

## **FEDERAL RESERVE SYSTEM**

**Docket No. OP-1631**

### **Application of the RFI/C(D) Rating System to Savings and Loan Holding Companies**

**AGENCY:** Board of Governors of the Federal Reserve System (Board).

**ACTION:** Notice.

**SUMMARY:** The Board has determined that it will apply the RFI/C(D) rating system to certain savings and loan holding companies (SLHCs). This is the same supervisory rating system that the Board currently applies to bank holding companies (BHCs). SLHCs that are engaged in significant commercial or insurance activities will continue to receive indicative supervisory ratings. SLHCs with \$100 billion or more in assets will receive ratings under the RFI/C(D) rating system until the Board applies the Large Financial Institution Rating System to them.

**DATES:** The application of the supervisory rating system to SLHCs is effective February 1, 2019.

**FOR FURTHER INFORMATION CONTACT:** T. Kirk Odegard, Assistant Director and Chief of Staff, Policy Implementation and Effectiveness, (202) 530-6225, Karen Caplan, Assistant Director, (202) 452-2710, Angela Knight-Davis, Manager, (202) 475-6679, Division of Banking Supervision and Regulation; or Benjamin McDonough, Assistant General Counsel, (202) 452-2036, Keisha Patrick, Senior Counsel, (202) 452-3559, Laura Bain, Senior Attorney, (202) 736-5546, Trevor Feigleson, Senior Attorney,

(202) 452-3274, Legal Division, Board of Governors of the Federal Reserve System, 20th and C Streets, NW, Washington, DC 20551.

**SUPPLEMENTARY INFORMATION:**

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**I. Background**

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) transferred responsibility for the supervision of SLHCs from the Office of Thrift Supervision (OTS) to the Federal Reserve in July 2011.<sup>1</sup> Since 2011, the Board has applied the RFI/C(D) rating system (commonly referred to as the “RFI rating system”)<sup>2</sup>

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<sup>1</sup> 12 U.S.C. 5412(b)(1).

<sup>2</sup> Under the RFI rating system, BHCs generally are assigned individual component ratings for risk management (R), financial condition (F), and impact (I) of nondepository entities on subsidiary depository institutions. The risk management component is supported by individual subcomponent ratings for board and senior management oversight; policies, procedures, and limits; risk monitoring and management and information systems; and internal controls. The financial condition rating is supported by individual subcomponent ratings for capital adequacy, asset quality, earnings, and liquidity. An additional component rating is assigned to generally reflect the condition of any depository institution subsidiaries (D), as determined by the primary supervisor(s) of those subsidiaries. An overall composite rating (C) is assigned based on an overall evaluation of a BHC’s managerial and financial condition and an assessment of potential

to SLHCs on an “indicative” basis as a way of providing feedback to SLHCs regarding supervisory expectations while Federal Reserve staff and SLHCs each became familiar with the newly established statutory framework for supervision. Federal Reserve supervisory staff have assigned to each SLHC an “indicative rating,” which describes how the SLHC would be rated under the RFI rating system if applied to the company. These indicative ratings have not carried any supervisory or regulatory consequences.<sup>3</sup>

Prior to the transfer of supervisory responsibility for SLHCs, the OTS assigned supervisory ratings for SLHCs under the CORE rating system.<sup>4</sup> The CORE rating system and the RFI rating system substantially overlapped and generally included assessments of the same set of financial and non-financial factors and provided a summary evaluation of each holding company’s condition.

The Board did not adopt the CORE rating system upon taking over supervision of SLHCs. Instead, because the vast majority of SLHCs face similar risks and engage largely in the same activities as BHCs, the Board sought to apply the same RFI rating system to SLHCs as the Board currently applies to BHCs to promote consistency.

After completing a number of supervisory cycles in which the RFI rating system has been applied to SLHCs on an indicative basis, the Board evaluated the information

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future risk to its subsidiary depository institution(s). A simplified version of the RFI rating system that includes only the risk management component and a composite rating is applied to noncomplex BHCs with assets of \$3 billion or less. *See infra* note 16.

<sup>3</sup> All SLHCs that have been inspected have received at least one indicative rating.

<sup>4</sup> *See* 72 FR 72442 (December 20, 2007). Under the CORE rating system, SLHCs generally were assigned individual component ratings for capital (C), organizational structure (O), risk management (R), and earnings (E), as well as a composite rating that reflected an overall assessment of the holding company as reflected by consolidated risk management and financial strength.

gained from that process, taking into account the differences between SLHCs engaged in traditional banking activities and those engaged in significant commercial or insurance activities. Experience with this process over the past seven years indicates that the RFI rating system is an effective approach to communicating supervisory expectations to most SLHCs. On December 13, 2016, the Board published a notice in the Federal Register requesting comment on a proposal (proposal) to fully apply the RFI rating system to all SLHCs except those that are excluded from the definition of “covered savings and loan holding company”<sup>5</sup> in section 217.2 of the Board’s Regulation Q.<sup>6</sup>

## **II. Summary of Comments**

The comment period on the proposal closed on February 13, 2017. The Board received one comment from the Insurance Coalition,<sup>7</sup> which expressed support for continuing to apply the RFI rating system on an indicative basis to insurance SLHCs. The commenter also generally supported the Board’s proposed approach for assessing capital adequacy for SLHCs receiving indicative ratings, but suggested that such assessment also should explicitly consider (i) the unique risks in the insurance business

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<sup>5</sup> 12 CFR 217.2. Section 217.2 excludes the following SLHCs from the definition of “covered savings and loan holding company”: (1) a top-tier SLHC that is (i) an institution that meets the requirements of section 10(c)(9)(C) of the Home Owners’ Loan Act (12 U.S.C. 1467a(c)(9)(C)) and (ii) as of June 30 of the previous calendar year, derived 50 percent or more of its total consolidated assets or 50 percent of its total revenues on an enterprise-wide basis (as calculated under GAAP) from activities that are not financial in nature under section 4(k) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(k)); (2) a top-tier SLHC that is an insurance company; or (3) a top-tier SLHC that, as of June 30 of the previous calendar year, held 25 percent or more of its total consolidated assets in subsidiaries that are insurance underwriting companies (other than assets associated with insurance for credit risk).

<sup>6</sup> 81 FR 89941 (December 13, 2016).

<sup>7</sup> The Insurance Coalition is a group of federally supervised insurance companies and interested parties.

model, (ii) an insurance SLHC's compliance with State capital rules, and (iii) the policyholder protection mandate. The commenter also requested that the Board delay imposing a formal rating system on insurance SLHCs until the insurance capital rules have been finalized, and that the rating system be tailored to the insurance business model and reflect the State regulatory capital framework. The commenter requested that this same approach be applied for insurers that have been designated systemically important financial institutions by the Financial Stability Oversight Council (FSOC) for supervision by the Federal Reserve.

In response to this comment and consistent with the proposal, the Board has determined that it will continue to apply the RFI rating system to insurance SLHCs on an indicative basis. In response to the commenter's request that the assessment of the capital adequacy for insurance SLHCs receiving indicative ratings should consider certain factors, the Board clarifies that its assessment of insurance SLHCs has taken and will continue to take into account (i) the unique risks in the insurance business model, (ii) an insurance SLHC's compliance with State capital rules, and (iii) the policyholder protection mandate. The commenter's other suggestions pertain to factors that would be considered in the development of any future rating system applicable to insurance SLHCs and any insurance companies that the FSOC has determined should be supervised by the Board.

### **III. Applying the RFI Rating System to Certain SLHCs**

After reviewing the comment on the proposal, the Board has determined that it will apply the RFI rating system to every SLHC that is depository in nature.<sup>8</sup> SLHCs that are engaged in significant insurance or commercial activities will continue to receive indicative ratings under the RFI rating system. SLHCs that are depository in nature and have \$100 billion or more in total consolidated assets will be rated under the RFI rating system only until the Board applies the new rating system for large financial institutions (LFI rating system) to them, which the Board is adopting concurrently through a separate rulemaking and is described below.

Specifically, the Board will continue to assign indicative ratings under the RFI rating system to (i) SLHCs that derive 50 percent or more of their total consolidated assets or total revenues from activities that are not financial in nature under section 4(k) of the Bank Holding Company Act of 1956, as amended (12 U.S.C. 1843(k)) (commercial SLHCs), and (ii) SLHCs that are insurance companies or that hold 25 percent or more of their total consolidated assets in subsidiaries that are insurance companies (insurance SLHCs). The Board will continue to review whether a modified version of the RFI rating system or some other supervisory rating system is appropriate for commercial or insurance SLHCs on a permanent basis.

Subsequent to the closing of the public comment period, on August 17, 2017, the Board invited public comment on a separate notice of proposed rulemaking to adopt the

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<sup>8</sup> The RFI rating system will apply to every SLHC except an SLHC that is not a “covered savings and loan holding company” in section 217.2 of the Board’s Regulation Q. 12 CFR 217.2.

LFI rating system,<sup>9</sup> a supervisory ratings framework designed in part to align with the supervisory programs and practices that the Federal Reserve implemented for large financial institutions following the 2007-2009 financial crisis. The LFI rating system would have applied to, among other entities, BHCs and non-insurance, non-commercial SLHCs with total consolidated assets of \$50 billion or more, and U.S. intermediate holding companies (IHCs) of foreign banking organizations (FBOs) established under Regulation YY.<sup>10</sup>

In its final rulemaking regarding the LFI framework, which the Board is adopting concurrently with this notice, the Board has modified the scope of application of the LFI rating system to take into consideration statutory changes resulting from the enactment of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA) on May 24, 2018.<sup>11</sup> Section 401 of EGRRCPA amended section 165 of the Dodd-Frank Act to raise the \$50 billion minimum asset threshold for general application of enhanced prudential standards.<sup>12</sup> Immediately on the date of enactment, BHCs with total consolidated assets of less than \$100 billion were no longer subject to these standards. Accordingly, the final LFI rating system applies to BHCs and non-insurance, non-

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<sup>9</sup> 82 FR 39049 (August 17, 2017). Under the proposed LFI rating system, each large financial institution would have been assigned ratings for three separate components: Capital Planning and Positions; Liquidity Risk Management and Positions; and Governance and Controls. The ratings would have been assigned using a four-point non-numeric scale (Satisfactory/Satisfactory Watch, Deficient-1, and Deficient-2). A firm would need a “Satisfactory” or “Satisfactory Watch” rating for each of the three component ratings to be considered “well managed.” The proposal would not have included the assignment of a standalone composite rating or any subcomponent ratings.

<sup>10</sup> 12 CFR 252.153.

<sup>11</sup> Pub. L. 115-174, 132 Stat. 1296-1368 (2018).

<sup>12</sup> EGRRCPA § 401.

commercial SLHCs with total consolidated assets of \$100 billion or more, and to all U.S. IHCs of FBOs. The Board will assign ratings to SLHCs with \$100 billion or more in total consolidated assets under the final LFI rating system beginning in early 2020.

However, along with all other depository SLHCs, the RFI rating system will apply to SLHCs with \$100 billion or more in total consolidated assets beginning on February 1, 2019. Once the Board applies the LFI rating system to SLHCs with \$100 billion or more in total consolidated assets in early 2020, the Board will cease to use the RFI rating system to assign ratings to such large SLHCs. The Board believes it is important to assign ratings to all depository SLHCs at this time in order to promote consistent supervision and treatment of BHCs and SLHCs.

All components of the RFI rating system (*i.e.*, risk management, financial condition, and potential impact of the parent company and nondepository subsidiaries on subsidiary depository institution(s)) will apply to SLHCs that are depository in nature.<sup>13</sup> Likewise, the depository institution rating, which generally mirrors the primary regulator's assessment of the subsidiary depository institution(s), will apply. A numeric rating of 1 indicates the highest rating, strongest performance and practices, and least degree of supervisory concern; a numeric rating of 5 indicates the lowest rating, weakest performance, and the highest degree of supervisory concern.

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<sup>13</sup> Consistent with the approach for BHCs, when assigning a rating to an SLHC, supervisory staff will take into account a company's size, complexity, and financial condition. For example, a noncomplex SLHC with total assets less than \$3 billion will not be assigned all subcomponent ratings; rather, only a risk management component rating and composite rating generally will be assigned. These will equate, respectively, to the management component and composite rating under the CAMELS rating system for depository institutions, as assigned to the SLHC's subsidiary savings association by its primary regulator.

The financial condition component of the RFI rating includes a subcomponent that represents an assessment of capital adequacy. Compliance with minimum regulatory capital requirements is part of a broader qualitative and quantitative assessment of an SLHC's capital adequacy. As of January 1, 2015, certain SLHCs became subject to minimum capital requirements and overall capital adequacy standards.<sup>14</sup> For SLHCs subject to minimum regulatory capital requirements, assessment of the SLHC's compliance with those requirements will be one element of a broader qualitative and quantitative assessment of capital adequacy.<sup>15</sup>

Noncomplex SLHCs that are subject to the Board's Small Bank Holding Company and Savings and Loan Holding Company Policy Statement (Regulation Y, appendix C) (Policy Statement)<sup>16</sup> will be assigned an abbreviated version of the RFI rating system consistent with the Board's practice for BHCs outlined in SR letter 13-21.<sup>17</sup>

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<sup>14</sup> See 78 FR 62018, 62028 (October 11, 2013) (outlining the timeframe for implementation of Regulation Q for SLHCs and others).

<sup>15</sup> See Sections 4060 and 4061 of the *Bank Holding Company Supervision Manual*; Supervision and Regulation Letter 15-19 (December 18, 2015), available at <https://www.federalreserve.gov/bankinfo/srletters/sr1519.htm>; Supervision and Regulation Letter 15-6 (April 6, 2015), available at <https://www.federalreserve.gov/bankinfo/srletters/sr1506.htm>; Supervision and Regulation Letter 09-04 (February 24, 2009, revised December 21, 2015), available at <http://www.federalreserve.gov/boarddocs/srletters/2009/sr0904.htm>.

<sup>16</sup> 12 CFR part 225, Appendix C. The Board issued an interim final rule raising the asset size threshold for determining applicability of the Policy Statement from \$1 billion to \$3 billion of total consolidated assets. See 83 FR 44195 (August 30, 2018).

<sup>17</sup> Supervision and Regulation Letter 13-21 (December 17, 2013), available at <https://www.federalreserve.gov/bankinfo/srletters/sr1321.htm>. Shortly after adoption of this notice, Board staff expects to update Supervision and Regulation Letter 13-21 to modify inspection frequency and scope of expectations for holding companies with total consolidated assets between \$1 billion and \$3 billion to align with the Policy Statement's revised asset size threshold. See *supra* note 16.

An offsite review of the SLHC will be conducted upon receipt of the lead depository institution's report of examination. The supervisory cycle will be determined by the examination frequency of the lead depository institution and the SLHC will be assigned only a risk management rating and a composite rating.

Finally, elements of the RFI rating system that are codified in the Board's *Bank Holding Company Supervision Manual*<sup>18</sup> will be revised to describe the application of the RFI rating system to certain SLHCs that are depository in nature.<sup>19</sup> *Assessment of capital adequacy and supervisory guidance for SLHCs that receive indicative ratings*

For SLHCs that continue to receive an indicative rating under the RFI rating system, examiners will consider the risks inherent in the SLHC's activities and the ability of capital to absorb unanticipated losses, provide a base for growth, and support the level and composition of the parent company and subsidiaries' debt in the evaluation of the SLHC's capital adequacy. As discussed above in Supplementary Information Section II, for insurance SLHCs that receive an indicative rating, examiners will consider the unique risks in the insurance business model, an insurance SLHC's compliance with State capital rules, and the policyholder protection mandate.

In 2013, Board staff published several supervisory letters extending the use of the RFI rating system for, and assignment of, indicative ratings to SLHCs and extending the scope and frequency requirements for supervised holding companies with total

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<sup>18</sup> Available at [http://www.federalreserve.gov/boarddocs/supmanual/supervision\\_bhc.htm](http://www.federalreserve.gov/boarddocs/supmanual/supervision_bhc.htm).

<sup>19</sup> See Supervision and Regulation Letter 04-18 (December 6, 2014), available at <http://www.federalreserve.gov/boarddocs/srletters/2004/sr0418.htm>.

consolidated assets of \$10 billion or less to SLHCs. Commercial SLHCs and insurance SLHCs may refer to these letters for staff-level guidance on the use of indicative ratings until such time as the Board adopts final guidance on the application of a rating system tailored to these SLHCs.

#### **IV. Implementation**

The Board will begin to apply the RFI rating system on February 1, 2019 to all non-insurance and non-commercial SLHCs, including for any inspections commencing after that date. Federal Reserve staff will use the RFI rating system to assign ratings to non-commercial, non-insurance SLHCs with \$100 billion or more in total consolidated assets in 2019, and assign ratings to such SLHCs using the new LFI rating system beginning in early 2020. As noted, commercial SLHCs and insurance SLHCs will continue to receive RFI ratings on an indicative basis. The Federal Reserve's numeric ratings for SLHCs, which are confidential supervisory information, will be disclosed on a confidential basis, in accordance with current disclosure practices.<sup>20</sup> Under no circumstances should an SLHC or any of its directors, officers, or employees disclose or make public any of the ratings.

#### **V. Regulatory Analysis**

##### *Paperwork Reduction Act*

There is no collection of information required by this notice that would be subject to the Paperwork Reduction Act of 1995, 44 U.S.C. 3501 *et seq.*

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<sup>20</sup> 12 CFR 261.20.

### *Regulatory Flexibility Analysis*

The Regulatory Flexibility Act (RFA) requires that an agency publish an initial regulatory flexibility analysis (IRFA) in connection with a proposed rule or certify that the proposed rule will not have a significant economic impact on a substantial number of small entities.<sup>21</sup> An IRFA was included in the proposal to fully apply the RFI rating system to SLHCs that are not insurance or commercial SLHCs.<sup>22</sup> In the IRFA, the Board requested comment on the effect of the proposal on small entities and on any significant alternatives that would reduce the regulatory burden on small entities. The Board did not receive any comments on the IRFA.

The RFA requires an agency to prepare a final regulatory flexibility analysis (FRFA) unless the agency certifies that the rule will not, if promulgated, have a significant economic impact on a substantial number of small entities. The FRFA must contain: (1) a statement of the need for, and objectives of, the rule; (2) a statement of the significant issues raised by the public comments in response to the IRFA, a statement of the agency's assessment of such issues, and a statement of any changes made in the proposed rule as a result of such comments; (3) the response of the agency to any comments filed by the Chief Counsel for Advocacy of the Small Business Administration in response to the proposed rule, and a detailed statement of any changes made to the proposed rule in the final rule as a result of the comments; (4) a description of an estimate

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<sup>21</sup> 5 U.S.C. 601 *et seq.*

<sup>22</sup> 81 FR 89941 (December 13, 2016).

of the number of small entities to which the rule will apply or an explanation of why no such estimate is available; (5) a description of the projected reporting, recordkeeping and other compliance requirements of the rule, including an estimate of the classes of small entities which will be subject to the requirement and type of professional skills necessary for preparation of the report or record; and (6) a description of the steps the agency has taken to minimize the significant economic impact on small entities, including a statement for selecting or rejecting the other significant alternatives to the rule considered by the agency. In accordance with section 604 of the RFA, the Board has reviewed the final rule.

Under regulations issued by the Small Business Administration, a small entity includes an SLHC with assets of \$550 million or less.<sup>23</sup> Based on data as of September 11, 2018, there are approximately 132 SLHCs that have total domestic assets of \$550 million or less and are therefore considered small entities for purposes of the RFA. The final rule applies to all non-insurance and non-commercial SLHCs. Based on the Board's analysis, and for the reasons stated below, the Board believes the final rule will not have a significant economic impact on a substantial number of small entities.

1. *Statement of the need for, and objectives of, the application of the final rule.*

As discussed, the Board is fully applying the RFI rating system to non-insurance and non-commercial SLHCs to further the Board's goal of ensuring that holding

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<sup>23</sup> See 13 CFR 121.201. Effective July 14, 2014, the Small Business Administration revised the size standards for banking organizations to \$550 million in assets from \$500 million in assets. 79 FR 33647 (June 12, 2014).

companies that control depository institutions are subject to consistent standards and supervisory programs. After a seven-year adjustment period in which the Board assigned RFI ratings to SLHCs on an indicative basis, the Board has determined that the RFI rating system is an effective approach to communicating supervisory expectations to all non-insurance and non-commercial SLHCs.

2. *Significant issues raised by the public comments in response to the IRFA, a statement of the Board's assessment of such issues, and a statement of any changes made in the rule as a result of such comments.*

As noted above, the Board did not receive any comments on the IRFA and only received one responsive comment on the proposal. The comment did not raise any issues regarding the application of the RFI rating system to small entities. Instead, the comment expressed support for continuing to apply the RFI rating system on an indicative basis to insurance SLHCs and requested the Board consider certain issues in developing any future rating system that may be applied to insurance SLHCs and to insurance companies that the FSOC has determined should be supervised by the Federal Reserve.

Accordingly, no changes were made as a result of public comments.

3. *Response to any comments filed by the Chief Counsel for Advocacy of the Small Business Administration in response to the proposed rule, and detailed statement of any changes made to the proposed rule in the final rule as a result of the comments.*

The Chief Counsel for Advocacy of the Small Business Administration did not file any comments in response to the proposal.

4. *Description and estimate of the number of small entities to which the rule will apply.*

The application of the RFI rating system to non-insurance and non-commercial SLHCs will apply to approximately 191 SLHCs, of which only 132 SLHCs have \$550 million or less in total consolidated assets. Moreover, as discussed, noncomplex SLHCs under \$3 billion will be assigned an abbreviated version of the RFI rating system consistent with the Board's practice for BHCs outlined in SR 13-21.

5. *Description of the projected reporting, recordkeeping and other compliance requirements of the rule, including an estimate of small entities which will be subject to the requirement and the type of professional skills necessary for preparation of the report or record.*

The application of the RFI rating system does not impose any recordkeeping, reporting, or compliance requirements.

6. *Description of the steps taken to minimize the economic impact on small entities, including a statement for selecting or rejecting the other significant alternatives to the rule considered by the agency.*

As noted, noncomplex SLHCs under \$3 billion will be assigned an abbreviated version of the RFI rating system consistent with the Board's practice for BHCs outlined in SR 13-21. An offsite review of the SLHC will be conducted upon receipt of the lead depository institution's report of examination. The supervisory cycle will be determined by the examination frequency of the lead depository institution and the SLHC will be assigned only a risk management rating and a composite rating.

Moreover, SLHCs have been subject to the RFI rating system on indicative basis for the past seven years, which has provided SLHCs the opportunity to adjust to the RFI rating system. The full application of the RFI rating system to small non-commercial and non-insurance SLHCs will not create any new economic impact on small entities.

In light of the foregoing, the Board does not believe that this final rule will have a significant economic impact on any small entities and therefore believes that there are no significant alternatives that would reduce the economic impact on small entities.

By order of the Board of Governors of the Federal Reserve System, November 2, 2018.

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Ann Misback,  
*Secretary of the Board.*