Insights

Federal Reserve Board Proposes Risk-Based Capital Surcharges

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On December 9, 2014, the Board of Governors of the Federal Reserve System (the Federal Reserve) proposed a framework to establish risk-based capital surcharges for the largest, most interconnected U.S. bank holding companies pursuant to Section 165 of the Dodd-Frank Act. The proposed rule establishes a methodology to identify whether a U.S. bank holding company is a globally systemically important bank holding company (GSIB). A firm identified as a GSIB would be subject to a risk-based capital surcharge that is calibrated based on its systemic risk profile. The proposed rule is based on the international standard for GSIB capital surcharges adopted by the Basel Committee on Banking Supervision, with modifications that the Federal Reserve believes better reflect systemic concerns specific to the funding structures of large U.S. bank holding companies.

The proposed rule would require a U.S. top-tier bank holding company with $50 billion or more in total consolidated assets to calculate a measure of its systemic importance and would identify a subset of those firms as GSIBs based on that measure. Each GSIB would be subject to a risk-based capital surcharge that would increase its capital conservation buffer under the Federal Reserve's regulatory capital rule.

A firm that is designated as a GSIB would be required to calculate a GSIB capital surcharge using two methods and then use the higher of the two surcharges.

- **Method 1** would be based on the sum of a firm's systemic indicator scores reflecting its size, interconnectedness, cross-jurisdictional activity, substitutability and complexity.
- **Method 2** would use similar inputs but would replace the systemic indicator score of substitutability with a measure of the firm's use of short-term wholesale funding (including commercial paper notes).

Under Method 2, a percentage of secured wholesale funding (other than operational deposits) that is not secured by high quality liquid assets (as determined under the Federal Reserve's liquidity coverage ratio regulation) and unsecured wholesale funding (other than operational deposits) would be included in the determination of the GSIB capital surcharge based on the remaining maturity of the funding as follows:

Remaining Maturity Included Percentage 30 days or less
or no maturity 100% 31 to 90 days 75% 91 to 180 days 50% 181 to 365 days 25%

The proposed rule would include wholesale funding (such as commercial paper notes) of the GSIB and consolidated entities in the calculation. Wholesale funding issued by entities that are sponsored by, but not consolidated with, the GSIB, however, would not be included. The Federal Reserve is alternatively proposing that the wholesale funding of such sponsored entities be included.

The GSIB capital surcharge would become effective pursuant to the same timeline as the capital conservation buffer, which will be phased in beginning in 2016 at a rate of 25 percent per year and become fully effective on January 1, 2019.

Comments on the proposed rule are due by February 28, 2015.

For a copy of the proposed framework, click here.

For a copy of the Federal Reserve's press release, click here.