Date: October 16, 2025

To: Board of Governors

From: Staff[1]

Subject: Final Notice Adopting Revisions to the Large Financial Institution Rating System and Framework for the Supervision of Insurance Organizations

ACTIONS REQUESTED:

Staff requests approval to publish in the *Federal Register* the attached draft final notice, which would finalize revisions to the Large Financial Institution rating system (LFI Framework) and Framework for the Supervision of Insurance Organizations (Insurance Supervisory Framework, together with the LFI Framework, the Frameworks). Staff also requests authority to make technical, non-substantive changes to the attached materials to prepare them for publication in the *Federal Register*.

EXECUTIVE SUMMARY:

- The vast majority of large financial institutions are well capitalized and have sound liquidity positions and good asset quality. However, approximately 47 percent of large financial institutions are not "well managed" under the current LFI Framework.
- The revisions contained in the final notice would result in the Frameworks more appropriately reflecting the financial and operational strength and resilience of firms subject to the Frameworks and align the Frameworks with other existing supervisory rating systems.
- The current Frameworks evaluate firms based on three components: capital planning and positions, liquidity risk management and positions, and governance and controls. Each component is rated based on a four-point non-numeric scale: Broadly Meets Expectations, Conditionally Meets Expectations, Deficient-1, and Deficient-2. A firm

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that receives any component rating of Deficient-1 or Deficient-2 is not currently considered "well managed."

- After carefully considering the comments received on the proposal, staff recommends finalizing the revisions largely as proposed and updating certain references, including removing a reference to reputational risk, in the Insurance Supervisory Framework.

BACKGROUND ON CURRENT FRAMEWORKS AND PROPOSAL:

The Frameworks[2] establish a supervisory rating system for certain holding companies[3] and include three components: capital planning and positions, liquidity risk management and positions, and governance and controls. Each component is rated based on a four-point non-numeric scale (in descending order): Broadly Meets Expectations,[4] Conditionally Meets Expectations,[5] Deficient-1,[6] and Deficient-2.[7] A firm that receives a rating of Deficient-1 or Deficient-2 in any component rating is not considered "well managed" under the Frameworks and the Bank Holding Company Act (BHC Act).[8] Moreover, the Frameworks establish a presumption that the Board will impose a formal or informal enforcement action on any firm with a Deficient-1 or Deficient-2 component rating.

On July 15, 2025, the Board proposed to modify the Frameworks[9] such that a firm with at least two Broadly Meets Expectations or Conditionally Meets Expectations component ratings and no more than one Deficient-1 component rating would be considered "well managed." In

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2 83 Fed. Reg. 58724 (Nov. 21, 2018); SR Letter 19-3 / CA Letter 19-2, Large Financial Institution (LFI) Rating System (Feb. 26, 2019), https://www.federalreserve.gov/supervisionreg/srletters/sr1903.htm; 87 Fed. Reg. 60160 (Oct. 4, 2022); SR Letter 22-8, Framework for the Supervision of Insurance Organizations (Sept. 28, 2022), https://www.federalreserve.gov/supervisionreg/srletters/SR2208.htm.

3 The LFI Framework applies to (i) bank holding companies and non-insurance, non-commercial savings and loan holding companies with total consolidated assets of $100 billion or more, and (ii) U.S. intermediate holding companies of foreign banking organizations with total consolidated assets of $50 billion or more. The Insurance Supervisory Framework applies to depository institution holding companies significantly engaged in insurance activities (supervised insurance organizations).

4 Indicates that a firm's practices and capabilities broadly meet supervisory expectations, and the firm possesses sufficient financial and operational strength and resilience to maintain safe and sound operations through a range of conditions.

5 Indicates that there are certain material financial or operational weaknesses in a firm's practices or capabilities that may place the firm's prospects for remaining safe and sound through a range of conditions at risk if not resolved in a timely manner during the normal course of business.

6 Indicates that there are financial or operational deficiencies in a firm's practices or capabilities, which put the firm's prospects for remaining safe and sound through a range of conditions at significant risk.

7 Indicates that there are financial or operational deficiencies in a firm's practices or capabilities that present a threat to the firm's safety and soundness, or have already put the firm in an unsafe and unsound condition.

8 See 12 U.S.C. § 1841(o)(9); 12 CFR 225.83, 238.66(b).

9 90 Fed. Reg. 31641 (July 15, 2025).

addition, the Board proposed to remove the presumption in the Frameworks that the Board will impose an enforcement action on firms with one or more Deficient-1 component ratings. Instead, decisions to impose enforcement actions on those firms would be made based on the particular facts and circumstances of the firm.

DISCUSSION:

Summary of Comments Received

The Board received ten comments on the proposal. Commenters included industry groups, public interest groups, academics, members of Congress, and other interested parties. Certain commenters expressed general support for the proposal and recommended expeditiously adopting the proposal. These commenters stated that the proposal would more accurately reflect a firm's financial and operational strength and resilience to maintain safe and sound operations through a range of conditions, including stressful ones, and thus appropriately increase firms' ability to expand efficiently, reduce compliance costs, and increase innovation. Further, these commenters asserted that the proposal would enable firms to more efficiently allocate resources between resolving material financial issues and serving customers and competing within the financial sector.

Other commenters opposed the proposal overall, stating that it was unnecessary and would increase risks to safety and soundness. Some of these commenters cited historical examples of firms that have failed, expressing concern that the proposal would have treated certain of these firms as "well managed." Other commenters also stated that the proposal would encourage growth in large banking organizations, presenting financial stability risks and increasing competitive disadvantages for community banks. One commenter also asserted the proposal was inconsistent with the Administrative Procedure Act.

Additionally, several commenters provided more specific views on the proposal's "well managed" definition and enforcement action presumption, as well as the proposal's economic analysis. While there were no comments submitted that were specific to the Insurance Supervisory Framework, some comments may still be relevant to the Insurance Supervisory Framework and have been considered in that context as well.

Overview of Final Notice[10]

Staff has considered all comments and recommends finalizing the proposal largely as proposed. The final notice would revise the Frameworks such that a firm with at least two Broadly Meets Expectations or Conditionally Meets Expectations component ratings and no more than one Deficient-1 component rating would be "well managed."[11] The final notice also would remove the presumption in the Frameworks that the Board will impose a formal or informal enforcement action on firms with one or more Deficient-1 ratings. Instead, firms with one or more Deficient-1 ratings may be subject to a formal or informal enforcement action by the Board, depending on the particular facts and circumstances of the firm.[12]

Additionally, the final notice would revise the text of the Insurance Supervisory Framework to remove a reference to reputational risk and update references to outdated supervisory guidance.[13]

The revisions contained in the final notice would result in the Frameworks more appropriately reflecting the financial and operational strength and resilience of firms subject to the Frameworks. Further, the final notice would reflect that a firm with a single component rating of Deficient-1 would generally have sufficient financial and operational strength and resilience to operate in a safe and sound manner through a range of conditions, if the other two components have a rating of Broadly Meets Expectations or Conditionally Meets Expectations.

By taking a more comprehensive approach, the final notice would more closely align the Frameworks with other existing supervisory rating systems.[14] No supervisory rating system applicable to Board-supervised institutions determines a firm's composite rating, which is relevant to its "well managed" status, based solely on a single component rating.[15]

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[10] In addition to this final notice, staff plans to develop and present for Board consideration at a later date more comprehensive changes to supervisory rating systems, including the Frameworks, that apply to Federal Reserve-supervised institutions.

[11] Consistent with the current Frameworks, a firm would not be "well managed" if it receives a Deficient-1 for two or more component ratings, or if it receives a Deficient-2 for any of the component ratings.

[12] The Frameworks would continue to include a presumption that the Board will impose a formal enforcement action on firms with one or more Deficient-2 component ratings.

[13] These changes are reflected in Appendix B of the final notice.

[14] See, e.g., 61 Fed. Reg. 67021 (Dec. 12, 1996); 70 Fed. Reg. 44256 (Aug 2, 2005); and SR Letter 96-36, Guidance on Evaluating Activities Under the Responsibility of U.S. Branches, Agencies and Nonbank Subsidiaries of Foreign Banking Organizations (Dec. 19, 1996), https://www.federalreserve.gov/boarddocs/srletters/1996/sr9636.htm.

[15] See, e.g., SR Letter 19-4 / CA Letter 19-3, Supervisory Rating System for Holding Companies with Total Consolidated Assets Less than $100 Billion (Feb. 26, 2019),

ECONOMIC ANALYSIS:

As of the third quarter of 2025, 36 holding companies were subject to the LFI Framework, of which 17 were not considered "well managed" under the LFI Framework. Staff estimates that the final notice would decrease the number of holding companies that are not "well managed" under the LFI Framework by seven. In addition to being "well managed" under the LFI Framework, a firm must be "well managed" at each of its depository institution subsidiaries to elect to be treated as a financial holding company, which, for example, permits the firm to engage in certain activities and invest in certain nonbank financial companies without obtaining prior Board approval. As a result, the revisions to the LFI Framework would likely have a more limited impact: only three of the seven firms whose holding companies would become "well managed" under the final notice would also become "well managed" under the BHC Act, as of the third quarter of 2025.

As of the third quarter of 2025, there were four firms subject to the Insurance Supervisory Framework. Under the final notice, one supervised insurance organization will see a change in its status to "well managed" under the BHC Act.

As a result of the final notice, firms subject to the Frameworks would face reduced compliance costs, and those that become "well managed" as a result of the final notice would be able to more easily pursue certain activities such as investments in new businesses, supporting financial innovation. Moreover, the final notice is likely to enhance supervisory efficiency and efficacy by ensuring that the definition of "well managed" reflects a firm's overall condition. These benefits justify the costs of the final notice, which include a potential increase in risk-taking as firms may be less incentivized to remediate single Deficient-1 component ratings. Supervisors would continue to monitor the remediation of supervisory issues, mitigating this cost and encouraging the resolution of these issues in an appropriate timeframe.

RECOMMENDATIONS:

Based on the foregoing, staff recommends that the Board approve the attached final notice for publication in the *Federal Register*. Staff also recommends that the Board delegate to

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https://www.federalreserve.gov/supervisionreg/srletters/sr1904.htm; SR Letter 96-38, Uniform Financial Institutions Rating System (Dec. 27, 1996), https://www.federalreserve.gov/boarddocs/srletters/1996/sr9638.htm; SR Letter 00-14, Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations (revised Oct. 23, 2020), https://www.federalreserve.gov/boarddocs/srletters/2000/sr0014.htm.

staff authority to make technical, non-substantive changes to the attached materials to prepare them for publication in the *Federal Register*.

Attachment