



BILLING CODE: 8070-01-P

FEDERAL HOUSING FINANCE AGENCY

12 CFR Part 1238

RIN 2590-AB05

Proposed Amendments to the Stress Test Rule

AGENCY: Federal Housing Finance Agency.

ACTION: Notice of proposed rulemaking with request for comment.

SUMMARY: The Federal Housing Finance Agency (FHFA) is requesting comment on a proposed rule that would amend its stress testing rule, consistent with section 401 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA).

Specifically, the proposed rule would revise the minimum threshold for the regulated entities to conduct stress tests from \$10 billion to \$250 billion, remove the requirements for Federal Home Loan Banks (Banks) subject to stress testing, and remove the adverse scenario from the list of required scenarios. These amendments align FHFA's rule with rules adopted by other financial institution regulators that implement the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) stress testing requirements, as amended by EGRRCPA. The proposed rule also makes certain conforming and technical changes.

DATES: Comments on the proposed amendments must be received on or before

[INSERT DATE 30 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit your comments, identified by regulatory identification number (RIN) 2590-AB05, by any of the following methods:

- Agency website: www.fhfa.gov/open-for-comment-or-input.
- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments. If you submit your comment to the Federal eRulemaking Portal, please also send it by e-mail to FHFA at RegComments@fhfa.gov to ensure timely receipt by the agency. Please include “RIN 2590-AB05” in the subject line of the message.
- Hand Delivered/Courier: The hand delivery address is: Alfred M. Pollard, General Counsel, Attention: Comments/RIN 2590-AB05, Federal Housing Finance Agency, Eighth Floor, 400 Seventh Street SW, Washington, DC 20219. Deliver the package to the Seventh Street entrance Guard’s Desk, First Floor, on business days between 9 a.m. and 5 p.m.
- U.S. Mail, United Parcel Service, Federal Express, or Other Mail Service: The mailing address for comments is: Alfred M. Pollard, General Counsel, Attention: Comments/RIN 2590-AB05, Federal Housing Finance Agency, Eighth Floor, 400 Seventh Street SW, Washington, DC 20219. Please note that all mail sent to FHFA via U.S. Mail is routed through a national irradiation facility, a process that may delay delivery by approximately two weeks.

See **SUPPLEMENTARY INFORMATION** for additional information on submission and posting of comments.

FOR FURTHER INFORMATION CONTACT: Naa Awaa Tagoe, Senior Associate Director, Office of Financial Analysis, Modeling and Simulations, (202) 649-3140,

naawaa.tagoe@fhfa.gov; Karen Heidel, Assistant General Counsel, Office of General Counsel, (202) 649-3073, karen.heidel@fhfa.gov; or Mark D. Laponsky, Deputy General Counsel, Office of General Counsel, (202) 649-3054, mark.laponsky@fhfa.gov. The telephone number for the Telecommunications Device for the Deaf is (800) 877-8339.

SUPPLEMENTARY INFORMATION:

I. Comments

FHFA invites comment on all aspects of the proposed amendments and will take all comments into consideration before adopting amendments through a final rule.

Copies of all comments received will be posted without change on the FHFA Web site at <http://www.fhfa.gov>, and will include any personal information you provide, such as your name, address, email address, and telephone number. In addition, copies of all comments received will be available for examination by the public through the electronic rulemaking docket for this proposed rule also located on the FHFA website.

II. Background

Section 401 of the EGRRCPA, (Pub. L. 115-174, section 401) amended the Dodd-Frank Act requirements to implement stress testing. Prior to the passage of the EGRRCPA,¹ section 165(i) of the Dodd-Frank Act² required each financial company with total consolidated assets of more than \$10 billion to conduct annual stress tests. In addition, section 165 required FHFA to issue regulations for regulated entities to conduct their stress tests, which were required to include at least three different stress testing scenarios: “baseline,” “adverse,” and “severely adverse.”³ In September 2013, FHFA published in the **Federal Register** a final rule implementing the Dodd-Frank Act stress

¹ Pub. L. 115-174, 132 Stat. 1296 (2018).

² Pub. L. 111-203, 124 Stat. 1376 (2010), codified at 12 U.S.C. 5365.

³ 12 U.S.C. 5365(i)(2)(C).

testing requirements. FHFA's regulation, located at 12 CFR part 1238, requires each regulated entity to conduct an annual stress test based on scenarios provided by FHFA and consistent with FHFA prescribed methodologies and practices. The regulation also requires that the agency issue to the regulated entities stress test scenarios that are generally consistent with and comparable to those developed by the FRB not later than 30 days after the FRB publishes its scenarios.⁴

Section 401 of EGRRCPA amended certain aspects of the stress testing requirements applicable to financial companies in section 165(i) of the Dodd-Frank Act.⁵ Specifically, after 18 months, section 401 of EGRRCPA raises the minimum asset threshold for application of the stress testing requirement from \$10 billion to \$250 billion in total consolidated assets, revises the requirement for financial companies to conduct stress tests "annually," and instead requires them to conduct stress tests "periodically", and no longer requires the stress test to include an "adverse" scenario, thus reducing the number of required stress test scenarios from three to two.

III. Analysis of Proposed Rule

The purpose of this proposed rule is to revise FHFA's stress testing rules applicable to its regulated entities, consistent with amendments made by section 401 of EGRRCPA. The proposed rule would also make additional technical changes to the stress testing rule. In sum, the proposed rule would discontinue the Dodd-Frank Act stress testing of the Banks and reduce the number of scenarios mandated for Enterprise Dodd-Frank Act stress testing.

A. Minimum Asset Threshold

⁴ 12 CFR 1238.3(b).

⁵ Pub. L. 115-174, 132 Stat. 1296-1368 (2018).

As described above, section 401 of EGRRCPA amended section 165 of the Dodd-Frank Act by raising the minimum threshold for financial companies required to conduct stress tests from \$10 billion to \$250 billion. As there are no Banks with total consolidated assets of over \$250 billion, the Banks will no longer be subject to the stress testing requirements of this rule. Though each of the Banks has total consolidated assets of less than \$250 billion, the rule expressly maintains the Director’s discretion to require any regulated entity with assets below the \$250 billion threshold to conduct the stress test. As the total consolidated assets for each Enterprise exceed the \$250 billion threshold, the Enterprises remain subject to stress testing under this rule.

B. Frequency of Stress Testing

Section 401 of EGRRCPA also revised the requirement under section 165 of the Dodd-Frank Act for financial companies to conduct stress tests, changing the required frequency from “annual” to “periodic.” The term “periodic” is not defined in EGRRCPA. Because of the Enterprises’ total consolidated asset amounts, their function in the mortgage market, size of their retained portfolios, and their share of the mortgage securitization market, FHFA proposes to require the Enterprises to conduct stress tests on an annual basis. This is consistent with FHFA’s regulatory mission to ensure each of the regulated entities “operates in a safe and sound manner.”⁶

C. Removal of the “Adverse” Scenario

As discussed above, section 401 of EGRRCPA amended section 165(i) of the Dodd-Frank Act to no longer require the Board to include an “adverse” stress-testing scenario, reducing the number of stress test scenarios from three to two. The “baseline” scenario is a set of conditions that affect the U.S. economy or the financial condition of

⁶ 12 U.S.C. 4513(a)(1)(B)

the regulated entities, and that reflect the consensus views of the economic and financial outlook, and the “severely adverse” scenario is a more severe set of conditions and the most stringent of the former three scenarios. Although the “adverse” scenario has provided some additional value in limited circumstances, the “baseline” and “severely adverse” scenarios largely cover the full range of expected and stressful conditions. Therefore FHFA does not consider it necessary, for its supervisory purposes, to require the additional burden of analyzing an “adverse” scenario.

VI. Coordination with the FRB and the Federal Insurance Office

In accordance with section 165(i)(2)(C), FHFA has coordinated with both the FRB and the Federal Insurance Office (FIO). On November 29, 2018, the FRB published a proposed rule which revised “the minimum threshold for state member banks to conduct stress tests from \$10 billion to \$250 billion,” and revised “the frequency with which state member banks with assets greater than \$250 billion would be required to conduct stress tests,” in addition to removing the adverse scenario from the list of required scenarios.⁷ The FDIC adopted its final rule;⁸ and the OCC its final rule.⁹ Although FHFA’s amended proposed rule would not be identical to those of the FRB, the FDIC, and the OCC, it is consistent and comparable with them. FHFA consulted with the FRB and FIO before proposing these amendments.

V. Paperwork Reduction Act

The proposed rule does not contain any collections of information pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501, *et seq.*). Therefore, FHFA has not submitted any information to the Office of Management and Budget for review.

⁷ 83 FR 61408 (Nov. 29, 2018).

⁸ 84 FR 56929 (Oct. 24, 2019).

⁹ 84 FR 54472 (Oct. 10, 2019).

VI. Regulatory Flexibility Act

The proposed rule applies only to the regulated entities, which do not come within the meaning of small entities as defined in the Regulatory Flexibility Act (see 5 U.S.C. 601(6)). Therefore, in accordance with section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 605(b)), the General Counsel of FHFA certifies that this proposed rule, if promulgated as a final rule, will not have a significant economic impact on a substantial number of small entities.

List of Subjects in 12 CFR Part 1238

Administrative practice and procedure, Capital, Federal Home Loan Banks, Government-sponsored enterprises, Regulated entities, Reporting and recordkeeping requirements, Stress test.

Authority and Issuance

For the reasons stated in the SUPPLEMENTARY INFORMATION section, and under the authority of 12 U.S.C. 5365(i), FHFA proposes to amend part 1238 of Title 12 of the Code of Federal Regulations to read as follows:

Part 1238 — STRESS TESTING OF REGULATED ENTITIES

1. The authority citation for part 1238 continues to read as follows:

Authority: 12 U.S.C. 1426; 4513; 4526; 4612; 5365(i).

2. Amend § 1238.1 to read as follows:

§ 1238.1 Authority and Purpose.

(a) *Authority.* This part is issued by the Federal Housing Finance Agency (FHFA) under section 165(i) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), Pub. L. 111-203, 124 Stat. 1376, 1423-32 (2010), 12 U.S.C. 5365(i),

as amended by section 401 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA), Pub. L. 115-174, 132 Stat. 1296 (2018), 12 U.S.C. 5365(i); and the Safety and Soundness Act (12 U.S.C. 4513, 4526, 4612).

(b) *Purpose.* (1) This part implements section 165(i)(2) of the Dodd-Frank Act, as amended by section 401 of the EGRRCPA, which requires all large financial companies that have total consolidated assets of more than \$250 billion, and are regulated by a primary federal financial regulatory agency, to conduct periodic stress tests.

(2) This part establishes requirements that apply to each Enterprise's performance of periodic stress tests. The purpose of the periodic stress test is to provide the Enterprises, FHFA, and the FRB with additional, forward-looking information that will help them to assess capital adequacy at the Enterprises under various scenarios; to review the Enterprises' stress test results; and to increase public disclosure of the Enterprises' capital condition by requiring broad dissemination of the stress test scenarios and results.

3. Amend § 1238.2 to read as follows:

§ 1238.2 Definitions.

For purposes of this part, the following definitions apply:

Planning horizon means the period of time over which the stress projections must extend. The planning horizon cannot be less than nine quarters.

Scenarios are sets of economic and financial conditions used in the Enterprises' stress tests, including baseline and severely adverse.

Stress test is a process to assess the potential impact on an Enterprise of economic and financial conditions ("scenarios") on the consolidated earnings, losses, and capital of

the Enterprise over a set planning horizon, taking into account the current condition of the Enterprise and the Enterprise's risks, exposures, strategies, and activities.

4. Amend § 1238.3 to read as follows:

§ 1238.3 Annual stress test.

(a) *In general.* Each Enterprise:

(1) Shall complete an annual stress test of itself based on its data as of December 31 of the preceding calendar year;

(2) The stress test shall be conducted in accordance with this section and the methodologies and practices described in § 1238.4 and in a supplemental guidance or order.

(b) *Scenarios provided by FHFA.* In conducting its annual stress tests under this section, each Enterprise must use scenarios provided by FHFA, which shall be generally consistent with and comparable to those established by the FRB, that reflect a minimum of two sets of economic and financial conditions, including a baseline and severely adverse scenario. Not later than 30 days after the FRB publishes its scenarios, FHFA will issue to the Enterprises a description of the baseline and severely adverse scenarios that each Enterprise shall use to conduct its annual stress tests under this part.

5. Amend § 1238.4 to read as follows:

§ 1238.4 Methodologies and practices.

(a) *Potential impact.* Except as noted in this subpart, in conducting a stress test under § 1238.3, each Enterprise shall calculate how each of the following is affected during each quarter of the stress test planning horizon, for each scenario:

(1) Potential losses, pre-provision net revenues, and future pro forma capital positions over the planning horizon; and

(2) Capital levels and capital ratios, including regulatory capital and net worth, and any capital ratios, specified by FHFA.

(b) *Planning horizon.* Each Enterprise must use a planning horizon of at least nine quarters over which the impact of specified scenarios would be assessed.

(c) *Additional analytical techniques.* If FHFA determines that the stress test methodologies and practices of an Enterprise are deficient, FHFA may determine that additional or alternative analytical techniques and exercises are appropriate for an Enterprise to use in identifying, measuring, and monitoring risks to the financial soundness of the Enterprise, and require an Enterprise to implement such techniques and exercises in order to fulfill the requirements of this part. In addition, FHFA will issue guidance annually to describe the baseline and severely adverse scenarios, and methodologies to be used in conducting the annual stress test.

(d) *Controls and oversight of the stress testing processes.* (1) The appropriate senior management of each Enterprise must ensure that the Enterprise establishes and maintains a system of controls, oversight, and documentation, including policies and procedures, designed to ensure that the stress testing processes used by the Enterprise are effective in meeting the requirements of this part. These policies and procedures must, at a minimum, describe the Enterprise's testing practices and methodologies, validation and use of stress test results, and processes for updating the Enterprise's stress testing practices consistent with relevant supervisory guidance;

(2) The board of directors, or a designated committee thereof, shall review and approve the policies and procedures established to comply with this part as frequently as economic conditions or the condition of the Enterprise warrants, but at least annually; and

(3) Senior management of the Enterprise and each member of the board of directors shall receive a summary of the stress test results.

6. Amend § 1238.5 to read as follows:

§ 1238.5 Required report to FHFA and FRB of stress test results and related information.

(a) *Report required for stress tests.* On or before May 20 of each year, the Enterprises must report the results of the stress tests required under § 1238.3 to FHFA, and to the FRB, in accordance with paragraph (b) of this section;

(b) *Content of the report for annual stress test.* Each Enterprise must file a report in the manner and form established by FHFA.

(c) *Confidential treatment of information submitted.* Reports submitted to FHFA under this part are FHFA property and records (as defined in 12 CFR part 1202 of this chapter). The reports are and include non-public information contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of, FHFA in connection with the performance of the agency's responsibilities regulating or supervising the Enterprises. Disclosure of any reports submitted to FHFA or the information contained in any such report is prohibited unless authorized by this part, legal obligation, or otherwise by the Director of FHFA.

7. Amend § 1238.6 to read as follows:

§ 1238.6 Post-assessment actions by the Enterprises.

Each Enterprise shall take the results of the stress test conducted under § 1238.3 into account in making changes, as appropriate, to the Enterprise's capital structure (including the level and composition of capital); its exposures, concentrations, and risk positions; any plans for recovery and resolution; and to improve overall risk management. If an Enterprise is under FHFA conservatorship, any post-assessment actions shall require prior FHFA approval.

8. Amend § 1238.7 to read as follows:

§ 1238.7 Publication of results by regulated entities.

(a) *Public disclosure of results required for stress tests of the Enterprises.* The Enterprises must disclose publicly a summary of the stress test results for the severely adverse scenario not earlier than August 1 and not later than August 15 of each year. The summary may be published on the Enterprise's Web site or in any other form that is reasonably accessible to the public.

(b) *Information to be disclosed in the summary.* The information disclosed by each Enterprise shall, at minimum, include—

(1) A description of the types of risks being included in the stress test;

(2) A high-level description of the scenario provided by FHFA, including key variables (such as GDP, unemployment rate, housing prices, and foreclosure rate, etc.);

(3) A general description of the methodologies employed to estimate losses, pre-provision net revenue, and changes in capital positions over the planning horizon;

(4) A general description of the use of the required stress test as one element in an Enterprise's overall capital planning and capital assessment. If an Enterprise is under conservatorship, this description shall be coordinated with FHFA;

(5) Aggregate losses, pre-provision net revenue, net income, net worth, pro forma capital levels and capital ratios (including regulatory and any other capital ratios specified by FHFA) over the planning horizon, under the scenario; and

(6) Such other data fields, in such form (e.g. aggregated), as the Director may require.

Dated: December 10, 2019.

Mark A. Calabria

Director, Federal Housing Finance Agency.

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