likelihood of material financial distress, adopting a higher threshold for what constitutes a “threat to the financial stability of the United States” and adding a 180-day remediation window, the Proposed Guidance would make designation more clearly a measure of last resort.

At the same time, the activities-based approach of the Proposed Guidance may lead to increased scrutiny of products, activities and practices by primary regulators, as FSOC places greater emphasis on system-wide risk identification and interagency coordination. In that sense, the Proposed Guidance may reduce the likelihood of firm-specific designation while potentially increasing the likelihood of market-wide regulatory attention coordinated by FSOC.

RE-PRIORITIZATION OF THE ACTIVITIES-BASED APPROACH

As noted, the Proposed Guidance would restore the primacy of an activities-based approach to assessing financial stability threats and risks, largely returning to the 2019

¹ 91 Fed. Reg. 15551 (Mar. 30, 2026), available [here](#). Our client alerts on the 2023 Guidance can be found [here](#) and [here](#).

Guidance framework. In practice, this means FSOC would look first to system-wide solutions before turning to entity-specific designation. Under this approach:

- FSOC would first identify and assess potential risks to U.S. financial stability across markets, products, activities and practices and, if it concludes action is warranted, seek to address those risks through coordination with the relevant financial regulators.
- Only if those risks cannot be, or are not, adequately addressed through that process would FSOC proceed to consider an entity-specific designation.

That sequencing marks an important shift from the 2023 Guidance. Although the 2023 Guidance recognized an activities-based approach as one available tool, it did not require FSOC to prioritize system-wide regulatory response *before* initiating a firm-specific review. The Proposed Guidance therefore would impose a longer procedural runway before nonbank financial companies become the subject of a formal designation process.

The underlying policy rationale is that an activities-based approach would better capture systemic externalities, where private market incentives may not internalize the spillovers to the broader financial system, and reduce the competitive distortions that can arise when similarly situated firms face uneven regulatory burdens simply because one is considered for designation, rather than because of differences in efficiency, quality or risk management. At the same time, FSOC acknowledges that an activities-based approach may be less precise, particularly where effective action depends on coordination across multiple regulators. For that reason, the Proposed Guidance would preserve entity-specific designation as a backstop where system-wide measures do not adequately address a perceived threat to the U.S. financial stability.

HEIGHTENED HURDLES TO DESIGNATION

Revival of Cost-Benefit Analysis and Assessment of the Likelihood of Material Financial Distress

The Proposed Guidance would revive two interrelated features of the 2019 Guidance that had been eliminated in 2023: (1) a cost-benefit analysis before designation; and (2) an assessment of the likelihood of a nonbank financial company's material financial distress.

Under the Proposed Guidance, FSOC would designate a nonbank financial company only if the expected financial-stability benefits from Federal Reserve Board supervision and prudential standards justify the expected costs that the designation would impose.

In making such a determination, FSOC would consider both quantifiable (using ranges, as appropriate) and non-quantifiable, “reasonably estimable” benefits and costs, including not only the regulatory burden imposed on the company by increased regulatory requirements, but also the broader effects on the U.S. economy, including potential impacts on economic growth and economic security.

The Proposed Guidance would also restore FSOC’s assessment of the likelihood of a company’s material financial distress, applying qualitative and quantitative indicators, such as market-based (e.g., distance-to-default measures), accounting-based (e.g., statistical models using capital adequacy) and hybrid (e.g., academic model) measures. That step is designed to reduce the risk of “over-designation, which can impose costs,” by distinguishing between firms whose distress could realistically pose a serious threat and those for which the prospect of “distress is highly remote,” such that designation would not be justified.

Higher Threshold for “Threat to Financial Stability”

The Proposed Guidance would raise the threshold for when a nonbank financial company may be deemed to pose “a threat to the financial stability of the United States,” a term used but not defined in the Dodd-Frank Wall Street Reform and Consumer Protection Act. Whereas the 2023 Analytic Framework interpreted the phrase to encompass events or conditions that could *substantially impair* the financial system’s ability to support economic activity, under the Proposed Guidance, FSOC would revert to the 2019 Guidance formulation in which the threat must involve an impairment of financial intermediation or financial market functioning to a degree sufficient to *inflict severe damage* on the broader U.S. economy. The practical effect is to reinforce that designation is intended to be an exceptional measure, reserved for only the most consequential threats.

Formalization of a Pre-Designation “Off-Ramp”

While preserving the existing procedural protections, the Proposed Guidance would add a new procedural step that makes more explicit the pre-designation remediation opportunity for firms to take remedial steps before formal designation and, in some cases, thereby avoid designation. After a preliminary evaluation, FSOC would identify remedial steps for the company or relevant regulators and generally expect materials risks to be addressed within 180 days. The addition is significant because it would formalize remediation before designation and enhance transparency in the designation process.

Broader Analytic Framework Incorporating Economic Growth and Security

The Proposed Guidance would update FSOC’s analytic methodologies to incorporate explicitly economic growth and economic security considerations into its identification

of financial stability risks, reflecting the view that “economic growth provides the strongest foundation for financial stability, and that economic security, in turn, supports economic growth.” In so proposing, FSOC signals that it would more explicitly account for the costs and burdens of regulation, including whether elements of the U.S. financial regulatory framework impose undue burdens that could constrain economic growth, impair intermediation, raise borrowing costs or reduce the availability of financial products. That suggests a more explicit analysis of tradeoffs in future FSOC actions, whether they are activities-based proposals or designations, and may give affected firms, particularly those that are subject to designation proceedings, additional footing to argue that proposed interventions should be calibrated to avoid unnecessary burdens on intermediation, credit availability or market functioning.

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Please do not hesitate to contact us with any questions.



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