Federal Reserve Bank of San Francisco
101 Market Street, San Francisco, California 94105

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To State Member Banks, Bank
Holding Companies, Financial Holding
Companies, Foreign Bank Offices and
Savings and Loan Holding Companies
in the Twelfth Federal Reserve District

Federal Reserve Board Proposes Steps to Strengthen Regulation and Supervision of Large Bank Holding Companies and Systemically Important Nonbank Financial Firms

The Federal Reserve Board on December 20, 2011 proposed steps to strengthen regulation and supervision of large bank holding companies and systemically important nonbank financial firms. The proposal, which includes a wide range of measures addressing issues such as capital, liquidity, credit exposure, stress testing, risk management, and early remediation requirements, is mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act.

The proposal generally applies to all U.S. bank holding companies with consolidated assets of $50 billion or more and any nonbank financial firms that may be designated by the Financial Stability Oversight Council as systemically important companies. The Board will issue a proposal regarding foreign banking organizations shortly. In general, savings and loan holding companies (SLHCs) would not be subject to the requirements in this proposal, except certain stress test requirements. The Board plans to issue a separate proposal later to address the applicability of the enhanced standards to SLHCs.

The Board is proposing a number of measures, including:

- **Risk-based capital and leverage requirements**. These requirements would be implemented in two phases. In the first phase, the institutions would be subject to the Board's capital plan rule, which was issued in November 2011. That rule requires firms to develop annual capital plans, conduct stress tests, and maintain adequate capital, including a tier one common risk-based capital ratio greater than 5 percent, under both expected and stressed conditions. In the second phase, the Board would issue a proposal to implement a risk-based capital surcharge based on the framework and methodology developed by the Basel Committee on Banking Supervision.

- **Liquidity requirements**. These measures would also be implemented in multiple phases. First, institutions would be subject to qualitative liquidity risk-management standards generally based on the interagency liquidity risk-management guidance issued in March 2010. These standards would require companies to conduct internal liquidity stress tests and set internal quantitative limits to manage liquidity risk. In the second phase, the Board would issue one or more proposals to implement quantitative liquidity requirements based on the Basel III liquidity rules.

- **Stress tests**. Stress tests of the companies would be conducted annually by the Board using three economic and financial market scenarios. A summary of the results, including company-specific information, would be made public. In addition, the proposal requires companies to conduct one or more company-run stress tests each year and to make a summary of their results public.

- **Single-counterparty credit limits**. These requirements would limit credit exposure of a covered financial firm to a single counterparty as a percentage of the firm's regulatory capital. Credit exposure between the largest financial companies would be subject to a tighter limit.

- **Early remediation requirements**. These measures would be put in place for all firms subject to the proposal so that financial weaknesses are addressed at an early stage. The Board is proposing a number of triggers for remediation--such as capital levels, stress test results, and risk-management weaknesses--in some cases calibrated to be forward-looking. Required actions would vary based on the severity of the situation, but could include restrictions on growth, capital distributions, and executive compensation, as well as capital raising or asset sales.

The Board is proposing that firms would need to comply with many of the enhanced standards a year after they are finalized. The requirements related to stress testing for bank holding companies, however, would take effect shortly after the rule is finalized.

The Federal Reserve consulted with other members of the Financial Stability Oversight Council in developing the proposal. Comments on the proposal are requested by March 31, 2012.

Additional Information

All circulars and documents are available on the Internet through the Federal Reserve Bank of San Francisco's website, at http://www.frbsf.org/banking/letters.

For additional information, please contact:

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Attachment: Proposed Rule (546 KB PDF)