

PUBLICATION

Federal Regulators Set to Name Firms as "Systemically Important"

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On June 3, several media outlets reported that the Financial Stability Oversight Council (FSOC) voted to provide notice to certain nonbank financial firms that they would be deemed "systemically important." The Dodd-Frank Act requires the FSOC to designate certain nonbank financial firms as systemically important and subject them to the regulatory scrutiny of the Federal Reserve Board. After the closed-door meeting, American International Group (AIG), Prudential Financial and GE Capital announced that they had been named the first systemically significant nonbank financial institutions.

Section 113 of the Dodd-Frank Act authorizes the FSOC to identify large nonbank financial companies that pose a systemic risk to the global and U.S. financial system. In mid-2012, the FSOC issued a final rule describing the policies that will guide it as it determines which companies will be covered by this new regulatory oversight. Each systemically important financial firm will be reviewed each year to reevaluate whether it continues to meet the requirements of a systemically important nonbank financial company.

The Dodd-Frank Act defines a "nonbank financial company" as a domestic or foreign company that is "predominantly engaged in financial activities," other than bank holding companies and certain other types of firms.

According to supplemental rule releases, the FSOC intends to use a three-part review of nonbank financial companies to determine which ones are systemically significant and therefore subject to additional regulatory scrutiny.

The FSOC's determination on whether a nonbank financial company will be deemed systemically significant is decided by vote of the board. A two-thirds vote by the various regulators which collectively make up the FSOC is required in order to subject a nonbank financial company to regulation by the Federal Reserve System.

Being designated a systemically important firm will subject an institution to additional regulatory oversight and require it to hold more capital as its potential failure is seen as posing significant risk to the wider financial system.

While AIG, Prudential and GE were widely expected to be among the first to be named systemically significant nonbank financial institutions, it remains to be seen just how many more entities the FSOC will designate. We will continue to monitor the FSOC's actions as it begins this new chapter in U.S. financial regulation.

If you have any questions about how this announcement could affect your company, please contact one of the attorneys in Baker Donelson's Securities Practice Group.