Regulatory Alert

Regulatory Insights for Financial Services

May 2025

Upcoming Regulatory Changes in/to Financial Risk

KPMG Regulatory Insights:

- **Priority on Financial Risk**: Will re-focus examiner priorities on areas such as market-, credit-, and capital-related risks
- **Coming Capital Changes:** May not reflect all of the Basel III Endgame standards but rather those regulators can "independently validate" and subject to public comment ; potential for supplementary leverage ratio changes to be separately addressed
- **Tailoring in All Shapes and Sizes:** Consideration of multiple efforts to tailor regulatory expectations for community banks (e.g., capital, TPRM) and ease requirements for large banks (e.g., stress testing, resolution planning)

Changes in the banking sector are underway as new leadership at the Department of the Treasury and the federal banking agencies take steps to outline new priorities and propose/redirect expectations related to:

1. Financial Risk Supervision
2. Stress Testing
3. Resolution Planning

1. Financial Risk Supervision

The Treasury Secretary and the federal bank regulators (FRB, FDIC) are outlining (and beginning to take) actions to:

- **Increase the Role of Treasury:** Treasury states that it intends to play a greater role in regulation through the FSOC (Financial Stability Oversight Council) and the President's Working Group on Financial Markets
- **"Modernize Capital":** Potential updates to capital requirements, including:
  - Reassessing the supplementary leverage ratio
  - Conducting analysis "from the ground-up" to determine the regulatory framework that is in the interest of the United States, borrowing "selectively" from the Basel III Endgame standards but then only to the extent that the underlying rationale can be independently validated and subject to public comment (Treasury Secretary statement).
  - Leveling the playing field between banks and nonbanks (e.g., reduced capital requirements for mortgage loans, opt-ins for entities not mandatorily subject to rule updates)
  - Updating the quantitative asset thresholds for "large bank" designations
- **Reassess the Liquidity Framework:** With the goal of identifying opportunities to expand the role of loans and other productive assets as collateral for funding during a period of stress, the agencies will consider:
  - The role of the discount window and the Federal Home Loan Banks (e.g., clarifying the role of these funding sources in internal liquidity stress testing and contingency funding plans)
  - Whether examiners ""have developed a bias toward reserves over other liquidity sources"
  - How to ensure liquidity buffers are not regulatory minimums
- **Prioritize Financial Risk:** Re-focus supervision to prioritize material financial risk rather than "non-core"

and "non-financial risks" such as IT, operational risk, risk management, internal controls, and governance (Treasury Secretary, FRB Governor). In addition, there is movement to:

- Reconsider the "management" component from the CAMELS rating system (Note: news reports suggest the FRB's next Supervision and Regulation Report will be released following confirmation of the new Vice Chair of Supervision)
- Remove "reputation risk" from the supervision and examinations framework (OCC, FDIC)
- Define "unsafe and unsound" through regulation using "objective measures rooted in financial risk"

— **Reintroduce Tailoring:** Reintroduce tailoring in regulations, especially for community banks, including the potential for "categorical exemptions" in areas such as third-party risk management and information security

— **Reconsider the Structure of the GSEs:** Although new FHFA leadership has stated a focus on operational efficiency and addressing potential fraud at Fannie Mae and Freddie Mac, significant changes to the board composition of both of these GSEs raise questions about whether (and when) the Administration is looking to restructure the GSEs including potentially removing them from conservatorship. Discussion points include mortgage rates, capital requirements, and legislative requirements.

(See remarks from the Treasury Secretary here; FRB Governor Bowman here; FDIC Acting Chairman here.)

2. Stress Testing

Consistent with a December 2024 press release, the FRB has issued a proposed rule that would amend the calculation of the agency's stress capital buffer requirements applicable to certain large banking organizations (hereinafter, firms – generally including firms with $100B in total consolidated assets subject to Category I-IV standards). With the stated aim of reducing the volatility of the capital requirements stemming from the annual stress test results, the FRB is proposing to:

— **Average** annual stress test results over the two most recent years (current and previous years) to inform a firm's stress capital buffer requirement. Firms that are subject to biennial supervisory stress tests would not be subject to results averaging.

— **Extend** the annual effective date of a firm's stress capital buffer requirement by one quarter, from October 1 to January 1 of the following year.

— **Change** data collected in the FR Y-14A/Q/M reports to isolate non-recurring expenses and obtain more granular data on compensation expenses. Additional changes would remove data items the FRB states are no longer needed for conducting the supervisory stress test.

As proposed, the changes to the calculation of the stress capital buffer requirement would be effective beginning with the 2025 supervisory stress test, which would average the results from the 2024 and 2025 supervisory stress tests for applicable firms. Comments on the proposal are due to the FRB no later than June 23, 2025.

The FRB states that it expects to propose additional changes later this year, including requirements to disclose and seek public comment on the models that determine the hypothetical losses and revenue of banks under stress, and to ensure that the public provides comment on the hypothetical scenarios used for the annual stress test before the scenarios are finalized.

3. Resolution Planning

The FDIC released an updated set of Frequently Asked Questions describing changes to its expectations for the initial resolution planning submissions by insured depository institutions (IDIs) under the FDIC's June 2024 final rule (see KPMG Regulatory here). The stated aim of the changes is to streamline the process and focus on operational information that would permit the FDIC to 1) resolve the bank over a weekend, or 2) operate the IDI for a short period of time while marketing it for sale.

The updates include clarifications, new exemptions, and modifications to previous expectations for both Group A ($100B or more in total assets) and Group B (at least $50B but less than $100B in total assets) filers. Importantly, the applicable asset thresholds and filing schedule for resolution plan submissions have not changed. The FDIC adds that additional changes may be forthcoming.

Select changes include:

Clarifications

— **Operational Readiness:** Banks are encouraged to maintain and document their capabilities to establish and manage Virtual Data Rooms (VDRs) efficiently.

— **Qualitative Descriptions:** Institutions must provide a qualitative description of the approaches they would employ for determining the values of franchise components and the IDI franchise as a whole, including the underlying assumptions and rationale.

- **Description of Exercises:** Full submissions must describe the exercises conducted by the IDI since the last full submission to assess the viability of its resolution strategy or to improve capabilities. IDIs are not required to have a capabilities assessment or testing framework.

Exemptions

- **Bridge Bank Strategy:** The requirement to develop and implement a bridge bank strategy has been waived, allowing institutions to propose one or more potential "suitable" resolution strategies, which may include a bridge bank.
- **Failure Scenario:** The obligation to develop and include a failure scenario in the plan has been removed.
- **Identification of Non-Deposit Claims:** The content requirements related to identifying non-deposit unsecured creditors of the IDI and its subsidiaries that are material entities have been waived.

Modifications

- **Valuation Requirements:** IDIs are expected to demonstrate that capabilities and processes exist to perform valuations of the IDI franchise components, divestiture options, and material asset portfolios though valuation estimates of the IDI franchise are no longer required.
- **Capabilities Testing:** Beginning in 2026, for each Group A IDI's initial submission the FDIC will conduct a horizontal test of the IDI's capabilities to establish and populate a VDR.
- **Credibility Determination:** The FDIC does not expect to make credibility determinations for each submission unless a submission is deemed to be not credible.

For more information, please contact Peter Torrente, Adam Levy, or Laura Byerly.

Contact the author:

Amy Matsuo
Principal and National Leader
Regulatory Insights
amatsuo@kpmg.com