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Regulatory Alert

Financial Services Regulatory Insight Center

January 2018

Forthcoming regulatory reforms – Federal Reserve

Randal Quarles, Federal Reserve Board Vice Chair for Supervision, outlines early observations for improving financial regulation

Key points

- Post-crisis core reforms, including capital, liquidity, stress testing, and resolution, should be preserved but re-assessed based on experience since implementation.
- Assessments should consider the effectiveness of the regulations as well as identify improvements based on the principles of efficiency, transparency, and simplicity.
- Change is currently underway in the areas of: small bank capital, resolution planning, stress testing, the leverage ratio, and the Volcker Rule.
- Emerging points of focus include further tailoring of supervision and regulation, refining the "advanced approaches" thresholds, simplifying the loss absorbency framework, and enhancing stress testing disclosures.

Summary

In an effort to address the question "What's next?" and begin to clarify the course forward for financial regulation, Federal Reserve Vice Chair for Supervision, Randal Quarles, recently articulated his approach for evaluating and improving the post-crisis regulatory regime.

Having "spent the better part of the past decade building out and standing up the post-crisis regulatory regime," Vice Chair Quarles believes that "now is an eminently natural and expected time [for the regulatory agencies] to step back and assess those efforts." He added that, "given the breadth and complexity of this new body of regulation – it is inevitable that we will be able to improve them." Such assessments should look to the effectiveness of the regulations and identify improvements to address efficiency, transparency, and simplicity. Simplicity, he said, is a principle that promotes public understanding and meaningful compliance while reducing unexpected negative synergies among regulations.

Work has already begun in certain areas identified during the summer of 2017, including:

- Simplification of small bank capital (proposed rules have been published)

— Burden reduction in resolution planning, (reporting cycles for certain institutions have been extended, and Vice Chair Quarles would like to permanently extend submission cycles to every two years and reduce the reporting burden for less significant systemic footprints)

— Enhancements to stress testing (proposed rules have been published).

In addition, priority initiatives are directed toward:

— Recalibration of the leverage ratio (a proposal is expected to be published "relatively soon")

— Simplification of the Volcker Rule (interagency work has begun though a consensus rulemaking is expected to take some time).

At the direction of Vice Chair Quarles, Federal Reserve staff is engaged in a comprehensive review, including cost and benefit analyses, of the regulations in the core reform areas (capital, stress testing, liquidity, and resolution). Based on preliminary findings, Vice Chair Quarles is also considering regulatory reforms/improvements in a number of areas, starting first with identifying opportunities for further tailoring of supervision and regulation. In particular, he noted the following emerging areas of focus for regulatory improvements:

— Additional opportunities for tailoring supervision and regulation to the size, systemic footprint, risk profile, and business model of banking firms, including opportunities for larger, non-global systemically important banks (non-G-SIBs). He specifically called out the need for such distinction with regard to the liquidity coverage ratio (LCR) and internal stress testing requirements of the enhanced prudential standards as well as potentially to single counterparty credit limits and resolution planning requirements.

  – He supports increasing the $50 billion SIFI threshold or introducing a factor-based threshold.

— Enhancing stress testing disclosures by encouraging comment to improve the current proposal.

— Revisiting the "advanced approaches" thresholds for identifying internationally active banks.

— Simplifying the framework of loss absorbency requirements, which may include such things as "elimination of the advances approaches risk-based capital requirements, one or more ratios in stress testing, and simplification of TLAC (total loss-absorbing capacity) rule

— Rationalizing and recalibrating the framework for making determinations of control under the BCH Act.

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