June 23, 2025

VIA ELECTRONIC SUBMISSION

Ann Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Re: Modifications to the Capital Plan Rule and Stress Capital Buffer Requirement (Docket R-1866 and RIN 7100-AG92)

Dear Ms. Misback:

The Financial Services Forum and the American Bankers Association (together, the "Associations")[1] appreciate this opportunity to submit this letter to the Federal Reserve Board (the "FRB") on its proposed rule (the "Proposal") to amend the calculation and annual effective date of the stress capital buffer ("SCB") requirement.[2] The Proposal is of significant importance to those of our member institutions that are subject to supervisory stress tests and the SCB requirement and, in particular, the eight U.S. global systemically important bank holding companies ("GSIBs").

We appreciate the FRB's efforts to reduce volatility of SCB requirements through the Proposal and welcome it as a useful first step in the FRB's previewed amendments to the broader stress testing framework. As discussed in Annex 2 to this letter, many aspects of the stress testing framework are in need of substantial reform, and the Proposal is but one component of the comprehensive effort that will be required to address the shortcomings of the stress testing framework. That said, efforts on other aspects of the framework should not delay finalization of a rule based on the Proposal. In this respect, we request that the FRB expeditiously adopt a final rule based on the Proposal and recommendations set forth in this letter. Doing so would be in line with the FRB's "inten[tion] to move expeditiously to initiate and complete … rulemaking proceedings" relating to the stress testing framework, including this Proposal.[3]

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1 A description of the Associations is included in Annex 1.

2 Modifications to the Capital Plan Rule and Stress Capital Buffer Requirement, 90 Fed. Reg. 16843 (Apr. 22, 2025).

3 Joint Motion to Stay Proceedings § 6, Case No. 2:24-cv-04300-ALM-CMV (S.D. Ohio May 23, 2025).

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In this letter, we wish to highlight the following key recommendations:

- **We strongly support a revised SCB rule becoming effective January 1, 2026**, provided that banking organizations may continue to operate under the existing rule's mechanics through September 30, 2026.

- **The final rule should adopt an asymmetric two-year averaging approach to the SCB requirement.** To address the asymmetric costs associated with increases in capital requirements identified by the Proposal, the final rule should provide that if a firm's stress capital decline in the current year is higher than the stress capital decline in the previous year, the firm's SCB requirement would be based on the average of the two stress capital decline values. However, if the firm's stress capital decline in the current year is lower than that of the previous year, the firm's SCB should be based solely on the current year's stress capital decline. This approach is consistent with the capital framework as a whole.

- **The final rule should remove the dividend add-on component of the SCB.** Given existing regulatory limitations on the payment of distributions and the FRB's authority to impose capital action restrictions if needed in specific cases, we believe the dividend add-on component of the SCB should be eliminated.

I. Effective Date; Transition Period.

As the FRB is aware, the Associations and other organizations, in their letter of May 16, 2025, requested that the FRB, no later than 14 calendar days before the scheduled date for the announcement of 2025 stress testing results, publicly announce that firms will be permitted to operate under the existing SCB framework through September 30, 2026, regardless of whether the FRB adopts revised SCB mechanics in a final rule with an effective date in that window. We are disappointed that the FRB has not yet made such an announcement, thus creating uncertainty with respect to the durability of banking organizations' capital requirements for SCBs taking effect on October 1, 2025. In line with that letter, we urge the FRB to state, when publishing stress testing results on June 27, 2025, that the current SCB rule's calculation mechanics will be available to banking organizations, regardless of whether the FRB finalizes a rule based on the Proposal with an effective date prior to October 1, 2026.

Assuming that the current SCB rule's calculation mechanics are available to banking organizations through September 30, 2026, **we support the Proposal's approach of an SCB requirement based on the rule becoming effective on January 1, 2026**.

Consistent with the letter of May 16, 2025, banking organizations should be able to choose to "opt in" to the revised mechanics upon the effective date of a final rule.[4]

Further, given that the FRB is currently in the early stages of proposing and adopting revisions to the stress testing framework, it is all the more important that a rule based on the Proposal be finalized expeditiously to address volatility introduced in the current stress testing cycle.

That said, moving the effective date of the SCB from October 1 to January 1, regardless of the year in which the transition occurs, creates uncertainty as to the SCB requirements that apply during the fourth quarter of the last year with an SCB effective date of October 1. We recommend that the final rule clarify that in the year that the revised SCB mechanics become effective (or, if they become effective January 1, 2026, a firm "opts in" to the revised mechanics), the SCB requirement effective through September 30 of that year would apply through December 31 of that year.

II. **Calculation of SCB Requirements.**

A. The final rule should adopt an asymmetric two-year averaging approach.

As the Proposal recognizes, averaging a firm's stress capital decline over multiple stress testing cycles reduces volatility in a firm's SCB requirement and better allows firms to allocate capital efficiently in support of the real economy. We believe that averaging stress testing results over two years addresses volatility while maintaining sufficient risk sensitivity.

The Proposal also recognizes the "asymmetric costs" associated with firms adjusting to higher capital requirements as opposed to adjusting to lower capital requirements.[5] In this regard, it considers as an alternative (Alternative 4), an asymmetric approach to results averaging. Under this approach, if a firm's stress capital decline in the current year is higher than the stress capital decline in the previous year, the firm's SCB would be based on the average of the two stress capital decline values. However, if the firm's stress capital decline in the current year is lower than that of the previous year, the firm's SCB would be based solely on the current year's stress capital decline. **We recommend that the FRB adopt this asymmetric approach as set forth in Alternative 4 in the Proposal.** Doing so would effectively address the asymmetric costs identified by the Proposal. And because it "offer[s] a less expensive framework for firms to manage their capital levels," firms would be better able to more cost-effectively serve their customers, leading to "more sustainable lending and other financial intermediation practices."[6]

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4 This section responds to Question 17.

5 90 Fed. Reg. at 16855.

6 *Id*. at 16854.

Accounting for asymmetric costs associated with increased capital requirements through asymmetric averaging is also congruent with other aspects of the FRB's capital framework. For example, increases in the GSIB surcharge become effective one full calendar year after decreases in the GSIB surcharge.[7] Similarly, increases in the countercyclical capital buffer generally take effect one year after the FRB announces an increase, while decreases take effect almost immediately.[8] Asymmetric averaging then would promote internal cohesion of the capital framework.

Finally, we do not believe, as the Proposal suggests, that such asymmetric averaging would "modestly reduce firms' average resilience to economic shocks."[9] Even when a firm's stress capital decline is lower than the previous year's, the firm's resulting SCB requirement still reflects the firm's maximum common equity tier 1 capital decline after a rigorous stress testing process. To suggest that result could reduce resilience is to cast doubt on the stress testing framework as a whole. We also believe suggestions that asymmetric averaging would *reduce* resilience are misguided because, in a given year, an SCB requirement calculated under the asymmetric averaging approach would either equal a firm's SCB requirement under the current rule or under the Proposal's symmetric averaging approach.

B. The final rule should remove the dividend add-on component of the SCB.

This section responds to Question 21 of the Proposal, which asks about "the advantages and disadvantages of removing the dividend add-on component from the calculation of a firm's stress capital buffer requirement."[10]

Under the current SCB rule, a firm's SCB requirement is determined based on its stress capital decline under the severely adverse scenario in the supervisory stress test for a given year and a dividend add-on component, which consists of four quarters of the firm's planned dividend payments. The FRB justified this approach in 2020 by citing it as "one way of promoting forward-looking dividend planning" and as a way to "mitigate procyclicality."[11] In practice, however, requiring firms to pre-capitalize dividends would be duplicative of, and inconsistent with, payout limitations under the capital rule.[12] In particular, if a firm's capital ratio were to breach its buffer, it could be restricted from actually paying the pre-capitalized dividends that comprise the buffer. Moreover, the FRB has a variety of supervisory tools to impose capital action restrictions if needed in

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7 12 CFR 217.403(d).

8 12 CFR 217.11(b)(2)(v).

9 90 Fed. Reg. at 16848.

10 *Id*. at 16850.

11 Regulations Q, Y, and YY: Regulatory Capital, Capital Plan, and Stress Test Rules, 85 Fed. Reg. 15576, 15579 (Mar. 18, 2020).

12 12 CFR 217.11(c)(1).

specific cases.[13] Accordingly, **the dividend add-on component should be removed from SCB requirements**.

Further, and in response to Question 7 in the Proposal, to our view, the capital rule's payout limitations also suggest that it is not necessary for the FRB to automatically impose consequences, including requiring a banking organization to resubmit its capital plans or seek prior approval for capital distributions if it undergoes or expects to undergo a material change.[14] Rather, material changes should only require prior approval for capital distributions if the banking organization would fall below applicable payout limitations.

III. Related Issues Presented by the Proposal.

A. The SCB requirement should not be floored at 2.5%.

To the extent the FRB, in line with our recommendation in Section II.B, above, removes the dividend add-on component of the SCB, the scenario mentioned in Question 20 – "where the firm, after subtracting the dividend add-on component, has a stress capital buffer requirement below the 2.5 percent stress capital buffer floor" – becomes more salient.[15] This section thus responds to Question 20.

A firm's SCB requirement is currently floored at 2.5%, meaning that a firm is subject to a 2.5% SCB requirement *even if its stress capital decline and dividend add-on component do not sum to 2.5%.* Flooring the SCB limits its use as a risk sensitive component of the capital framework because the floor definitionally requires banking organizations to overcapitalize beyond the levels required to continue lending (and making distributions) in a severely adverse scenario. **As such, we recommend that, to the extent the federal banking agencies seek to amend the capital conservation buffer, the FRB should eliminate the SCB floor.** Doing so would free up capital resources that can be used to support lending, including during economic downturns.

B. The FRB should undertake comprehensive, not piecemeal, revisions to its Stress Testing Policy Statement.

The Proposal would remove Section 2.3 of the FRB's Stress Testing Policy Statement, which provides that results of highly material supervisory model changes are phased in over a two-year period. We do not believe the FRB should amend the Stress Testing Policy Statement in such a piecemeal manner. Rather, the FRB should provide an

13 *See*, *e.g.*, 12 CFR Part 263, Subpart E.

14 12 CFR 225.8(e)(4); 12 CFR 225.8(j)(1).

15 90 Fed. Reg. at 16850.

opportunity to comment on the Statement as a whole as part of the FRB's previewed approach of seeking comment on other aspects of the stress testing framework.

C. The FRB should release more information as to the use of information collected on reporting forms to seek more informed feedback from the public.

In addition, the FRB proposes to revise the FR Y-14A/Q/M reporting forms to collect more information regarding compensation and non-recurring expenses, while removing certain items related to non-interest income from servicing activities that the FRB states are no longer needed for supervisory stress testing.[16]

We welcome efforts to streamline and focus reporting forms to collect salient information and appreciate Question 24 in the Proposal as to other potential modifications to the FR Y-14A/Q/M to reduce regulatory burden while allowing the FRB to conduct supervisory stress tests. However, because the public does not have visibility into how the FRB uses data gathered through the FR Y-14A/Q/M (and other) reporting forms, we cannot effectively answer the FRB's questions. Therefore, the FRB should provide the public with complete information as to how it uses line items in the FR Y-14A/Q/M so that the public can better provide the FRB with feedback as to how reporting forms could be improved.

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[16] *Id*. at 16856.

We would appreciate the opportunity to provide additional input for the FRB's consideration and would welcome the opportunity to meet to discuss our recommendations further. If you have any questions, please contact Sean Campbell of the Financial Services Forum by phone at (202) 821-2574 or by email at scampbell@fsforum.com or Hu Benton of the American Bankers Association by phone at (202) 663-5042 or by email at hbenton@aba.com.

Respectfully submitted,

Financial Services Forum
American Bankers Association

Annex 1

The **Financial Services Forum** is an economic policy and advocacy organization whose members are the eight largest and most diversified financial institutions headquartered in the United States. Forum member institutions are a leading source of lending and investment in the United States and serve millions of consumers, businesses, investors and communities throughout the country. The Forum promotes policies that support savings and investment, deep and liquid capital markets, a competitive global marketplace and a sound financial system.

The **American Bankers Association** is the voice of the nation's $24.2 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2.1 million people, safeguard $19.1 trillion in deposits and extend $12.6 trillion in loans.

Annex 2: Broader Stress Testing Policy Concerns[17]

As mentioned above, we appreciate the FRB's efforts to address volatility of SCB requirements through the Proposal. However, the volatility inherent in the stress testing process stems from more fundamental structural flaws in the design of the stress testing framework. Averaging stress capital decline across stress testing cycles does not address these underlying issues.

Here, we offer certain suggestions that the FRB should consider as part of revising its stress testing framework to bring it into compliance with the Administrative Procedure Act. We look forward to expanding on these points as part of the additional proposals for the comment the FRB has stated it will release by October 2025.

These comments relate to the stress testing framework more broadly; they should not cause the FRB to delay expeditiously adopting a final rule based on the Proposal. Moreover, these comments are not intended to comprehensively present our views as to the stress testing framework or the legal and policy flaws in the current framework.

The stress testing framework should not double count risks.

In considering revisions to the stress testing framework, the FRB should ensure that the same risks are not "double counted" between the FRB's capital rule and applicable buffers. For example, the FRB should not over-capitalize for operational, market, and credit valuation adjustment risk through overlaps between the SCB requirement and a future Basel III Endgame proposal.

The FRB should provide greater transparency to banking organizations with respect to models and stress testing results.

In communicating stress testing results to banking organizations, the FRB should provide the banking organization with complete and detailed firm-specific nonpublic information regarding the firm's stress testing performance and the calculation of the firm's SCB requirement. This transparency would better allow firms to understand their performance under the stress tests, making supervisory stress testing a more useful risk management tool for banking organizations, and would resolve some (but not all) of the legal flaws in the current framework. In addition, it would enable firms to meaningfully seek reconsideration of their SCB requirement.

We also believe, as the Proposal suggests, that the FRB should fully and clearly define the paths of additional variables in the stress testing scenarios. Doing so would improve

[17] This Annex 2 responds to Question 1.

consistency and further address volatility in capital requirements and help resolve some (but not all) of the legal flaws in the current framework.

Certain aspects of the stress testing framework should be recalibrated.

The Global Market Shock ("GMS") and Large Counterparty Default ("LCD") in particular should be recalibrated to improve risk sensitivity. For instance, the GMS's assumption of no liquidity over an extended period of time should be modified to an assumption of limited liquidity. In addition, the LCD should be modified to reflect a default based on the average of a banking organization's top counterparties, not the single largest counterparty.

Similarly, the supervisory pre-provision net revenue ("PPNR") and loan loss models should better align with market realities. For example, PPNR models should reflect higher trading income derived from client-driven activity during periods of volatility and the loan loss models should better reflect underlying collateral on secured loans.