

Regulatory Alert

Regulatory Insights

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Financial Stability: Nonbank Determination; Proposed Interpretive Guidance

KPMG Regulatory Insights:

Old is New: Proposal would revert to some elements of the Interpretive Guidance first introduced in 2019 but changed in 2023, including an activities-based approach to reviewing threats to financial stability, along with additional updates.

Activities vs. Entities: Priority will be on identifying and responding to risks from activities or practices across markets rather than on individual companies.

Off-Ramp Option: Under a new process, the FSOC would be able to identify steps a nonbank financial company could take to address potential risks to U.S. financial stability.

The Financial Stability Oversight Council (FSOC) has [issued](#) proposed interpretive guidance that would amend existing guidance on nonbank financial company determinations and the analytic framework for financial stability risks. In general, the proposal would reintroduce an activities-based approach for identifying and addressing potential risks to U.S. financial stability; replace, in its entirety, the FSOC’s 2023 Interpretive Guidance found in Appendix A of its regulations providing “Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies” (i.e., 12 CFR 1310) while leaving the rules intact; and rescind the 2023 Analytic Framework. (See KPMG Regulatory Alert on the 2023 Interpretive Guidance and Analytic Framework, [here](#).)

Key proposed changes and other modifications to the existing guidance consider:

- The analytic methodology, including new vulnerabilities that contribute to financial stability risks
- An activities-based approach to identifying, assessing, and responding to potential financial stability risks, with a process for FSOC members to act to address an identified risk
- A cost-benefit analysis before making a determination
- The interpretation of a “threat to financial stability”

- Steps a nonbank financial company may take to address a potential threat to financial stability

Comments will be accepted through May 14, 2026.

Proposed Amendments to the 2023 Interpretive Guidance

In late 2023, the FSOC approved guidance (the “2023 Interpretive Guidance”) that replaced the earlier “2019 Interpretive Guidance” and published an analytic framework (the “2023 Analytic Framework”) to describe the approach that the FSOC expected to take in identifying, assessing, and responding to certain potential risks to U.S. financial stability. The FSOC is now proposing select changes to this existing guidance, which encompasses the process the FSOC uses to determine (or “designate”) whether to subject a nonbank financial company to supervision and prudential standards by the Federal Reserve Board. The proposed changes address the following:

Analytic Methodology: The list of vulnerabilities that most commonly contribute to financial stability risks would be updated to include “impediments to economic growth and economic security” (such as through regulatory requirements, technological innovation) and “asset valuations” while “destabilizing activities” would be removed.

Updates to the analytic methodologies would be used in both designation and non-designation contexts.

Activities-Based Approach: As proposed, FSOC efforts to identify, assess, and respond to potential risks to U.S. financial stability would begin with an activities-based approach. (Note: a “risk to U.S. financial stability” would mean the potential for an event, act, or development (i.e., distinct from vulnerabilities) that could impair financial intermediation or financial market functioning to a degree that would be sufficient to inflict significant damage on the broader U.S. economy.) Entity-specific determinations would be pursued only if a potential risk to U.S. financial stability cannot be, or is not, adequately addressed through the activities-based two-step approach:

- **Step One:** Monitoring diverse financial markets and market developments on a system-wide basis, in cooperation and consultation with relevant financial regulatory agencies, to identify products, activities, or practices that could pose risks to U.S. financial stability. Analysis would address:
 - What shocks or other developments would trigger the potential risk and what vulnerabilities would be implicated?
 - How might adverse effects from the potential risk be transmitted to financial markets or participants?
 - What would be the potential effects on the U.S. financial system (e.g., scale, concentration)?
 - Could the potential effects impair the financial intermediation or financial market function to a such a degree that the U.S. economy could be “severely damaged”?
- **Step Two:** Working with the relevant financial regulatory agencies at the federal and state levels to respond to an identified potential risk that merits action (e.g.,

amending supervisory priorities, implementing new or enhanced standards.)

Cost-Benefit Analysis: Before making any determination/designation, the FSOC would conduct a cost-benefit analysis; a determination would be made only if the expected benefits (quantitative and qualitative) outweigh the expected costs. Expected benefits would include an assessment of the likelihood of the company’s risk of “material financial distress,” as well as whether the determination enhances financial stability and improves the functioning of markets by reducing the likelihood or severity of a potential financial crisis. Relevant costs to the company might include regulatory requirements (e.g., supervision, examination, capital/liquidity, innovation) while costs to the U.S. economy might include impact to the availability and cost of credit or financial products.

Threat to Financial Stability: The interpretation of a “threat to financial stability” would mean, the threat of an impairment of financial intermediation or of financial market functioning to a degree that would be sufficient to inflict “severe damage” on the broader U.S. economy. The FSOC suggests this is a higher threshold than “substantially impair” as used in the existing guidance.

Nonbank Financial Company Determinations: The process for making a nonbank financial company determination would “generally” remain consistent with existing guidance but a new step would be added where the FSOC would identify steps that a nonbank financial company or financial regulatory agencies would be allowed to take at a preliminary stage (i.e., following the Stage 1 evaluation process) – referred to as “remediation steps” - to address a potential threat to U.S. financial stability. The FSOC would generally expect “material risks” to be addressed within 180 days.

For more information, please contact [Todd Semanco](#) or [Laura Byerly](#).

Background

Pursuant to the Dodd-Frank Act (12 U.S.C. 5322), the purposes of the FSOC are “(A) to identify risks to the financial stability of the United States that could arise from the material financial distress or failure, or ongoing activities, of large, interconnected bank holding companies or nonbank financial companies, or that could arise outside the financial services marketplace; (B) to promote market discipline, by eliminating expectations on the part of shareholders, creditors, and counterparties of such companies that the Government will shield them from losses in the event of failure; and (C) to respond to emerging threats to the stability of the United States financial system.”

The Dodd-Frank Act gives the FSOC broad discretion to determine how to respond to potential threats to U.S. financial stability, including collecting information from regulators, requesting data and analyses from the Office of Financial Research, monitoring the financial services marketplace and financial regulatory developments, facilitating information sharing and coordination among regulators, recommending to the FSOC member agencies general supervisory priorities and principles, identifying regulatory gaps, making recommendations to the Federal Reserve Board or other primary financial regulatory agencies, and designating certain entities or payment, clearing, and settlement activities for additional regulation.

Nonbank financial companies subject to an FSOC determination/designation would be supervised by the Federal Reserve Board.

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