LUSE GORMAN

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LEGAL UPDATES AND NEWS

Federal Reserve Board Sets Out Policies For Savings and Loan Holding Company Supervision and Capital Assessment

The Federal Reserve Board ("FRB" or "Board") is seeking comment on a Notice it recently issued which outlines its intended policies with respect to the supervision of savings and loan holding companies ("SLHCs"), including the assessment of regulatory capital. Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act"), the FRB is scheduled to assume the responsibilities of the Office of Thrift Supervision ("OTS") as to SLHCs on July 21, 2011.

The Notice reflects the FRB's general intention of applying to SLHCs the supervisory policies applicable to similarly situated bank holding companies, except to the extent that any unique characteristics of SLHCs require otherwise. The FRB's stated supervisory objective is to "ensure that the SLHC and its nondepository subsidiaries are effectively supervised and can serve as a source strength for, and do not threaten the soundness of" its subsidiary institution[s].

Large and regional SLHCs (generally consolidated assets of $10 billion or more) will be subject to the FRB's consolidated supervision program, which involves risk-based consolidated supervision that ties the frequency and intensity of supervisory activities (*e.g.*, monitoring, on site inspections, testing) to the size, complexity and perceived risk of the particular holding company. While noting that the FRB's program has some similarities to OTS' current approach, the Notice states that some large and regional SLHCs may be subjected to more rigorous supervision than what they have been experiencing with the OTS.

Smaller SLHCs would generally be supervised according to the FRB program applicable to similarly situated bank holding companies. A noncomplex shell holding company of less than $1 billion in assets, should expect no on-site FRB review, but rather ratings based on the examination of their lead depository institution subsidiary. A noncomplex holding company with total consolidated assets of between $1-10 billion will usually receive a limited scope on-site inspection every two years. A complex bank holding company (*i.e.*, determined based on factors such as complicated structures, material intercompany transactions involving the depository institution subsidiary, significant non bank activities, material public debt, etc.) and any holding company whose depository institution subsidiary receives less than a satisfactory composite or management ratings, receives greater scrutiny. The Notice also suggests that SLHCs will become subject to the rating system that the FRB currently uses for bank holding companies.

The Notice addresses the differences between OTS and FRB practices as to assessing holding company capital adequacy. In contrast to the FRB, the OTS does not have minimum capital ratio standards for SLHCs. However, the Dodd-Frank Act requires the FRB to issue new minimum leverage and risk-based requirements for both SLHCs and bank holding companies

that are not less stringent than those applicable to depository institutions themselves. The Notice indicates the FRB's intent that the application of consolidated capital requirements to SLHCs be addressed as part of the banking agencies' rulemaking process later this year and into 2012 concerning the application of the BASEL III capital standards to all depository institutions and their holding companies. According to the Notice, the FRB is considering applying to SLHCs the same consolidated capital requirements applicable to bank holding companies, except as necessary to accommodate any unique characteristics of SLHCs. Until the regulations are finalized, the FRB intends to evaluate the capital adequacy of SLHCs similarly to OTS' approach, i.e., a qualitative and quantitative assessment.

The Notice recognizes that the Dodd-Frank Act expressly preserved the FRB's Small Bank Holding Company Policy Statement which, if continued, would exempt bank holding companies of under $500 million in consolidated assets from the new consolidated capital requirements. However, the Notice also states that Dodd-Frank Act "did not expressly provide a similar exemption" for similarly situated SLHCs. The Notice is silent on the FRB's predisposition (or lack thereof) to create a similar exception by regulation for SLHCs. The Notice also does not address the Dodd-Frank Act language that requires a five year transition period (from the July 21, 2010 effective date of Dodd-Frank Act) before the statutorily-required consolidated holding company capital requirements may apply to holding companies that were not regulated by the FRB as of May 19, 2010, which should include SLHCs in existence on that date.

As mentioned previously, the Notice makes clear that the FRB intends to consider whether aspects of its supervisory practices regarding bank holding companies are inappropriate for SLHCs due to their unique characteristics. The FRB is accepting comments until May 23, 2011 on the proposed supervisory scheme for SLHCs outlined in the Notice.

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