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Nonbank Financial Company Designations
Notice of Proposed Rulemaking and Proposed Interpretive Guidance
Fact Sheet

In the recent financial crisis, financial distress at certain nonbank financial companies contributed to a broad seizing up of financial markets. These nonbank financial companies were not subject to the type of regulation and consolidated supervision applied to bank holding companies, nor were there effective mechanisms in place to resolve the largest and most interconnected of these nonbank financial companies without causing further instability.

To address any potential risks posed to U.S. financial stability by these companies, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") authorizes the Financial Stability Oversight Council (the "Council") to determine that certain nonbank financial companies will be subject to supervision by the Board of Governors of the Federal Reserve System (the "Board of Governors") and to enhanced prudential standards.

The Council is releasing for public comment a revised notice of proposed rulemaking on nonbank financial companies including proposed interpretive guidance (the "Revised NPR"), superseding the previous notice of proposed rulemaking on the same subject released on January 26, 2011. The Revised NPR provides (a) additional details regarding the framework that the Council intends to use in the process of determining whether a nonbank financial company should be subject to supervision by the Board of Governors and to enhanced prudential standards; and (b) further opportunity for public comment on the Council's proposed approach to making these determinations. The Revised NPR will be published in the Federal Register for a 60-day public comment period. After the final rule is issued, the Council will begin the process of determining whether particular nonbank financial companies should be subject to supervision by the Board of Governors and to enhanced prudential standards

A determination by the Council to subject a nonbank financial company to supervision by the Board of Governors and to enhanced prudential standards is one of many tools established by the Dodd-Frank Act to monitor and mitigate any potential threats to U.S. financial stability. Other measures established under the Dodd-Frank Act include:

- Automatically subjecting bank holding companies with consolidated assets greater than $50 billion to enhanced prudential standards.
- Providing the Council the authority to designate systemically important financial market utilities for enhanced supervision.
- Authorizing the Council to make recommendations to financial regulatory agencies to apply new or heightened standards and safeguards for a financial activity or practice.

The Council has developed a careful framework for evaluating whether a nonbank financial company should be subject to Board of Governors supervision and to enhanced prudential standards

- The Council will approach each decision on a firm-specific basis, considering the unique risks that each nonbank financial company may pose. The analysis will encompass both quantitative analysis and the Council's qualitative judgment.
- The Dodd-Frank Act requires the Council to assess 10 considerations when evaluating nonbank financial companies. The Council proposes to group these statutory considerations into a six-category framework.
- The Council will seek to assess the potential impact of a company's financial distress on the broader economy based on three of the framework categories—size, substitutability, and interconnectedness.
- The Council will seek to assess the vulnerability of a company to financial distress based on the other three framework categories— leverage, liquidity risk and maturity mismatch, and existing regulatory scrutiny.
- Nonbank financial companies will generally be assessed in a three-stage process:

    Stage 1: First, the Council will apply uniform quantitative thresholds, outlined below, to identify those nonbank financial companies that will be subject to further evaluation.

Stage 2: The Council will analyze the nonbank financial companies identified in stage 1, using a broad range of information available to the Council primarily through existing public and regulatory sources.

Stage 3: The Council will contact each nonbank financial company that the Council believes merits further review to collect information directly from the company that was not available in the earlier stages. Each nonbank financial company that is reviewed in stage 3 will be notified that it is under consideration and be provided an opportunity to submit written materials related to the Council's consideration of the company for a proposed determination.

- At the end of stage 3, based on the results of the analyses conducted during each stage of review, the Council may, by a vote of at least two-thirds of the Council's voting members, including an affirmative vote by the Chairperson of the Council, make a proposed determination regarding the company. If a proposed determination is made, the Council will provide the nonbank financial company with a written explanation of the basis of the proposed determination. The company may request a hearing to contest the proposed determination. In order to make a final determination, the Council must again vote by a two-thirds majority, including an affirmative vote by the Chairperson.

The Council intends to apply the following uniform quantitative thresholds to a broad group of nonbank financial companies in stage 1 to help identify companies for further evaluation.

- A nonbank financial company will be subject to further evaluation if it has at least $50 billion in total consolidated assets and meets or exceeds any one of the following thresholds:
    - $30 billion in gross notional credit default swaps outstanding for which the nonbank financial company is the reference entity;
    - $3.5 billion in derivative liabilities;
    - $20 billion of outstanding loans borrowed and bonds issued;
    - 15 to 1 leverage ratio, as measured by total consolidated assets (excluding separate accounts) to total equity; or
    - 10 percent ratio of short-term debt (having a remaining maturity of less than 12 months) to total consolidated assets.
- Further evaluation by the Council of a nonbank financial company identified in stage 1 does not mean that the company will be subject to a final determination by the Council.
- The Council believes the proposed thresholds will provide meaningful initial assessments regarding the likelihood that a nonbank financial company could pose a threat to U.S. financial stability.
- These thresholds add significant transparency to the designation process by helping nonbank financial companies assess whether they will likely be subject to additional review by the Council. In addition, the Council may consider any nonbank financial company for a determination if the Council believes the company could pose a threat to U.S. financial stability.
- The Council will continue to evaluate and adjust as appropriate this framework and the thresholds as more data about firms and industries, such as asset managers, hedge funds, private equity firms, and swaps entities, becomes available.

A final determination by the Council regarding a nonbank financial company has two results: the company becomes subject to supervision by the Board of Governors and subject to enhanced prudential standards.

- The Board of Governors will establish the prudential standards for each nonbank financial company.
- The Council may make recommendations to the Board of Governors concerning the establishment and refinement of prudential standards and reporting and disclosure standards applicable to nonbank financial companies.