

BETTER MARKETS, DENNIS KELLEHER

Proposal and Comment Information

Title: Enhanced Transparency and Public Accountability of the Supervisory Stress Test Models and Scenarios; Modifications to the Capital Planning and Stress Capital Buffer Requirement Rule, Enhanced Prudential Standards Rule, and Regulation LL, R-1873

Comment ID: FR-2025-0063-01-C17

Subject

RIN 7100-AH05

Submitter Information

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Submitted Date: 02/20/2026

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February 20, 2026

Benjamin W. McDonough
Deputy Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Re: Enhanced Transparency and Public Accountability of the Supervisory Stress Test Models and Scenarios; Modifications to the Capital Planning and Stress Capital Buffer Requirement Rule, Enhanced Prudential Standards Rule, and Regulation LL; Docket No. R-1873; RIN 7100-AH05; Document No. 2025-20211; 90 Fed. Reg. 51856 (Nov. 18, 2025)

Dear Ladies and Gentlemen:

Better Markets¹ appreciates the opportunity to comment on the Board of Governors of the Federal Reserve System's ("Fed") proposal to invite comment on the details of the stress test framework this year and annually and amend the policy statements that outline general policies for the stress testing framework ("Proposal").² The Proposal would fundamentally and structurally undermine the value of the stress testing framework for the largest, most complex bank holding companies that pose the greatest threat to financial stability, ultimately making it nothing but a charade. It is important to note that the Fed has made or proposed several other changes to the stress testing framework,³ and this Proposal contains only a portion of those changes, albeit a very important portion.

¹ Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans' jobs, savings, retirements, and more.

² Enhanced Transparency and Public Accountability of the Supervisory Stress Test Models and Scenarios; Modifications to the Capital Planning and Stress Capital Buffer Requirement Rule, Enhanced Prudential Standards Rule, and Regulation LL; Docket No. R-1873; RIN 7100-AH05; Document No. 2025-20211; 90 Fed. Reg. 51856 (Nov. 18, 2025), <https://www.federalregister.gov/documents/2025/11/18/2025-20211/enhanced-transparency-and-public-accountability-of-the-supervisory-stress-test-models-and-scenarios>.

³ Press Release, Board of Governors of the Federal Reserve System, *Due to Evolving Legal Landscape & Changes in the Framework of Administrative Law, Federal Reserve Board Will Soon Seek Public Comment on Significant Changes to Improve Transparency of Bank Stress Tests & Reduce Volatility Of Resulting Capital Requirements* (Dec. 23, 2024), <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20241223a.htm>.

The Proposal unnecessarily and irresponsibly publishes the full details of the stress testing framework, including details of both the loss estimation models and the scenario design framework, and would seek public comment on models and scenarios every year. Along with the irresponsible publication of the 2026 stress test scenarios for public comment,⁴ this Proposal will destroy the effectiveness of the stress testing framework. First, the Proposal undermines two key components of what makes an effective stress test: 1) a framework that is not easily gamed and 2) dynamism that allows the capture of salient and unseen or under-appreciated risks. Bank holding companies that undergo the stress test (“stress tested banks”) already are gaming the stress tests based on the current level of disclosed information, and publishing the full details of the framework allows the stress test to be gamed perfectly. Also, the stress tests already have lost a lot of dynamism because essentially the same scenario is used every year.

Second, the Proposal, in conjunction with other completed and proposed changes to the supervisory stress test framework, virtually guarantees that the associated capital requirement – the stress capital buffer or “SCB” – will be perpetually floored at the 2.5 percent minimum for most stress tested banks and will be at least close to that minimum floor for all stress tested banks. After this happens, there will be little difference between the risk-based capital requirements for the largest banks and the requirement for community banks.

Third, despite the pretext for the Proposal to respond to the evolving legal landscape, the Proposal has the opposite effect of opening up the Fed to even more litigation. Stress tested banks will be able to comment on and threaten litigation over every aspect of the stress testing framework, including model functional forms and coefficients.

While the stress tests began in the wake of the 2008 Financial Crisis (“2008 Crash”) as a robust framework that was strong enough to reassure regulators and the public that the banks were relatively strong and resilient to severely adverse events, the tests have been substantially weakened in recent years.⁵ The net effect of these past changes is a reduction in the amount of capital that large banks must maintain. These past changes combined with the several proposed changes completely undermine the value of the stress test and make the largest banks, the financial system, and the economy more vulnerable. In doing so, they also erode confidence that the banking system is resilient enough to withstand a severely stressful period without requiring another taxpayer-supported bailout. That eroding confidence alone will contribute to making bank failures and taxpayer bailouts more likely. Stress testing carried out that incorporates the many proposals being floated for weakening them, importantly including this Proposal will provide the American people with grossly false comfort that the banking system is safe.

⁴ See Better Markets comment letter re: Request for Comment on Scenarios for the Board's 2026 Supervisory Stress Test (December 1, 2025), <https://bettermarkets.org/wp-content/uploads/2025/12/Better-Markets-Comment-Letter-Federal-Reserve-Board-2026-Supervisory-Stress-Test.pdf>.

⁵ See, e.g., Shayna Olesiuk, *The Fed's Bank Stress Tests Protect Americans' Jobs and Homes: They Need to Be Stronger* 6-12, Better Markets Fact Sheet (May 29, 2025), <https://bettermarkets.org/wp-content/uploads/2025/05/Fact-Sheet-Stress-Tests-5.28.2025.pdf>.

Better Markets opposed previous changes to the stress test framework⁶ and strongly opposes this Proposal. The Proposal prioritizes banks' private interests over the public interest, makes the information provided by the stress test to the public worthless, and destroys the usefulness of the stress test and SCB in promoting a strong and resilient financial system.

BACKGROUND

In the aftermath of the 2008 Crash, fear permeated the country as millions of Americans lost their jobs, savings, and homes.⁷ Lending and economic activity ground to a halt because no one knew how big the losses were at the banks, which banks had enough capital to absorb those losses, or which were going to collapse next. For good reason, people were losing faith in the banking and financial systems, which was making everything worse. That downward spiral was stopped in large part because the government imposed very strong stress tests on the banks to determine which ones had enough capital to survive the economic downturn and which ones might not. Those that did not were required to increase their capitalization.

Stress testing of any system should use severe enough scenarios that can identify and remediate weaknesses in the system. In the context of the banking system, the American people rely on the Fed to develop a stress test that is sufficiently challenging to be an accurate indicator of the resilience of the largest banks in the face of a potential serious financial shock or economic downturn. Additionally, using strong stress tests to help set bank capital buffers reduces the chance of bank failures, crises, contagion, and taxpayer-funded bailouts of Wall Street's biggest banks. Done wrong, however, stress tests give false comfort, which could make crashes and bailouts more likely, and endanger Main Street families, businesses, and community banks. Perhaps more importantly, the credibility of the stress tests will be undermined and the confidence that banks could withstand a severely adverse operating environment or event will be reduced. That alone makes the system less safe and completely undermines the value of the stress tests.

Banks and regulators alike view the stress tests conducted during 2008 Crash as a great success because they provided much-needed information on banks financial condition and ultimately were used to require many of the largest banks to raise capital in the private markets, which helped to restore confidence in the financial system at a time of tremendous uncertainty. For example, the then-President and COO of Goldman Sachs, Gary Cohn, sang the praises of stress tests and capital:

⁶ See, e.g., *Conference: "Stress Testing: A Discussion and Review" Panel One "Stress Tests as Policy Tool"*, (July 19, 2019), <https://bettermarkets.org/analysis/conference-stress-testing-discussion-and-review-panel-one-stress-tests-policy-tool/>; Better Markets Comment Letter, *Enhanced Disclosure of the Models Used in the Federal Reserve's Supervisory Stress Test (Docket No. OP-1586)* ("Model Disclosure Proposal"); *Stress Testing Policy Statement (Docket No. OP-1587)* ("Stress Testing Policy Proposal"); and *Policy Statement on the Scenario Design Framework for Stress Testing (Docket No. OP-1588)* ("Scenario Design Proposal") (Jan. 22, 2018), https://bettermarkets.org/wp-content/uploads/2021/07/FRS-CL-Stress-Testing_0.pdf.

⁷ Better Markets, *Cost of the Crisis* (July 2015), https://bettermarkets.org/wp-content/uploads/2021/07/Better-Markets-Cost-of-the-Crisis-2_0.pdf.

[US banks were] subject to enormously robust stress tests here in the United States, and I give the Fed enormous credit for what they've done in stress testing the major banks here in the United States.⁸

Former Fed Governor Daniel Tarullo, in his final official speech before he departed from the Fed in 2017, said, stress tests are regarded as “the key innovation in capital regulation and supervision,” making other reforms, such as enhanced capital standards, “more effective.”⁹

Unfortunately, the Fed stress tests have been systematically and structurally weakened over time. Even now the stress test has been so gutted that the results provide false comfort and result in insufficient capital requirements. This Proposal will only make matters worse.

COMMENTS

I. THE PROPOSAL UNDERMINES TWO KEY COMPONENTS OF WHAT MAKES AN EFFECTIVE STRESS TEST – A FRAMEWORK THAT MINIMIZES GAMING AND IS DYNAMIC

The purpose of stress tests is to be stressful. In fact, stress testing in any context should push a system to its breaking point so that weaknesses can be identified and remediated. The first key factor to achieving this outcome is to minimize the ability of the test takers to reverse-engineer and game the test by keeping important details of the test from them. The reasons why this destroys the effectiveness of a stress test has been recognized by the Fed itself:

The Federal Reserve also believes there are material risks associated with fully disclosing the models to the firms subject to the supervisory stress test. One implication of releasing all details of the models is that firms could conceivably use them to make modifications to their businesses that change the results of the stress test without actually changing the risks they face. In the presence of such behavior, the stress test could give a misleading picture of the actual vulnerabilities faced by firms. Further, such behavior could increase correlations in asset holdings among the largest banks, making the financial system more vulnerable to adverse financial shocks. Another implication is that full model disclosure could incent banks to simply use models similar to the Federal Reserve's, rather than build their own capacity to identify, measure, and manage risk. That convergence to the Federal Reserve's model would create a “model monoculture” in which all firms have similar internal stress testing models, and this could cause firms to miss key idiosyncratic risks that they face.¹⁰

⁸ Dakin Campbell, *U.S. Banks Safer Than Europeans Due to Early Medicine*, BLOOMBERG (Feb. 9, 2016), <https://www.bloomberg.com/news/articles/2016-02-09/u-s-banks-safer-than-europeans-due-to-early-medicine-cohn-says>.

⁹ Board of Governors of the Federal Reserve System, *Departing Thoughts* (Apr. 4, 2017), <https://www.federalreserve.gov/newsevents/speech/tarullo20170404a.htm>.

¹⁰ 84 Fed. Reg. 6784.

Until this Proposal, the stance of the Fed was to limit the level of detail released about the stress testing framework. While the level of disclosure has increased since stress testing began,¹¹ the Fed has refrained from disclosing the full details of the framework to avoid the outcomes discussed above. This stance to refrain from full disclosure has lasted for fifteen iterations of Fed stress tests that have occurred since the first stress test was executed in 2009. Now, the Fed is proposing to disclose full details of:

- Equations, variables, and coefficients used in each model,
- Assumptions and limitations of each model,
- Rationales for modeling decisions,
- Discussions of alternative models, and
- Guides that are used to inform the Fed's scenario design, including the paths of variables in the macroeconomic scenario and the direction and severity of factors in the global market shock component.

This begs the question of why the Fed is now proposing to disclose the full details of the stress testing framework. Shockingly, the Fed acknowledges the reason in the Proposal:

[T]he Board believes more detailed information, beyond what is in the current Enhanced Model Disclosure, would improve the ability of firms to accurately assess how changes in their business activities might impact their supervisory stress test results and, relatedly, their stress capital buffer requirements and overall capital requirements.

That is, Proposal directly acknowledges that the Fed wants firms to be able to reverse-engineer the stress test results. Put another way, the Fed is saying the Proposal will allow firms to make “changes in their business activities” to bring about positive “impact to their supervisory stress test results and, relatedly, their stress capital buffer requirements and overall capital requirements.” That is the very definition of gaming and clearly an activity the Fed fully expects – in fact, encourages – stress tested banks to do.

The second key factor in designing a stress testing framework that is effective and actually stressful is ensuring the stress tests are dynamic from test to test so that it can capture salient and unseen or under-appreciated risks. By publishing not only the details of the models but also the specifics of the scenarios and the scenario design process for comment, the Fed is ensuring that the dynamism of the stress test will be completely eliminated.

Opening the supervisory stress test scenarios and the scenario design framework to public comment by the very banks to which the stress test applies ultimately will undermine the scenario design process and result in the scenarios being even more repetitive and historically tied than they already have been. Surely, each bank will object to any scenario design factors that would result

¹¹ Id.

in larger losses for itself under the stress test and will demand robust justification from the Fed for scenario variables and their paths. This will water down the severity of scenarios and make them predictable, allowing banks to limit their losses under the stress test. Models would be less dynamic as well.

As for the models, the Fed itself pointed out in the quote above that there would be a model monoculture among firms for their internal models. And similar to the scenarios, firms surely will object to any aspect of the model framework that leads to larger losses. Furthermore, making the models subject to the public comment process will slow their evolution so much that it will be pointless to make the updates in the first place. That is, by the time the updates are proposed and implemented, the changes would be out of date. That's exactly why the Board of Governors voted to delay the implementation of this year's stress test results into the SCB framework by one year.¹² So we don't have to guess that the public comment process will massively delay the implementation of the stress test, it's already happening.

The bottom line is, the Proposal completely destroys the stressfulness of the Fed's stress test and makes it a charade that is run each year with the same result.

II. THE PROPOSAL ALONG WITH OTHER CHANGES VIRTUALLY GUARANTEES ALL STRESS TESTED BANKS WILL BE CLOSE TO OR AT THE SCB MINIMUM EVERY YEAR

The stress test already has been weakened tremendously, mostly the result of changes that were implemented when the Fed ended the Comprehensive Capital Analysis and Review ("CCAR") program and switched to the SCB framework. The changes that weakened the stress test results the most were:

- Including only four quarters of dividend distributions, rather than the original nine quarters of both dividend distributions and share repurchases,
- Eliminating the assumption that firms' balance sheets grow during the nine-quarter capital planning horizon and instead assuming balance sheets remain static, and
- Publishing many previously undisclosed details of the stress test framework.¹³

The effects of these changes were immediately obvious.¹⁴ The average difference between starting and minimum common equity tier 1 capital ratios in the 2019 CCAR exercise for the eight

¹² See Board of Governors of the Federal Reserve System, *Federal Reserve Board finalizes hypothetical scenarios for its annual stress test and votes to maintain the current stress test-related capital requirements until public feedback can be considered* (February 4, 2026), <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20260204a.htm>.

¹³ As noted in the Proposal, the Fed increased the level of disclosure around the stress test framework in 2019 with the finalization of the Stress Testing Policy Statement (84 Fed. Reg. 6664) and the Enhanced Disclosure of the Models Used in the Federal Reserve's Supervisory Stress Test (84 Fed. Reg. 6784).

¹⁴ Analysis in this and the following paragraph are author's calculations based on data from the Fed's CCAR results, available at <https://www.federalreserve.gov/supervisionreg/ccar-by-year.htm>, and from the Fed's

U.S. global systemically important banks (“GSIBs”) was 5.7 percent, already down from an average of 7.1 percent in the 2015 CCAR exercise (the first year the common equity tier 1 requirement was fully included). The average GSIB SCB requirement in 2020 was only 3.5 percent, which essentially means there was a 2.2 percentage point decline in stress-related capital requirements after the changes noted above were implemented. That average GSIB SCB requirement declined even further to just 3 percent last year, barely above the 2.5 percent minimum of the SCB framework.

In fact, last year the SCBs for 5 of the 8 GSIBs were floored at the 2.5 percent minimum due to their results being lower than that figure (in some cases well below). For the three GSIBs that weren’t floored, their SCB requirements were an average of only 1.3 percentage points above the minimum. That was significantly down from 2020 where GSIBs that weren’t floored at the minimum had SCBs an average of 2.7 percentage points above the minimum. Across all 31 firms that were part of last year’s stress test, 40 percent of them were floored at the minimum.

Of course, the Proposal along with the Fed’s other proposal to publish the stress test scenarios for comment are allowing stress tested banks to further optimize their stress test results and associated SCBs. Surely, banks will game the stress test even more than they already do, and the 2026 SCBs will have even more stress tested banks that are floored at the 2.5 percent minimum as well as lower SCBs for those stress-tested banks that are not floored at the minimum.

III. THE PROPOSAL ACTUALLY OPENS THE FED UP TO MORE LITIGATION

In late 2024, the Fed announced that it would be seeking public comment on “significant changes to improve transparency” of its stress testing framework, and cited the pretext of “the evolving legal landscape” as the sole motivation.¹⁵ The announcement stated that the Fed would be proposing “disclosing and seeking public comment on all of the models that determine the hypothetical losses and revenue of banks under stress.” This Proposal is exactly that, and although the Proposal itself does not refer to potential litigation as a reason for disclosing the full details of the models and methodologies, the original announcement made clear that reason.

Of course, citing the legal landscape as a motivation has always been just a pretext. That is apparent in the fact that the Proposal ironically in fact actually opens up the Fed to more litigation that was the case prior to the proposal. That is, by making public the exact details of the models, including model functional forms and coefficients, as well as the scenario design framework the industry now can bring litigation against the Fed on each aspect of its stress testing framework – every variable, coefficient, assumption, set of rationale, design choices, etc.

¹⁵ annual large bank capital requirements, available at <https://www.federalreserve.gov/supervisionreg/large-bank-capital-requirements.htm>.
Board of Governors of the Federal Reserve System press release, *Due to evolving legal landscape & changes in the framework of administrative law, Federal Reserve Board will soon seek public comment on significant changes to improve transparency of bank stress tests & reduce volatility of resulting capital requirements* (December 23, 2024), <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20241223a.htm>.

Perhaps the Fed understands this already, and so it will use “the legal landscape” also on model variables and coefficients as a further pretext to weaken the stress test models to the point where they are worthless. This seems to be the motivation for publishing the full details of the models for public comment. In that way, stress testing banks can comment on aspects of the framework they don’t like, and the Fed can push through all the changes stress testing banks want based on the legal landscape pretext.

CONCLUSION

The Proposal and other completed and proposed changes to the supervisory stress test framework effectively destroy the purpose of the supervisory stress test and make it very likely that the SCB will be perpetually floored at the 2.5 percent minimum for most stress testing banks. The Proposal should be rescinded, although at this point stress testing banks already have seen the details of the framework.

We hope these comments are helpful and that the Fed stops undermining its mandate to conduct supervision and regulation of bank holding companies, especially for the largest bank holding companies.

Sincerely,



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