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FEDERAL RESERVE SYSTEM

12 CFR Chapter II

[Docket No. OP-1589]

Federal Reserve Policy on Payment System Risk; U.S. Branches and Agencies of Foreign Banking Organizations

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Policy statement; request for comment.

SUMMARY: The Board of Governors of the Federal Reserve System ("Board") is requesting comment on proposed changes to part II of the Federal Reserve Policy on Payment System Risk ("PSR policy") related to procedures for determining the net debit cap and maximum daylight overdraft capacity of a U.S. branch or agency of a foreign banking organization ("FBO"). Under the PSR policy, an FBO's strength of support assessment ("SOSA") ranking can affect its eligibility for a positive net debit cap, the size of its net debit cap, and its eligibility to request a streamlined procedure to obtain maximum daylight overdraft capacity. Additionally, an FBO that is a financial holding company ("FHC") can generally receive a higher net debit cap than an FBO that is not an FHC, and is generally eligible to request a streamlined procedure to obtain maximum daylight overdraft capacity. The proposed changes to the PSR policy would remove references to the SOSA ranking; remove references to FBOs' FHC status; and adopt alternative methods for determining an FBO's eligibility for a positive net debit cap, the size of its net debit cap, and its eligibility to request a streamlined procedure to obtain maximum daylight overdraft capacity. The Board recognizes that the proposed changes would reduce net debit caps for some FBOs, but the Board believes that the adjusted FBO net debit caps would be better tailored to FBOs' actual usage of intraday credit and would not constrain FBOs' U.S. operations.

DATES: Comments on the proposed changes must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments, identified by Docket No. OP-1589, by any of the following methods:

- Agency Web Site: http://www.federalreserve.gov. Follow the instructions for submitting comments at http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm.
- Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions for submitting comments.
- E-mail: regs.comments@federalreserve.gov. Include docket number in the subject line of the message.
- FAX: 202/452-3819 or 202/452-3102.
- Mail: Ann E. Misback, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, DC 20551.

All public comments are available from the Board's web site at www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm as submitted, except as necessary for technical reasons. Accordingly, your comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper in Room 3515, 1801 K Street NW. (between 18th and 19th Streets NW.), Washington, DC 20006 between 9:00 a.m. and 5:00 p.m. on weekdays.

FOR FURTHER INFORMATION CONTACT: Jeffrey Walker, Assistant Director (202-721–4559), Jason Hinkle, Manager (202-912-7805), or Alex So, Senior Financial Services Analyst (202-452-2300), Division of Reserve Bank Operations and Payment Systems; or Evan Winerman, Counsel (202-872-7578), Legal Division, Board of Governors of the Federal Reserve

System. For users of Telecommunications Device for the Deaf (TDD) only, please call 202-263–4869.

SUPPLEMENTARY INFORMATION:

I. Current Use of SOSA Ranking and FHC Status in the PSR Policy

Part II of the PSR policy establishes the maximum levels of daylight overdrafts that depository institutions ("institutions") may incur in their Federal Reserve accounts.[20] As described further below, an FBO's SOSA ranking—which assesses an FBO's ability to provide financial, liquidity, and management support to its U.S. operations—can affect the FBO's daylight overdraft capacity. Similarly, an FBO's status as an FHC can affect its daylight overdraft capacity.[21]

A. Net Debit Caps

An institution's net debit cap is the maximum amount of uncollateralized daylight overdrafts that the institution can incur in its Federal Reserve account. The PSR policy generally requires that an institution be "financially healthy" to be eligible for a positive net debit cap.[22] To that end, the *Guide to the Federal Reserve's Payment System Risk Policy* ("Guide") clarifies that most FBOs with a SOSA ranking of 3 or a U.S. Operations Supervisory Composite Rating of marginal or unsatisfactory generally do not qualify for a positive net debit cap.[23]

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[20] *See* https://www.federalreserve.gov/paymentsystems/files/psr_policy.pdf.

[21] The Gramm-Leach-Bliley Act defines a "financial holding company" as a bank holding company that meets certain eligibility requirements. In order for a bank holding company to become a financial holding company and be eligible to engage in the new activities authorized under the Gramm-Leach-Bliley Act, the Act requires that all depository institutions controlled by the bank holding company be well capitalized and well managed (12 U.S.C. 1841(p)). With regard to a foreign bank that operates a branch or agency or owns or controls a commercial lending company in the United States, the Act requires the Board to apply comparable capital and management standards that give due regard to the principle of national treatment and equality of competitive opportunity (12 U.S.C. 1843(l)).

[22] *See* Part II.D.1 of the PSR Policy.

[23] Section VI.A.1 of the Guide states that "[m]ost SOSA 3-ranked institutions do not qualify for a positive net debit cap," though it clarifies that "[i]n limited circumstances, a Reserve Bank may grant a net debit cap or extend

Assuming that an institution qualifies for a positive net debit cap, the size of its net debit cap equals the institution's "capital measure" multiplied by its "cap multiple."[24] As described further below, an institution's capital measure is a number derived (under most circumstances) from the size of its capital base. An institution's cap multiple is determined by the institution's "cap category," which generally reflects, among other things, the institution's creditworthiness. An institution with a higher capital measure or a higher cap category (and thus a higher cap multiple) will qualify for a higher net debit cap than an institution with a lower capital measure or lower cap category.

An FBO's SOSA ranking can affect both its cap category and its capital measure. An FBO's status as an FHC can affect its capital measure.[25]

1. Cap categories and cap multiples

Under Section II.D.2 of the PSR policy, an institution's "cap category" is one of six classifications—high, above average, average, de minimis, exempt-from-filing, and zero. In order to establish a cap category of high, above average, or average, an institution must perform a self-assessment of its own creditworthiness, intraday funds management and control, customer credit policies and controls, and operating controls and contingency procedures. Other cap categories do not require a self-assessment.[26] Each cap category corresponds to a "cap

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intraday credit to a financially healthy SOSA 3-ranked FBO." Separately, Table VII-2 of the Guide states that SOSA-3 ranked FBOs and FBOs that receive a U.S. Operations Supervisory Composite Rating of marginal or unsatisfactory have "below standard" creditworthiness, and Table VII-3 of the Guide states that institutions with below standard creditworthiness cannot incur daylight overdrafts.

[24] *See* Part II.D.1 of the PSR Policy. All net debit caps are granted at the discretion of the institution's Administrative Reserve Bank, which is the Reserve Bank that is responsible for managing an institution's account relationship with the Federal Reserve.

[25] In contrast, the FHC status of a domestic bank holding company does not affect its capital measure.

[26] An institution that meets reasonable safety and soundness standards can request a de minimis cap category, without performing a self-assessment, by submitting a board of directors resolution to its Administrative Reserve Bank. An institution that only rarely incurs daylight overdrafts in its Federal Reserve account that exceed the lesser

multiple."[27] As noted above, an institution's net debit cap generally equals its capital measure multiplied by its cap multiple.

An FBO's SOSA ranking can affect its cap category (and thus its cap multiple). As noted above, an institution that wishes to establish a net debit cap category of high, above average, or average must perform a self-assessment of, among other things, its own creditworthiness. Under Part II.D.2.a of the PSR policy, "[t]he assessment of creditworthiness is based on the institution's supervisory rating and Prompt Corrective Action (PCA) designation." Part VII.A of the Guide includes a matrix for assessing *domestic* institutions' creditworthiness that incorporates an institution's supervisory rating and PCA designation. Because FBOs do not receive PCA designations, however, Part VII.A of the Guide includes a separate matrix for assessing FBO creditworthiness that incorporates an FBO's U.S. Operations Supervisory Composite Rating and—in lieu of a PCA designation—SOSA ranking.[28]

Similarly, while an FBO is not required to perform a self-assessment if it requests a cap category of de minimis or wishes to be assigned a cap category of exempt-from-filing by the Reserve Bank, the Reserve Banks rely on the minimum standards set by the creditworthiness matrix when they evaluate FBO requests for *any* cap category greater than zero. Accordingly, the Reserve Banks generally do not allow FBOs to qualify for a positive net debit cap, including

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of $10 million or 20 percent of its capital measure can be assigned an "exempt-from-filing" cap category without performing a self-assessment or filing a board of directors resolution with its Administrative Reserve Bank.

[27] Under Section II.D.1 of the PSR policy, the cap multiple for the "high" category is 2.25, for the "above average" category is 1.875, for the "average" category is 1.125, for the "de minimis" category is 0.4, for the "exempt-from-filing" category is 0.2 or $10 million, and for the "zero" category is 0. Note that the net debit cap for the exempt-from-filing category is equal to the *lesser* of $10 million or 0.2 multiplied by the capital measure.

[28] Under Section 38 of the Federal Deposit Insurance Act, 12 U.S.C. 1831o, PCA designations apply only to insured depository institutions.

the de minimis or exempt-from-filing cap category, if the FBO has a SOSA ranking of 3 or a U.S. Operations Supervisory Composite Rating of marginal or unsatisfactory.[29]

In certain situations, the Reserve Banks require institutions to perform a full assessment of their creditworthiness instead of using the relevant self-assessment matrix (*e.g.*, when the institution has experienced a significant development that may materially affect its financial condition). The Guide includes procedures for full assessments of creditworthiness.

2. Capital measures

Under Section II.D.3 of the PSR policy, an institution's "capital measure" is a number derived (under most circumstances) from the size of its capital base. The determination of the capital measure, however, differs between domestic institutions and FBOs. A domestic institution's capital measure equals 100 percent of the institution's risk-based capital. Conversely, an FBO's capital measure (also called "U.S. capital equivalency")[30] equals a percentage of (under most circumstances) the FBO's worldwide capital base[31] ranging from 5 percent to 35 percent, with the exact percentage depending on (1) the FBO's SOSA ranking and (2) whether the FBO is an FHC. Specifically, the capital measure of an FBO that is an FHC is 35 percent of its capital; an FBO that is not an FHC and has a SOSA ranking of 1 is 25 percent of its capital; and an FBO that is not an FHC and has a SOSA ranking of 2 is 10 percent of its capital. The capital measure of an FBO that is not an FHC and has a SOSA ranking of 3 equals 5

[29] *See* n. 4, *supra*, and accompanying text.

[30] The term "U.S. capital equivalency" is used in this context to refer to the particular capital measure used to calculate net debit caps and does not necessarily represent an appropriate capital measure for supervisory or other purposes.

[31] FBOs that wish to establish a non-zero net debit cap must report their worldwide capital on the Annual Daylight Overdraft Capital Report for U.S. Branches and Agencies of Foreign Banks (FR 2225). The instructions for FR 2225 explain how FBOs should calculate their worldwide capital. *See* https://www.federalreserve.gov/apps/reportforms/reportdetail.aspx?sOoYJ+5BzDZ1kLYTc+ZpEQ==.

percent of its "net due to related depository institutions" (although, as noted above, FBOs with a SOSA ranking of 3 generally do not qualify for a positive net debit cap).[32]

B. Maximum Daylight Overdraft Capacity

Section II.E of the PSR policy allows certain institutions with self-assessed net debit caps to pledge collateral to their Administrative Reserve Bank to secure daylight overdraft capacity in excess of their net debit caps. An institution's maximum daylight overdraft capacity ("max cap") equals its net debit cap plus its additional collateralized capacity. The max cap policy is "intended to provide extra liquidity through the pledge of collateral by the few institutions that might otherwise be constrained from participating in risk-reducing payment system initiatives."

Institutions that wish to obtain a max cap must generally provide (1) documentation of the business need for collateralized capacity and (2) an annual board of directors' resolution approving any collateralized capacity. Under Section II.E.2 of the PSR policy, however, an FBO that has a SOSA ranking of 1 or is an FHC may request a streamlined procedure for obtaining a max cap.[33] Such an FBO is not required to document its business need for collateralized capacity, nor is it required to obtain a board of directors' resolution approving collateralized capacity, as long as the FBO requests a max cap that is 100 percent or less of the FBO's worldwide capital times its self-assessed cap multiple.[34]

II. Discussion of Proposed Changes; Request for Comment

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[32] An FBO reports its "net due to related depository institutions" on the Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks (FFIEC 002).

[33] Even under the streamlined procedure, the Administrative Reserve Bank retains the right to assess an FBO's financial and supervisory information, including the FBO's ability to manage intraday credit.

[34] As described above, for example, the capital measure of an FBO that is not an FHC and has a SOSA ranking of 1 is 25 percent of worldwide capital. The net debit cap of such an FBO equals its capital measure times the cap multiple that corresponds to its cap category. The streamlined max cap procedure therefore allows the FBO to request additional collateralized capacity of 75 percent of worldwide capital times its cap multiple. If the FBO requests a max cap in excess of 100 percent of worldwide capital times its cap multiple, the FBO would be ineligible for the streamlined max cap procedure.

The SOSA ranking was originally established to provide input to the development and maintenance of a comprehensive supervisory strategy for the U.S. activities of an FBO, but Federal Reserve supervisors no longer use SOSA rankings for this purpose.[35] As a result, the only current use of SOSA rankings by the Federal Reserve is in setting guidelines related to FBO access to Reserve Bank intraday credit and the discount window.[36] Federal Reserve supervisors currently provide SOSA rankings to many FBOs, including FBOs that have not requested positive net debit caps. The Board believes that this is an inefficient use of the Federal Reserve's supervisory resources, and that it should streamline the Federal Reserve's FBO supervision program by discontinuing the SOSA ranking. As described further below, the Board proposes to remove references to the SOSA ranking in the PSR policy. The Federal Reserve will continue to provide SOSA rankings until the Board removes such references in the PSR Policy.

Additionally, for reasons discussed below, the Board no longer believes that an FBO should receive greater daylight overdraft capacity because it is an FHC. The Board therefore proposes to remove references to FBOs' FHC status in the PSR policy.

The Board proposes to adopt alternative methods for determining an FBO's eligibility for a positive net debit cap, the size of its net debit cap, and its eligibility to request a streamlined procedure to obtain a max cap. As described more fully below:

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[35] *See* SR Letter 00-14, "Enhancements to the Interagency Program for Supervising the U.S. Operations of Foreign Banking Organizations" (Oct. 23, 2000), https://www.federalreserve.gov/boarddocs/srletters/2000/sr0014.htm (letter adopting the SOSA ranking in its current form). *See also* Section II.C.1.a, *infra*, explaining that Federal Reserve supervisory staff now have access to better supervisory information that allows supervisors to monitor FBOs on an ongoing basis.

[36] In addition to the PSR policy's use of SOSA rankings, the Reserve Banks use SOSA rankings to determine whether an FBO can receive discount window loans. *See* https://www.frbdiscountwindow.org/en/Pages/General-Information/The-Discount-Window.aspx. Eliminating SOSA rankings will require adjustments to the Reserve Banks' standards for determining FBO access to primary credit.

- Many undercapitalized FBOs, and all significantly or critically undercapitalized FBOs, would have "below standard" creditworthiness and would generally be ineligible for a positive net debit cap.
- An FBO's creditworthiness self-assessment would generally be based on the FBO's U.S. Operations Supervisory Composite Rating and the PCA designation that would apply to the FBO if it were subject to the Board's Regulation H.[37] An FBO that is not based in a country that adheres to the Basel Capital Accords ("BCA") would be required to perform a full assessment of its creditworthiness in lieu of the matrix approach to assessing creditworthiness.
- The capital measure of an FBO would equal 10 percent of its worldwide capital.
- An FBO that is well capitalized could request the streamlined procedure for obtaining a max cap.

The Board requests comment on all aspects of the proposal, including whether FBOs would require a transition period to adjust to the proposed changes.

A. Eligibility of SOSA-3 Ranked FBOs for a Positive Net Debit Cap

As discussed above, SOSA-3 ranked FBOs are presumptively ineligible for a positive net debit cap. Because the proposal would remove all references to the SOSA ranking in the PSR policy, FBOs that currently hold a SOSA-3 ranking would not be—on that basis—presumptively ineligible for a positive net debit cap. Some of those FBOs would be ineligible for positive net debit caps for other reasons, however. First, the revised creditworthiness self-assessment matrix in the Guide (discussed further below) would continue to assume that FBOs that have U.S. Operations Supervisory Composite Ratings of "marginal" or "unsatisfactory" have "below

[37] *See* 12 CFR 208.43(b).

standard" creditworthiness and are generally ineligible for a positive net debit cap.[38] Second, the revised creditworthiness self-assessment matrix would—as described further below—assume that many undercapitalized FBOs, and all significantly or critically undercapitalized FBOs, have "below standard" creditworthiness and are generally ineligible for a positive net debit cap. Finally, an Administrative Reserve Bank might decline to provide a positive net debit cap to an FBO if the Reserve Bank has supervisory concerns regarding that FBO.

B. FBO Creditworthiness

As discussed above, an institution that wishes to establish a net debit cap category of high, above average, or average must perform a self-assessment of, among other things, its own creditworthiness. The Board is proposing to revise the PSR policy to provide that, if an FBO is based in a jurisdiction that adheres to the BCA, the FBO's creditworthiness self-assessment will be based on (1) the FBO's U.S. Operations Supervisory Composite Rating and (2) the PCA designation that would apply to the FBO if it were subject to the Board's Regulation H.[39] To determine its equivalent PCA designation, the FBO would compare the Regulation H ratios for total risk-based capital, tier 1 risk-based capital, common equity tier 1 risk-based capital, and leverage to the equivalent ratios that the FBO has calculated under its home country standards or on a pro forma basis.

The Board believes that an FBO's equivalent PCA designation would serve the same purpose as the SOSA ranking in the creditworthiness self-assessment matrix. The SOSA ranking has been useful for assessing FBO creditworthiness because it provides insight into whether an FBO's home office has the ability to support its U.S. branch or agency. Similarly, an equivalent

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[38] *See* n. 4, *supra*. Based on data from third-quarter 2017, one SOSA-3 ranked FBO currently has a U.S. Operations Supervisory Composite Rating of "marginal" or "unsatisfactory," while nineteen SOSA-3 ranked FBOs currently have U.S. Operations Supervisory Composite Ratings higher than "marginal" or "unsatisfactory."

[39] *See* 12 CFR 208.43(b).

PCA designation would provide insight into an FBO's worldwide financial profile and its ability to support its U.S. branch or agency.

Replacing the SOSA ranking with an equivalent PCA designation would also align the creditworthiness self-assessment for FBOs with the existing creditworthiness self-assessment for domestic institutions.[40] The Board would implement these changes by incorporating FBO creditworthiness self-assessments into the Guide's existing matrix for assessing domestic institutions' creditworthiness.[41] The revised matrix would assume that many undercapitalized FBOs,[42] and all significantly or critically undercapitalized FBOs, have "below standard" creditworthiness and are (like SOSA-3 ranked FBOs under the current PSR policy) generally ineligible for a positive net debit cap.

The Board does not expect that the proposed changes to the creditworthiness self-assessment matrix would significantly affect FBOs' access to Reserve Bank intraday credit. If the proposed changes were to take effect, only four of the eleven FBOs that currently maintain a self-assessed cap category might qualify for a higher creditworthiness self-assessment rating and thus a higher cap category. These four entities would also need to satisfy the other criteria of the cap category self-assessment (intraday funds management and control, customer credit policies and controls, and operating controls and contingency procedures) to qualify for a higher cap

[40] Until April 2002, the Guide included a single creditworthiness self-assessment matrix for domestic institutions and FBOs, with PCA categories on one axis and supervisory composite ratings on the other axis. The Guide instructed FBOs to calculate an equivalent PCA designation using tier I and total risk-based capital ratios, but did not require FBOs to use leverage ratios. In April 2002, the Guide was revised to its present form, with a separate FBO creditworthiness matrix that lists SOSA rankings on one axis and U.S. supervisory composite ratings on the other axis.

[41] *See* Table VII-1 of the Guide.

[42] An undercapitalized FBO with a U.S. Operations Supervisory Composite Rating of "strong" or "satisfactory" would (like a similarly situated domestic institution) be permitted to perform a full assessment of its creditworthiness to determine its eligibility for a positive net debit cap.

category.[43] Similarly, if the proposed changes were to take effect, the Board estimates that only one of the eleven FBOs that currently maintain a self-assessed cap category could potentially lose its self-assessed cap and/or be required to complete a full creditworthiness self-assessment.

The Board does not believe that it will be burdensome for FBOs to calculate an equivalent PCA designation. The Board's FR Y-7Q report currently requires that FBOs with total consolidated assets of $50 billion or more report the numerators and denominators of all four ratios in the PCA determination. The FR Y-7Q report also requires that FBOs with total consolidated assets below $50 billion report the numerators and denominators of all ratios in the PCA determination except the common equity tier 1 capital ratio. FBOs with total consolidated assets below $50 billion that are based in BCA-adhering jurisdictions already calculate their common equity tier 1 capital ratios under home country standards.

As discussed above, while an FBO is not required to perform a self-assessment if it requests a cap category of de minimis or wishes to be assigned a cap category of exempt-from-filing by the Reserve Bank, the Reserve Banks currently rely on the minimum standards set by the creditworthiness matrix when they evaluate an FBO's eligibility for *any* positive net debit cap, including the de minimis and exempt-from-filing cap categories. The Board proposes that the Reserve Banks will rely on the minimum standards of the revised creditworthiness matrix when they evaluate whether FBOs from BCA-adhering jurisdictions are eligible for a positive net debit cap, including a de minimis or exempt-from-filing cap category. Under the revised creditworthiness matrix, the Reserve Banks generally would not allow significantly or critically undercapitalized FBOs, many undercapitalized FBOs, and FBOs with a U.S. Operations Supervisory Composite Rating of marginal or unsatisfactory to qualify for a positive net debit

[43] *See* Table VII-3 of the Guide.

cap, including a de minimis or exempt-from-filing cap category. The Reserve Banks would use publicly available data to determine the equivalent PCA designation of FBOs that request a cap category of de minimis or wish to be assigned a cap category of exempt-from-filing.

The Board is also proposing to revise the PSR policy to provide that, if an FBO is *not* based in a country that adheres to the BCA, the FBO must perform a full assessment of its creditworthiness in lieu of the matrix approach to assessing creditworthiness. As noted above, the Guide includes procedures for full assessments of creditworthiness. The requirement to perform a full assessment of creditworthiness would apply to FBOs from non-BCA jurisdictions that request *any* net debit cap greater than the exempt-from-filing category, including FBOs that request a de minimis cap category. Additionally, Reserve Banks may request that FBOs from non-BCA jurisdictions perform a full assessment of creditworthiness before assigning the FBO an exempt-from-filing cap category.

C. FBO Capital Measure

As discussed above, under the PSR policy, the determination of an FBO's capital measure is based on the FBO's capital base, SOSA ranking, and FHC status. The Board is proposing to (1) eliminate references to SOSA rankings and FHC status in calculating an FBO's capital measure and (2) replace the existing four-tier structure for calculating an FBO's capital measure with a simplified fixed-rate calculation that depends solely on the FBO's capital base. Specifically, the proposed change would provide that the capital measure of an FBO equals 10 percent of its worldwide capital.

For the reasons described below, the Board believes that it is unnecessary to replace the SOSA ranking with an alternative supervisory rating for purposes of calculating an FBO's capital measure. The Board also believes that an FBO's status as an FHC should not allow the

FBO to qualify for a higher capital measure. While the proposed fixed-rate FBO capital measure calculation would reduce net debit caps for many FBOs, the Board believes that the adjusted FBO net debit caps would be better tailored to FBOs' actual usage of intraday credit and generally would not constrain FBOs' U.S. operations. Finally, while FBOs operating in the United States should be, generally, treated no less favorably than similarly-situated U.S. banking organizations, the Board continues to believe that it is reasonable to calculate an FBO's capital measure as a fraction of its worldwide capital, notwithstanding that the capital measure of a domestic institution generally equals 100 percent of the institution's risk-based capital.

1. It is unnecessary to replace the SOSA ranking with an alternative supervisory rating for purposes of calculating an FBO's capital measure.

    a. The Board and the Reserve Banks now have better supervisory information regarding FBOs**.**

Before the Board adopted the current capital measure calculation process in 2002, an FBO's capital measure depended solely on whether the FBO was based in a country that adhered to the BCA.[44] The Board adopted the current capital measure calculation in 2002 because it believed that SOSA rankings offered a superior basis for calculating an FBO's capital measure compared to home-country BCA status, explaining that "SOSA rankings provide[d] broader information about the condition of the FBO, its supervision, and the home country, whereas the BCA distinction provide[d] information only about the home country treatment of bank capital adequacy."[45] The Board also noted that "the BCA designation reflect[ed] the one-time adoption

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[44] FBOs from countries that adhered to the BCA were eligible to use as their capital measure the greater of 10 percent of their capital or 5 percent of their liabilities to nonrelated parties. FBOs from countries that did not adhere to the BCA were eligible to use as their capital measure the greater of 5 percent of their liabilities to nonrelated parties or the amount of capital that would be required of a national bank being organized at each location.
[45] 66 FR 64419, 64424 (Dec. 13, 2001).

of BCA standards by a country's supervisory authority, while U.S. bank supervisors update[d] the SOSA rankings regularly."[46]

Since the Board adopted the current FBO capital measure calculation in February 2002, Federal Reserve staff have gained access to new internal and external resources that allow the Federal Reserve to better monitor FBOs on an ongoing basis.[47] These new resources offer Federal Reserve staff additional information regarding the financial and managerial conditions of FBOs' U.S. and global operations. These resources also provide information regarding home-country accounting practices, financial systems, as well as international supervisory and regulatory developments. Additionally, Federal Reserve staff now enjoy better ongoing communication with many FBOs' home country supervisors.[48] Collectively, this improved information allows Administrative Reserve Banks to make better decisions, on an ongoing basis, regarding FBO's level of access to intraday credit. The Board therefore believes that it is unnecessary to include a point-in-time supervisory rating when determining an FBO's capital measure.

b. Other elements of the net debit cap calculation consider an FBO's overall financial condition.

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[46] *Id*.

[47] For example, the Board began requiring in December 2002 and March 2014 that a top-tier FBO file capital and asset information quarterly (rather than annually) if the FBO is (respectively) an FHC or has total consolidated assets of $50 billion or more. *See* FR Y-7Q (Capital and Asset Report for Foreign Banking Organizations); 67 FR 72953 (Dec. 9, 2002) and 79 FR 9900 (Feb. 21, 2014). Additionally, improved commercial databases now offer Federal Reserve supervisors more detailed and timely information regarding FBOs and their home countries.

[48] For example, Federal Reserve supervisors participate in "supervisory colleges," which are "multilateral working groups of relevant supervisors that are formed to promote effective, ongoing consolidated supervision of the overall operations of an international banking group." These supervisory colleges "enhance[] the Federal Reserve's communication and collaboration with foreign supervisors and supplement[] bilateral working relationships with foreign supervisors." *Federal Reserve System Purposes & Functions*, 94-96. https://www.federalreserve.gov/aboutthefed/files/pf_complete.pdf.

As discussed above, an FBO's net debit cap is determined by its capital measure and cap category. Under the Board's proposed changes to the FBO creditworthiness self-assessment procedures (described above), an FBO's worldwide capital ratios would affect its creditworthiness (and thus its cap category). Additionally, the FBO creditworthiness self-assessment procedures would continue to consider FBOs' U.S. Operations Supervisory Composite ratings. Given that other elements of the net debit cap calculation already consider an FBO's supervisory ratings (and will consider an FBO's overall financial condition if the proposed changes take effect), the Board believes that it is unnecessary to replace the SOSA ranking with an alternative supervisory rating in the FBO capital measure calculation.

2. An FBO should not qualify for a higher capital measure because it is an FHC.

When the Board adopted the current FBO capital measure calculation in 2002, it believed that an FBO's status as an FHC indicated that the FBO was financially and managerially strong, and that the FBO should accordingly qualify for a higher capital measure than a non-FHC FBO. Since 2002, however, the Board has recognized the limitations of FHC status in measuring an FBO's health. In particular, FBOs can maintain nominal FHC status (though with reduced ability to use their FHC powers) even when they are out of compliance with the requirement that they remain well capitalized. Accordingly, the Board no longer believes that an FBO should qualify for a higher capital measure because it is an FHC.

3. The adjusted FBO net debit caps would be better tailored to FBOs' actual usage of intraday credit and generally would not constrain FBOs' U.S. operations.

While the Board's proposed fixed-rate capital measure calculation would reduce net debit caps for twenty of the 49 FBOs that currently maintain a positive net debit cap,[49] the Board believes that the adjusted FBO net debit caps would be better tailored to FBOs' actual usage of intraday credit: since 2015, only 25 of 62 FBOs with a positive net debit cap have used any daylight overdraft capacity, the highest average cap utilization by an FBO was 28.5 percent, and only two FBOs had an average cap utilization greater than 25 percent.[50] Even during the 2007–09 financial crisis, when the use of intraday credit spiked amid the market turmoil near the end of 2008, 51 of 58 FBOs with a positive net debit cap used capacity, the highest average cap utilization was 65 percent, and only seven FBOs had an average cap utilization greater than 25 percent.

The Board recognizes that daylight overdrafts may currently occur less frequently because many institutions hold excess reserves and thus have higher opening balances in their Federal Reserve accounts. The Board believes, however, that FBOs' adjusted net debit caps would not constrain most FBOs' U.S. operations even if FBOs hold lower reserves in the future. The Board has reached this conclusion by comparing FBOs' projected net debit caps under the proposed fixed-rate capital measure calculation to FBOs' actual daylight overdrafts between

[49] Aggregate FBO net debit caps would be reduced by 57%, seventeen FBOs would have their net debit caps reduced by 71%, and three FBOs would have their net debit caps reduced by 60%.

[50] In this context, average cap utilization equals an institution's average daily peak daylight overdraft divided by the FBO's net debit cap.

2003 and 2007, when FBOs generally maintained lower reserves.[51] The Board's comparison indicates that, between 2003 and 2007, only four of the 29 FBOs that currently maintain a cap category higher than exempt-from-filing regularly incurred daylight overdrafts that exceeded their projected net debit caps, while five of the 29 FBOs incurred daylight overdrafts that exceeded their projected net debit caps in limited instances. Twenty of the 29 FBOs never incurred daylight overdrafts that exceeded their projected net debit caps.

The Board also notes that FBO net debit caps are large when compared to the net debit caps of peer domestic institutions. For example, the average net debit cap of an FBO with between $10 billion and $50 billion in U.S.-based assets is $2.6 billion, while the average net debit cap of a domestic institution with between $10 billion and $50 billion in assets is $1.4 billion; similarly, the average net debit cap of an FBO with between $50 billion and $150 billion in U.S.-based assets is $28.2 billion, while the average net debit cap of a domestic institution with between $50 billion and $150 billion in assets is $10.5 billion.[52] FBOs currently hold seven of the twenty largest net debit caps, but only three FBOs hold U.S. assets that rank among the twenty largest institutions by asset size.

The Board recognizes that its proposed changes to the capital measure calculation may increase the instances in which FBOs need additional daylight overdraft capacity. An FBO with a de minimis cap could request a higher net debit cap by applying for a self-assessed cap.[53]

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[51] For this purpose, the Board projected FBOs' net debit caps using an FBO's worldwide capital at the time of past overdrafts, multiplied by the proposed 10 percent FBO capital measure multiplier, multiplied by the relevant cap multiple that corresponds to the FBO's cap category.

[52] The Board excluded institutions with a cap category of exempt-from-filing from these comparisons because these institutions are limited to a $10 million net debit cap. No FBO has U.S.-based assets above $150 billion.

[53] Most FBOs with a cap category of exempt-from-filing receive the maximum net debit cap of $10 million and would not be affected by the proposed changes to the FBO capital measure calculation.

Similarly, an FBO with a self-assessed cap could apply for a max cap in order to obtain additional collateralized capacity.

4. National treatment considerations

Under the principle of national treatment, FBOs operating in the United States should be, generally, treated no less favorably than similarly-situated U.S. banking organizations.[54] When FBOs incur daylight overdrafts, however, they present special legal risks to the Federal Reserve because of differences in insolvency laws in the various FBOs' home countries. As the Board explained in 2001,

> In international financial transactions, the overall risk borne by each party is affected not only by the governing law set out in the contract, but also by the law governing the possible insolvency of its counterparty. The insolvency of an international bank presents significant legal issues in enforcing particular provisions of a financial contract (such as close-out netting or irrevocability provisions) against third parties (such as the liquidator or supervisor of the failed bank). The insolvent party's national law also may permit the liquidator to subordinate other parties' claims (such as by permitting the home country tax authorities to have first priority in bankruptcy), may reclassify or impose a stay on the right the nondefaulting party has to collateral pledged by the defaulting party in support of a particular transaction, or may require a separate proceeding to be initiated against the head office in addition to any proceeding against the branch.
>
> It is not practicable for the Federal Reserve to undertake and keep current extensive analysis of the legal risks presented by the insolvency law(s) applicable to each FBO with a Federal Reserve account in order to quantify precisely the legal risk that the Federal Reserve incurs by providing intraday credit to that

[54] *See, e.g.*, International Banking Act of 1978, Public Law 95-369, 12 U.S.C. 3101 *et seq;* S. Rep. No. 95-1073 (Aug. 8, 1978) (legislative history of the International Banking Act of 1978); Gramm-Leach-Bliley Act of 1999, Public Law 106-102, section 141, 12 U.S.C. 3106(c); Dodd-Frank Act, Public Law 111-203, section 165(b)(2), 12 U.S.C. 5365(b)(2).

> institution. It is reasonable, however, for the Federal Reserve to recognize that FBOs generally present additional legal risks to the payments system and, accordingly, limit its exposure to these institutions.[55]

The Board continues to believe that FBOs present legal risks to the Federal Reserve that are above and beyond the risks posed by domestic institutions when FBOs incur daylight overdrafts. Accordingly, the Board continues to believe that it is reasonable to calculate an FBO's capital measure as a fraction of its worldwide capital, notwithstanding that the capital measure of a domestic institution generally equals 100 percent of the institution's risk-based capital. Nevertheless, as discussed above, the proposed fixed-rate capital measure calculation would allow FBOs to obtain net debit caps that would be well tailored to FBOs' actual usage of intraday credit and generally would not constrain FBOs' U.S. operations.

D. FBO Requests for Additional Collateralized Credit under the Max Cap Policy

As discussed above, an FBO that has a SOSA-1 ranking or is an FHC may request a streamlined procedure for obtaining a max cap. The Board is proposing to remove the SOSA-1 ranking and FHC status as factors in determining whether FBOs can request the streamlined procedure. The Board instead proposes to allow FBOs that are well capitalized to request the streamlined procedure for obtaining a max cap.[56]

The Board believes that allowing well-capitalized FBOs to request the streamlined max cap procedure would serve a similar purpose as allowing SOSA-1 ranked FBOs and FBOs with FHC status to request the streamlined procedure. The Board originally allowed SOSA-1 ranked

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[55] 66 FR 30205, 30206 (Aug. 6, 2001).

[56] For these purposes, an FBO would determine whether it is well capitalized using the same methodology by which it would determine its equivalent PCA designation for the creditworthiness self-assessment matrix, *i.e.*, the FBO would compare the Regulation H ratios for total risk-based capital, tier 1 risk-based capital, common equity tier 1 risk-based capital, and leverage to the equivalent ratios that the FBO has calculated under its home country standards or on a pro forma basis.

FBOs and FBOs with FHC status to request the streamlined max cap procedure because the Board believed that such FBOs raised fewer supervisory concerns.[57] As noted above, however, the Board now believes that (1) creating the SOSA ranking is an inefficient use of Federal Reserve resources and (2) FHC status does not necessarily indicate that FBO status provides a strong indication of financial health, since an FBO can retain nominal FHC status when it is not well capitalized. The Board believes instead that well-capitalized FBOs should be able to request the streamlined max cap procedure, because well-capitalized FBOs are (generally) better positioned than other FBOs to support their U.S. branches and agencies. The Board does not believe that it would be appropriate to substitute another supervisory rating for the SOSA-1 ranking in determining FBO eligibility for the streamlined max cap procedure, because non-SOSA supervisory ratings focus only on the U.S. operations of FBOs.

The streamlined max cap procedure would provide well-capitalized FBOs with a straightforward process for obtaining collateralized intraday overdraft capacity, which could offset the reduction to FBO net debit caps that would result from the proposed changes to the FBO capital measure calculation. Any FBO that is not well capitalized and wishes to establish a max cap could continue to use the general procedure for requesting a max cap.

III. Regulatory Flexibility Act

Congress enacted the Regulatory Flexibility Act ("RFA") (5 U.S.C. 601 *et seq.*) to address concerns related to the effects of agency rules on small entities, and the Board is sensitive to the impact its rules may impose on small entities. The RFA requires agencies either to provide an initial regulatory flexibility analysis with a proposed rule or to certify that the proposed rule will not have a significant economic impact on a substantial number of small

[57] 73 FR 12417, 12430 (Mar. 7, 2008).

entities. In this case, the relevant provisions of the PSR policy apply to all FBOs that maintain accounts at Federal Reserve Banks. While the Board does not believe that the proposed changes would have a significant impact on small entities, and regardless of whether the RFA applies to the PSR Policy per se, the Board has nevertheless prepared the following Initial Regulatory Flexibility analysis in accordance with 5 U.S.C. 603. The Board requests public comments on all aspects of this analysis.

1. *Statement of the need for, objectives of, and legal basis for, the proposed rule.* Section 11(j) of the Federal Reserve Act[58] authorizes the Board to oversee the Reserve Banks' provision of intraday credit to Reserve Bank account holders.

As discussed above, the Board is issuing this proposal to remove references to the SOSA ranking and FBOs' FHC status in the PSR policy. Discontinuing the SOSA ranking would streamline the Federal Reserve's FBO supervision program by eliminating the need for Federal Reserve supervisors to provide supervisory rankings that only serve a purpose for Reserve Bank credit decisions for many FBOs—including FBOs that have not requested positive net debit caps. Removing references to FHC status in the PSR policy would align the policy with the Board's view that an FBO's status as an FHC is not a suitable factor for determining the FBO's eligibility for intraday credit.

2. *Small entities affected by the proposed rule.* Pursuant to regulations issued by the Small Business Administration ("SBA") (13 CFR 121.201), a "small entity" includes an entity that engages in commercial banking and has assets of $550 million or less (NAICS code 522110). Thirty-nine FBOs that maintain Federal Reserve accounts are small entities. Six of those FBOs maintain positive net debit caps.

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[58] 12 U.S.C. 248(j).

3. *Projected reporting, recordkeeping, and other compliance requirements.* The proposed changes would alter the procedures by which FBOs obtain intraday credit from the Reserve Banks. The most important new requirement is that an FBO would need to determine an equivalent PCA designation, based on its worldwide capital ratios, to establish its creditworthiness under the PSR policy. Additionally, an FBO would need to determine that it is well capitalized, based on worldwide capital ratios, in order to qualify for a streamlined procedure for requesting collateralized intraday credit.

As noted above, the Board does not believe that it will be burdensome for an FBO to calculate an equivalent PCA designation or determine whether it is well capitalized. The Board's FR Y-7Q report currently requires that FBOs with total consolidated assets of $50 billion or more report the numerators and denominators of all four ratios in the PCA determination. The FR Y-7Q report also requires that FBOs with total consolidated assets below $50 billion report the numerators and denominators of all ratios in the PCA determination except the common equity tier 1 capital ratio. FBOs with total consolidated assets below $50 billion that are based in BCA-adhering jurisdictions already calculate their common equity tier 1 capital ratios under home country standards.

4. *Identification of duplicative, overlapping, or conflicting Federal rules.* The Board has not identified any Federal rules that duplicate, overlap with, or conflict with the proposed changes to the PSR policy.

5. *Significant alternatives.* The Board does not believe that alternatives to the proposed changes would better accomplish the objectives of limiting credit risk to the Reserve Banks while minimizing any economic impact on small entities. While one alternative would be to continue providing SOSA rankings to FBOs and leave the PSR policy in its present form, the

Board believes that Federal Reserve supervisory resources should be allocated to other matters. Similarly, the Board could continue to allow FBOs that are FHCs to qualify for higher levels of intraday credit than FBOs that are not FHCs, but (as described above) the Board does not believe that an FBO's status as an FHC should determine the FBO's eligibility for intraday credit.

In two places—specifically, in the capital measure calculation process and in the eligibility criteria for a streamlined max cap procedure—the proposed changes would delete references to SOSA without replacing those references with an alternative supervisory rating. For the reasons described above, the Board believes that it is unnecessary to substitute another supervisory rating.

Finally, the proposed changes would replace SOSA rankings in the creditworthiness self-assessment matrix with an equivalent PCA designation. This change would require an FBO to calculate its equivalent PCA designation using worldwide capital ratios. Alternatively, the Board could simply delete the SOSA ranking and judge an FBO's creditworthiness solely on the basis of its U.S. operations supervisory composite rating. The Board believes, however, that using equivalent PCA designations in conjunction with supervisory ratings will better protect the Reserve Banks from credit risk, because an equivalent PCA designation would provide insight into an FBO's worldwide financial profile and its ability to support its U.S. branches and agencies.

IV. Competitive Impact Analysis

The Board conducts a competitive impact analysis when it considers a rule or policy change that may have a substantial effect on payment system participants. Specifically, the Board determines whether there would be a direct or material adverse effect on the ability of other service providers to compete with the Federal Reserve due to differing legal powers or due to the Federal Reserve's dominant market position deriving from such legal differences.[59]

The Board believes that the proposed modifications to the PSR policy will have no adverse effect on the ability of other service providers to compete with the Reserve Banks in providing similar services. While the Board expects that the proposed modifications would reduce net debit caps for many FBOs, the Board does not believe this will have a significant effect on FBOs because (as explained above) the adjusted FBO net debit caps would still provide ample levels of intraday credit. The Board therefore believes that most FBOs would retain sufficient access to Reserve Bank intraday credit if the proposed modifications take effect, and accordingly does not expect the proposed modifications would have a significant effect on FBOs' use of Federal Reserve Bank services. Additionally, the proposed modifications will have no effect on intraday credit access for domestic institutions, which comprise the vast majority of Reserve Bank account holders.

V. Paperwork Reduction Act

In accordance with section 3512 of the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3521) ("PRA"), the Board may not conduct or sponsor, and a respondent is not required to respond to, an information collection unless it displays a currently valid Office of Management and Budget ("OMB") control number. The OMB control number is 7100-0217. The Board reviewed the PSR policy changes it is considering under the authority delegated to the Board by the OMB.

Comments are invited on:

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[59] Federal Reserve Regulatory Service, 9-1558.

(a) Whether the collections of information are necessary for the proper performance of the agencies' functions, including whether the information has practical utility;

(b) The accuracy of the estimates of the burden of the information collections, including the validity of the methodology and assumptions used;

(c) Ways to enhance the quality, utility, and clarity of the information to be collected;

(d) Ways to minimize the burden of the information collections on respondents, including through the use of automated collection techniques or other forms of information technology; and

(e) Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

All comments will become a matter of public record. Comments on aspects of this notice that may affect reporting, recordkeeping, or disclosure requirements and burden estimates should be sent to the addresses listed in the **ADDRESSES** section of this document. A copy of the comments may also be submitted to the OMB desk officer: by mail to U.S. Office of Management and Budget, 725 17th Street NW., # 10235, Washington, DC 20503; by facsimile to (202) 395–5806; or by email to: *oira_submission@omb.eop.gov*, Attention, Federal Banking Agency Desk Officer.

Proposed Revisions, With Extension for Three Years, of the Following Information Collection: (1)

Title of Information Collection: Annual Report of Net Debit Cap.

Agency Form Number: FR 2226.

OMB Control Number: 7100-0217

Frequency of Response: Annually.

Respondents: Depository institutions' board of directors.

Abstract: Federal Reserve Banks collect these data annually to provide information that is essential for their administration of the PSR policy. The reporting panel includes all financially healthy depository institutions with access to the discount window. The Report of Net Debit Cap comprises three resolutions, which are filed by a depository institution's board of directors depending on its needs. The first resolution is used to establish a de minimis net debit cap and the second resolution is used to establish a self-assessed net debit cap.[60] The third resolution is used to establish simultaneously a self-assessed net debit cap and maximum daylight overdraft capacity.

Current Actions: Under the PSR policy, an FBO's SOSA ranking can affect its eligibility for a positive net debit cap, the size of its net debit cap, and its eligibility to request a streamlined procedure to obtain maximum daylight overdraft capacity. Additionally, an FBO's status as an FHC can affect the size of its net debit cap and its eligibility to request a streamlined procedure to obtain maximum daylight overdraft capacity. The proposed changes to the PSR policy would (1) remove references to the SOSA ranking, (2) remove references to FBOs' FHC status, and (3) adopt alternative methods for determining an FBO's eligibility for a positive net debit cap, the size of its net debit cap, and its eligibility to request a streamlined procedure to obtain maximum daylight overdraft capacity. The proposed revisions would increase the estimated average hours per response for FR 2226 self-assessment and de minimis respondents that are FBOs by half an hour.

[60] Institutions use these two resolutions to establish a capacity for daylight overdrafts above the lesser of $10 million or 20 percent of the institution's capital measure. Financially healthy U.S. chartered institutions that rarely incur daylight overdrafts in excess of the lesser of $10 million or 20 percent of the institution's capital measure do not need to file board of directors' resolutions or self-assessments with their Reserve Bank.

Estimated number of respondents: De Minimis Cap: Non-FBOs, 915 respondents and FBOs, 18 respondents; Self-Assessment Cap: Non-FBOs, 110 respondents and FBOs, 11 respondents; and Maximum Daylight Overdraft Capacity, 4 respondents.

Estimated average hours per response: De Minimis Cap – Non-FBOs, 1 hour and FBOs, 1.5 hour; Self-Assessment Cap – Non-FBOs, 1 hour and FBOs, 1.5 hours, and Maximum Daylight Overdraft Capacity, 1 hour.

Estimated annual burden hours: De Minimis Cap: Non-FBOs, 915 hours and FBOs, 27 hours; Self-Assessment Cap: Non-FBOs, 110 hours and FBOs, 16.5 hours; and Maximum Daylight Overdraft Capacity, 4 hours.

VI. Federal Reserve Policy on Payment System Risk

Revisions to Section II.D of the PSR Policy

The Board proposes to revise Section II.D of the "Federal Reserve Policy on Payment System Risk" as follows:

D. Net debit caps

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2. Cap categories

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a. Self-assessed

In order to establish a net debit cap category of high, above average, or average, an institution must perform a self-assessment of its own creditworthiness, intraday funds management and control, customer credit policies and controls, and operating controls and contingency procedures.[61] For domestic institutions, the assessment of creditworthiness is based on the institution's supervisory rating and Prompt Corrective Action (PCA) designation.[62] For U.S. branches and agencies of FBOs that are based in jurisdictions that adhere to the Basel Capital Accord, the assessment of creditworthiness is based on the institution's supervisory rating and the PCA designation that would apply to the FBO if it were subject to the Board's Regulation H.[63] An institution may perform a full assessment of its creditworthiness in certain limited circumstances—for example, if its condition has changed significantly since its last examination or if it possesses additional substantive information regarding its financial condition. Additionally, U.S. branches and agencies of FBOs based in jurisdictions that do not adhere to the Basel Capital Accord are required to perform a full assessment of creditworthiness to determine their ratings for the creditworthiness component. An institution performing a self-assessment must also evaluate its intraday funds-management procedures and its procedures for evaluating the financial condition

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[61] This assessment should be done on an individual-institution basis, treating as separate entities each commercial bank, each Edge corporation (and its branches), each thrift institution, and so on. An exception is made in the case of U.S. branches and agencies of FBOs. Because these entities have no existence separate from the FBO, all the U.S. offices of FBOs (excluding U.S.-chartered bank subsidiaries and U.S.-chartered Edge subsidiaries) should be treated as a consolidated family relying on the FBO's capital.

[62] An insured depository institution is (1) "well capitalized" if it significantly exceeds the required minimum level for each relevant capital measure, (2) "adequately capitalized" if it meets the required minimum level for each relevant capital measure, (3) "undercapitalized" if it fails to meet the required minimum level for any relevant capital measure, (4) "significantly undercapitalized" if it is significantly below the required minimum level for any relevant capital measure, or (5) "critically undercapitalized" if it fails to meet any leverage limit (the ratio of tangible equity to total assets) specified by the appropriate federal banking agency, in consultation with the FDIC, or any other relevant capital measure established by the agency to determine when an institution is critically undercapitalized (12 U.S.C. 1831o).

[63] *See* 12 CFR 208.43(b).

of and establishing intraday credit limits for its customers. Finally, the institution must evaluate its operating controls and contingency procedures to determine if they are sufficient to prevent losses due to fraud or system failures. The Guide includes a detailed explanation of the self-assessment process. * * *

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b. De minimis

Many institutions incur relatively small overdrafts and thus pose little risk to the Federal Reserve. To ease the burden on these small overdrafters of engaging in the self-assessment process and to ease the burden on the Federal Reserve of administering caps, the Board allows institutions that meet reasonable safety and soundness standards to incur de minimis amounts of daylight overdrafts without performing a self-assessment.[67] An institution may incur daylight overdrafts of up to 40 percent of its capital measure if the institution submits a board of directors resolution. * * *

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c. Exempt-from-filing

Institutions that only rarely incur daylight overdrafts in their Federal Reserve accounts that exceed the lesser of $10 million or 20 percent of their capital measure are excused from performing self-assessments and filing board of

[67] U.S. branches and agencies of FBOs that are based in jurisdictions that do not adhere to the Basel Capital Accord are required to perform a full assessment of creditworthiness to determine whether they meet reasonable safety and soundness standards. These FBOs must submit an assessment of creditworthiness with their board of directors resolution requesting a de minimis cap category. U.S. branches and agencies of FBOs that are based in jurisdictions that adhere to the Basel Capital Accord are not required to complete an assessment of creditworthiness, but Reserve Banks will assess such an FBO's creditworthiness based on the FBO's supervisory rating and the PCA designation that would apply to the FBO if it were subject to the Board's Regulation H.

directors resolutions with their Reserve Banks.[68] This dual test of dollar amount and percent of capital measure is designed to limit the filing exemption to institutions that create only low-dollar risks to the Reserve Banks and that incur small overdrafts relative to their capital measure. * * *

[68] The Reserve Bank may require U.S. branches and agencies of FBOs that are based in jurisdictions that do not adhere to the Basel Capital Accord to perform a full assessment of creditworthiness to determine whether the FBO meets reasonable safety and soundness standards. U.S. branches and agencies of FBOs that are based in jurisdictions that adhere to the Basel Capital Accord will not be required to complete an assessment of creditworthiness, but Reserve Banks will assess such an FBO's creditworthiness based on the FBO's supervisory rating and the PCA designation that would apply to the FBO if it were subject to the Board's Regulation H.

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3. *Capital measure*

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b. U.S. Branches and Agencies for Foreign Banks

For U.S. branches and agencies of foreign banks, net debit caps on daylight overdrafts in Federal Reserve accounts are calculated by applying the cap multiples for each cap category to the FBO's U.S. capital equivalency measure.[69] U.S. capital equivalency is equal to 10 percent of worldwide capital for FBOs.[70]

An FBO that is well capitalized (calculated as if the FBO were subject to the Board's Regulation H[71]) may be eligible for a streamlined procedure (see section II.E.) for obtaining additional collateralized intraday credit under the maximum daylight overdraft capacity provision.

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Revisions to Section II.E of the PSR Policy

The Board proposes to revise Section II.E of the "Federal Reserve Policy on Payment System Risk" as follows:

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[69] The term "U.S. capital equivalency" is used in this context to refer the particular measure calculate net debit caps and does not necessarily represent an appropriate for supervisory or other purposes.
[70] FBOs that wish to establish a non-zero net debit cap must report their worldwide capital on the Annual Daylight Overdraft Capital Report for U.S. Branches and Agencies of Foreign Banks (FR 2225). The instructions for FR explain how FBOs should calculate their worldwide capital. *See* https://www.federalreserve.gov/apps/reportforms/reportdetail.aspx?sOoYJ+5BzDZ1kLYTc+ZpEQ==.
[71] *See* 12 CFR 208.43(b).

E. Maximum daylight overdraft capacity

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1. General procedure

An institution with a self-assessed net debit cap that wishes to expand its daylight overdraft capacity by pledging collateral should consult with its administrative Reserve Bank. The Reserve Bank will work with an institution that requests additional daylight overdraft capacity to determine the appropriate maximum daylight overdraft capacity level. In considering the institution's request, the Reserve Bank will evaluate the institution's rationale for requesting additional daylight overdraft capacity as well as its financial and supervisory information. The financial and supervisory information considered may include, but is not limited to, capital and liquidity ratios, the composition of balance sheet assets, and CAMELS or other supervisory ratings and assessments. An institution approved for a maximum daylight overdraft capacity level must submit at least once in each twelve-month period a board of directors resolution indicating its board's approval of that level. * * *

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2. Streamlined procedure for certain FBOs

An FBO that is well capitalized (calculated as if the FBO were subject to the Board's Regulation H[75]) and has a self-assessed net debit cap may request from its Reserve Bank a streamlined procedure to obtain a maximum daylight overdraft

[75] *See* 12 CFR 208.43(b).

capacity. These FBOs are not required to provide documentation of the business need or obtain the board of directors' resolution for collateralized capacity in an amount that exceeds its current net debit cap (which is based on 10 percent worldwide capital times its cap multiple), as long as the requested total capacity is 100 percent or less of worldwide capital times a self-assessed cap multiple.[76] In order to ensure that intraday liquidity risk is managed appropriately and that the FBO will be able to repay daylight overdrafts, eligible FBOs under the streamlined procedure will be subject to initial and periodic reviews of liquidity plans that are analogous to the liquidity reviews undergone by U.S. institutions.[77] If an eligible FBO requests capacity in excess of 100 percent of worldwide capital times the self-assessed cap multiple, it would be subject to the general procedure.

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By order of the Board of Governors of the Federal Reserve System, December 8, 2017.

Ann E. Misback
Secretary of the Board

BILLING CODE: 6210-01P

[76] For example, an FBO that is well capitalized is eligible for uncollateralized capacity of 10 percent of worldwide capital times the cap multiple. The streamlined max cap procedure would provide such an institution with additional collateralized capacity of 90 percent of worldwide capital times the cap multiple. As noted above, FBOs report their worldwide capital on the Annual Daylight Overdraft Capital Report for U.S. Branches and Agencies of Foreign Banks (FR 2225).

[77] The liquidity reviews will be conducted by the administrative Reserve Bank, in consultation with each FBO's home country supervisor.

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