

Basel III Endgame Evolution

Strategic Implications for Alternative Asset Managers

March 25, 2026

On March 19, 2026, the federal banking agencies issued a package of proposed changes to the regulatory capital requirements for banking institutions of all sizes, from the largest GSIBs and super-regional banks to community banks. This package of proposals (the “[Proposed Rules](#)”) is a second full attempt at implementing the 2017 “Basel III Endgame” international framework—following the agencies’ initial package of proposals in July 2023 (the “[2023 NPR](#)”)—to better reflect credit, trading and operational risk in the calculation of regulatory capital ratios. As summarized in our [initial client alert](#), the Proposed Rules would mark the culmination of a nearly decade-long effort to complete the fundamental overhaul of bank capital requirements initially spurred by the 2008-2009 financial crisis.

As part of our series of [industry-focused client memoranda](#), this alert examines the expected impacts of the Proposed Rules on market participants within the [alternative asset management industry](#), including both banking sector participants as well as non-bank asset managers who both partner and compete with banks.

The proposed recalibration of bank capital requirements will likely impact a broad range of participants in credit and liquidity markets, and may present both opportunities and risks for various sectors of the alternative asset management industry (including private equity, private credit, and fund finance). On the one hand, the projected capital relief under the Proposed Rules should enhance the ability of banks to serve as vital upstream credit and liquidity providers to private funds (*e.g.*, through subscription lines and warehouse facilities, or as investors and securities financing counterparties). On the other hand, the proposed risk weight adjustments for corporate (particularly investment-grade) loan exposures may empower banks to compete more effectively with non-bank lenders in some segments of the private credit market, and less punitive capital treatment for bank fee income and seed capital investments may allow banks to more efficiently grow their own asset management capabilities.

The following analysis highlights key aspects of the Proposed Rules to assist asset managers as they navigate the effects of these revised bank capital rules on their business and strategic planning.

Private Credit

POTENTIALLY SIGNIFICANT GROWTH IN BANK CORPORATE LENDING CAPACITY

While the 2023 NPR would have largely collapsed regulatory “tailoring” efforts by applying a one-size-fits-all “expanded risk-based approach” (“ERBA”) to every bank with at least \$100 billion in assets, the Proposed Rules would restore the threshold for mandatory ERBA compliance to banks in Categories I and II (and, to a modified extent, those with significant trading or derivatives activity), generally consistent with the thresholds for “advanced approaches” and market risk requirements under existing capital rules.¹ Banks of any size would be permitted to opt in to ERBA standards.²

With this return to regulatory differentiation, as a general matter banks with under \$700 billion in total assets³ will continue to be subject to simpler calculations of capital and risk-weighted assets under a “Standardized” approach, and be exempt from the new operational risk framework (among others) which would have imposed additional capital charges on fee income from various business lines including lending, asset and wealth management and investment advisory services. For banks subject to either capital approach, the proposed amendments are expected to provide broad regulatory capital relief (with common equity tier 1 capital requirements expected to decline by 2.4% for the largest banks subject to the ERBA, 3% for large regional banks subject to the simplified Standardized Approach, and nearly 8% for Standardized Approach banks under \$100 billion in asset size).

For corporate lending in particular, both proposed capital approaches would reduce the applicable asset risk weights—and resulting regulatory capital charges—compared to the flat 100% risk-weighting currently applicable under existing capital rules:

- **Standardized Approach (Regional & Community) Banks:** The Proposed Rules would replace the current 100% corporate loan risk weight with a single across-the-board 95% risk weight for most corporate loan exposures, without segmenting by borrower creditworthiness.
- **ERBA (GSIBs and ≥ \$700B Super-Regional) Banks:** The Proposed Rules would allow for a preferential 65% risk for corporate loan exposures to any company deemed “investment grade” based on the bank’s qualifying internal credit risk rating system (and defaulting to the current 100% risk weight for other non-investment grade corporate loan exposures). While the 2023 NPR would have limited this preferential

¹ Category III and IV banks would, however, be required to recognize AOCI in regulatory capital, subject to a five-year phase-in period.

² The Proposed Rules estimate that several Category III and IV banks, and up to one-third of smaller banks, would see significant reductions in capital requirements by opting in to the ERBA standards.

³ Category II banks that would be subject to Operational Risk, Market Risk, and CVA Risk frameworks also include banks with ≥ \$75 billion in cross-jurisdictional activity, regardless of asset size. Market Risk and CVA Risk frameworks would also apply to banks that are not in Category I or II but have significant trading activity (and, in the case of the CVA Risk framework, significant OTC derivative exposures).

Descriptions in this client alert of provisions applicable to banks with “≥\$700 billion in assets” would also apply to these other banks that have less than \$700 billion in assets but also significant cross-jurisdictional, trading and/or derivatives activities.

65% risk weight only to exposures where the corporate counterparty is *publicly listed* on an exchange, the Proposed Rules extend the preferential 65% corporate loan risk-weight to all investment grade borrowers—regardless of whether the borrower is publicly listed—effectively removing the private company premium that the 2023 NPR would have imposed on creditworthy but unlisted borrowers.

The 5-percentage-point reduction in corporate loan risk weighting under the proposed Standardized Approach, and the up-to-35-percentage-point reduction in corporate loan risk weighting under the proposed ERBA, would contribute to reductions in aggregate risk weighted corporate loan assets of over 7% for regional and community banks, and over 18% for the largest money center banks.⁴

According to the banking agencies, these risk-weighted asset reductions could translate to up to \$226 billion in additional balance sheet lending capacity attributable to the reduced capital requirements for corporate loan assets for Standardized Approach regional and community banks. Applying the same lending-capacity projection method used in the Standardized Approach proposal to banking-agency data in the ERBA proposal, we estimate that the projected risk-weighted asset reductions could translate to up to \$441 billion in additional balance sheet lending capacity attributable to the reduced capital requirements for corporate loan assets for GSIBs and other ERBA banks.⁵

The impacts of this increased balance sheet lending capacity to bank participation in private credit markets could be significant. Among Standardized Approach banks, the balance sheet capacity expansion effects may be particularly beneficial to the larger regional banks: based on agency data, banks between \$100-\$700 billion in total assets hold approximately twice the volume of corporate loans as banks with assets between \$10 billion and \$100 billion. With expanded balance sheet resources, these larger regional banks may be able to improve their competitiveness in the private credit market, particularly for mid-market borrowers or specialty lending lines with which these banks may be able to leverage their local geographic experience and relationships (even if the decline in corporate loan risk-weighting, from 100% to 95%, is relatively modest for these banks).

Further, the preferential 65% corporate loan risk weight under the ERBA could significantly reduce regulatory costs associated with private credit lending for the largest banks, despite the risk-weight advantage being limited

⁴ Effects of “credit conversion factor” changes for off-balance sheet exposures, as well as operational risk charges under the ERBA, also contribute to the total amount by which risk weighted corporate loan assets would be reduced under the Proposed Rules.

⁵ Based on (i) bank-agency projected corporate loan risk-weighted assets of \$1,604 billion for ERBA banks, compared to \$1,964 billion of corporate loan risk-weighted assets for ERBA banks under current capital rules (implying a total reduction of ~\$360 billion in corporate loan risk-weighted assets, and an average ~82% ERBA risk weight for corporate loan exposures, reflecting the agencies’ estimate that approximately 53% of on-balance sheet corporate exposures would be classified as “investment grade” and subject to the 65% risk weight), and (ii) the lending capacity projection formula described in the Standardized Approach, equal to the asset class RWA Reduction *divided by* its Average Proposed Risk Weight).

When combined with the effects of reduced capital charges against residential mortgages, retail loans and other assets, the banking agencies project that new balance sheet capacity potentially available for these Standardized Approach banks to lend to businesses and consumers would be a massive \$1.17 trillion (exclusive of securitization effects), equivalent to 9% of the total U.S. bank loans and leases currently outstanding. Under the projection methods described above, this figure would further increase by approximately \$583 billion, to a total of \$1.75 trillion of total increased bank capacity for business and consumer loans, when accounting for potential increased loan capacity of the largest GSIBs and other ERBA banks.

to investment grade exposures. Investment grade loans have become an increasingly important part of the private credit market, with industry analyses estimating average annual investment-grade private credit issuances of approximately \$100 billion over the past decade resulting in a current investment-grade private credit market of approximately \$1 trillion (compared to the \$6 trillion public investment-grade market).⁶ Investment-grade private credit deal volumes have recently reached record levels both in terms of overall market issuance and average deal size, and industry analysis has generally predicted that this growth trajectory for investment-grade private credit loans (including for bank-acted private credit) will persist.⁷

To be sure, many banks may choose to deploy portions of their additional capital unlocked by these reduced corporate loan capital charges toward other asset classes, shareholder capital distributions, M&A or strategic initiatives other than corporate lending. Thus, the agencies' estimates of potential additional lending capacity are likely to overstate the actual corporate bank loan growth—including in private credit markets—that would result from the capital amendments. Nevertheless, these projections indicate the potential for the proposal to drive expansion in bank lending that could partially reverse the ongoing migration of activity to the nonbank financial sector, particularly in the private credit space—which is one of the stated goals of the Proposed Rules.

ABSENCE OF BASEL PREFERENCES FOR PROJECT FINANCE AND SME LOANS

The proposal would introduce a new treatment of project finance exposures for banks subject to the ERBA, applying a more punitive 130% risk weight during the project's "pre-operational phase" and a 100% risk weight during the "operational phase" (when the project has sufficient net cash flow to support the project's debt service). Unlike the Basel international standards, the proposal omits a preferential 80% risk-weight for exposures to "high-quality" infrastructure projects that have demonstrated robust ability to meet financial commitments even in the event of adverse changes to the economic cycle or conditions. For banks subject to the Standardized Approach, project finance loans would be assigned a flat 95% risk weight under the general "corporate exposure" category.

Similarly, the proposal declines to adopt a separate preferential risk-weight category for small- and medium-sized enterprise loans (in contrast to the dedicated 85% risk weight for corporate SMEs under the international Basel standard), effectively defaulting most SME loans to a 100% risk weight for banks subject to the ERBA, or the flat 95% corporate loan risk weight for banks subject to the Standardized Approach.

⁶ Sources: Wellington Management Institutional Insights, "Investment-grade private credit market deep dive," (October 2025); Voya Investment Management, "A Guide to Investment Grade Private Credit," (June 2025); Apollo Global Management, "Demystifying the Opportunity in Investment Grade Private Credit," (December 2024); McKinsey & Company Insights, "The next era of private credit," (September 2024).

⁷ *Id.*

COLLATERALIZED LOAN OBLIGATIONS

Compared to the 2023 NPR, the Proposed Rules would reduce bank capital charges for securitizations such as CLOs by lowering the applicable supervisory capital calibration parameter and by implementing certain other improvements for high-quality, lower-risk securitizations which, together, the banking agencies expect would incentivize banks to hold more securitized assets and encourage the sale of loan pools to securitization structures.

In particular, the Proposed Rules would restore the applicable “p-factor” supervisory capital calibration parameter to 0.5 (down from the 1.0 proposed in the 2023 NPR), effectively reducing the supervisory surcharge applicable to securitization exposures to account for risks not fully captured by the underlying assets, such as concentration and correlation risk.

Beyond the reduced “p-factor” calibration parameter, the Proposed Rules would reduce the supervisory risk-weight floor for most securitizations from 20% to 15%, which the agencies note should be particularly beneficial for more senior tranches of securitization exposures—*e.g.*, AAA-rated CLO securities—for which the risk-weighting “floor” would be more likely to be binding. The proposal would also introduce a “look-through approach” to risk weighting senior securitization exposures, which would allow a bank to cap the risk weight applied to a senior securitization exposure (other than a resecuritization) at the weighted-average risk weight of the securitization’s underlying exposures, so long as the bank has sufficient information on the composition of the underlying exposures.

The banking agencies project that the Proposed Rules would reduce risk-weighted assets attributable to securitization exposures by an estimated \$21 billion for Standardized Approach banks, resulting in up to \$91 billion of additional Standardized Approach bank balance sheet capacity for securitizations.

Since the mechanics of the Proposed Rules specifically favor high-quality senior tranches, which are the primary holdings for bank investors in the CLO market, these capital amendments could provide a significant incentive for banks to increase their securitization activities.⁸ The agencies note that if banks’ increased securitization activities were to approach the projected \$91 billion of additional balance sheet capacity for securitizations, these capital amendments may place downward pressure on prices of securitized assets. For CLO issuers, this could mean lower funding costs as bank demand for senior tranches increases. Further, to the extent that the Proposed Rules make it more economically attractive for banks to aggregate and sell corporate loans into CLO pools and/or invest in CLO securities, these amendments could enhance pools of bank capital for CLO managers, and foster a potentially more active secondary market for CLO tranches. In turn, these could improve the liquidity and risk diversification in leveraged loan markets.

⁸ Federal Reserve FEDS Notes, “*Who Owns U.S. CLO Securities? An Update by Tranche*,” (June 2020) (finding that the vast majority—95.4%—of CLO security holdings by banks are senior tranche securities).

BALANCE SHEET AND RISK MANAGEMENT TRANSACTIONS

In recent years, banks have increasingly used synthetic risk transfers and other forms of credit risk mitigation transactions to manage capital-imposed balance sheet constraints, often transacting with private credit funds or other investors, such as credit hedge funds, to share risk on leveraged loans or other portfolios of credit assets. However, existing capital rules leave significant ambiguity as to the regulatory capital treatment of such balance sheet-management transactions.

For example, under existing capital rules, balance sheet-management transactions that qualify as “synthetic securitizations” allow banks to recognize credit risk-mitigating benefits of “financial collateral” for regulatory capital purposes. However, cash proceeds from pre-funded credit protection—as in the case of sales of credit-linked notes—generally do not qualify as eligible “financial collateral” under the credit risk mitigation framework of existing capital rules, despite the clear credit risk benefits of such upfront cash payments. While the Federal Reserve has permitted certain banks to recognize the credit risk-mitigating benefits of CLN cash proceeds on an ad hoc basis under its “reservation of authority” powers, it has not yet codified generally applicable standards that would permit the broader banking industry to conduct such transactions under a clear regulatory roadmap.

The Proposed Rules would recalibrate aspects of the credit risk mitigation capital framework to more appropriately account for the credit risk reduction achieved through various balance sheet-management transactions and structures, including by codifying eligibility standards for pre-funded cash proceeds from directly-issued CLNs as eligible credit risk mitigants.

These clarifications in the Proposed Rules should provide both banks and alternative investors (as credit protection providers) more certainty when participating in these risk-sharing transactions, and may facilitate further expansion of synthetic risk transfer partnerships between banks and private credit funds and hedge funds.

Fund Equity Exposures

REGULATED FUNDS – LOOK-THROUGH APPROACH

Current capital rules allow banks to assign risk weights to equity interests in investment funds without material leverage—such as 1940 Act-registered funds, collective investment funds and pension funds, which are generally subject to regulatory restrictions on leverage—using one of three optional “look-through” approaches:

- a “full” look-through approach if the bank has sufficient verified information to calculate a risk-weighted asset amount for each of the fund’s underlying investments;
- an “alternative modified” look-through approach in which the bank assigns the fund’s carrying value to different asset categories on a pro rata basis based on the investment limits specified in the fund’s offering materials and applies the rule’s applicable risk weights to each of those allocated amounts, or

- a “simple modified” look-through approach in which the bank’s RWA amount for a fund interest is the investment’s carrying value multiplied by the *highest risk weight* applicable to *any* exposure the fund is permitted to hold under its specified investment mandate.

The 2023 NPR would have removed the optionality for a bank to choose which of the look-through approaches to apply—instead imposing a strict hierarchy requiring use of the “full” look-through approach whenever sufficient verified information was available—and eliminated the availability of the “simple modified” look-through approach, replacing it instead with a fallback requirement to apply a highly punitive 1,250% risk weight to the fund investment’s carrying value if the bank lacks sufficient information to apply either of the other two look-through approaches.

The Proposed Rules would essentially uphold the current treatment of equity interests in non-leveraged investment funds by restoring the availability of the “simple modified” look-through option, as well as banks’ ability to choose between any of the three look-through approaches for any fund investment (without a mandatory 1,250% risk weight for fund investments lacking granular portfolio investment data). While the optional use of the “alternative modified” or “simple modified” look-through approaches would not allow banks to apply lower risk weights to investment fund investments than would apply under the “full” look-through approach, it would relieve banks from the burdensome and time-consuming requirement to make exposure-by-exposure risk weight determinations for fund portfolio investments (particularly for investments in funds sponsored by unaffiliated non-bank managers).

PRIVATE FUNDS – “NON-SIGNIFICANT INVESTMENTS” BUCKET

Bank investments in most private funds would generally be risk-weighted under the “simple risk-weight approach” (rather than the look-through approaches described above) due to the typical leverage levels of those funds. Under existing capital rules, banks are permitted to assign a favorable 100% risk weight to a broad class of equity exposures, including investments in private funds, up to an aggregate 10%-of-total-capital “bucket.”

The 2023 NPR would have eliminated this long-standing 100%-risk-weight bucket for banks’ non-significant equity exposures below 10% of their total capital, and would have instead generally applied a 400% risk weight for investments in private funds. While banks’ ability to invest in private funds has been broadly restricted under the Volcker Rule, this change would have quadrupled the capital costs for banks’ Volcker-permitted investments in private funds such as credit funds and seed capital investments in bank-sponsored funds.

By reinstating the 100%-risk-weight bucket for banks’ non-significant equity exposures, the Proposed Rules would avoid deterring banks from expanding their Volcker-permitted private fund sponsorship activities, while also fostering bank investments in Volcker-permitted third-party sponsored funds (such as qualifying credit funds). This reversal in the Proposed Rules would also reduce capital costs for banks’ investments in tax credit equity funding structures, such as those for low-income housing, renewable energy investments or historic preservation.

Fund Finance

FUND-LEVEL CREDIT FACILITIES

Under existing bank capital requirements, on-balance sheet fund finance loans such as subscription, warehouse and back-leverage facilities are generally treated as corporate exposures subject to the flat 100% risk-weighting described above. In addition, bank capital rules apply a “credit conversion factor” to capture the off-balance sheet risk of future draws against a bank’s loan commitment, resulting in a capital charge against the undrawn portions of revolving commitments (including most typical fund finance loans). Under existing capital rules, these conversion factors generally vary based on the maturity of the facility, with lower conversion factors (and thus lower capital charges) applying to shorter-term commitments and those that are unconditionally cancelable by the bank.

As discussed above, the Proposed Rules would apply a 5-percentage-point reduction to existing risk weights for corporate loan exposures—including fund finance facilities—for banks subject to the proposed Standardized Approach.

Even more significantly, banks subject to the ERBA framework should be able to apply the preferential 65% risk weight for investment grade corporate exposures to a wide range of fund finance facilities. By abandoning the 2023 NPR’s public listing requirement for the 65% risk weight, discussed above (which would have made this preferential risk-weight unavailable for fund finance loans to unlisted private funds, pension funds and 1940 Act funds), banks subject to the ERBA framework would be able to apply the 65% risk-weight to any non-subordinated subscription line, back-leverage or similar facility to funds that are considered “investment grade” (as determined by the bank’s own qualifying internal credit risk rating system, regardless of whether the fund has obtained a credit rating from a ratings agency).

Further, the Proposed Rules would change the risk weighting approach for undrawn commitments from a series of graduated factors to a single 40% credit conversion factor for all undrawn commitments (regardless of original maturity) except those that are unconditionally cancelable. This change would result in higher capital charges for undrawn commitments with an original maturity of one year or less (increasing from 20% to 40%), but *lower* capital charges for commitments with maturities exceeding one year (decreasing from 50% to 40%).⁹

The practical impact of these proposed amendments could be significant to the fund finance market. While regulators have noted that granular data on the size of banks’ loan exposures to private funds is challenging to obtain, the Federal Reserve has recently found committed credit lines by large U.S. banks to private credit vehicles

⁹ For unconditionally cancelable commitments, the impact of the Proposed Rules’ CCF amendments would diverge by bank size and applicable capital framework: banks subject to the ERBA would face a new 10% CCF for unconditionally cancelable undrawn commitments, while those subject to the Standardized Approach would retain a 0% CCF for unconditionally cancelable commitments under risk-based capital rules. These CCF rules for unconditionally cancelable facilities are not typically relevant for fund finance facilities.

(including private debt funds and BDCs)—a subset of the overall fund finance market—to be about \$95 billion (as of year-end 2024), representing about 7% of banks’ regulatory capital on average.¹⁰

Over 80% of these outstanding bank facilities (~\$79 billion) are in the form of revolving credit lines, with the undrawn portions of these facilities subject to capital charges under the “credit conversion factor” rules. The Federal Reserve found that these private-credit-vehicle facilities had average utilization rates of only approximately 56% and average maturities between 2.6 to 4.1 years, such that the proposed “credit conversion factor” amendments would *lower* the capital charges against the approximately \$35 billion in undrawn commitments under these facilities compared to existing capital rules.

Notably, the Federal Reserve also found that about 60% of these bank fund-finance loan commitments are concentrated among five U.S. GSIBs and that, on average across all large banks, these exposures have investment-grade ratings based on banks’ own credit risk rating determinations. In particular, approximately \$62 billion (or ~65%) of fund-finance bank facilities to private credit vehicles were found to be investment grade. Even when only accounting for the ~60% of these facilities held by the top five U.S. GSIBs, this would imply that at least \$37 billion of such fund finance facilities could be eligible for a 35% risk-weight reduction under the proposed ERBA framework.

The Proposed Rules could thus meaningfully expand banks’ willingness to lend to high credit quality investment funds, reduce bank disincentives against providing higher credit limits for committed fund finance facilities, and potentially lower borrowing costs for those funds. Even conservatively assuming that only 60% of these facilities are held by ERBA banks, the combined effects of the Proposed Rules’ risk weighting and “credit conversion factor” amendments on capital charges for private credit vehicle facilities implies a total reduction in risk weighted assets for these facilities of about \$15.1 billion¹¹ and an average risk weight of 65.7%.¹² Applying the same lending-capacity projection method used in the Standardized Approach proposal to this data, we estimate that the projected risk-weighted asset reductions could translate to up to \$23 billion in additional balance sheet lending capacity for fund finance facilities to private credit vehicles.

¹⁰ Federal Reserve FEDS Notes, “*Bank Lending to Private Credit: Size, Characteristics, and Financial Stability Implications*,” (May 2025).

¹¹ Aggregate baseline RWA for such facilities under current capital rules determined to be ~\$77.5 billion, based on \$60 billion in on-balance sheet drawn commitments and term loans, plus \$17.5 billion of off-balance sheet exposure after applying a 50% CCF to \$35 billion in undrawn revolving commitments, each risk weighted at 100%. Aggregate baseline RWA of \$77.5 billion conservatively allocated 60% (\$46.5B) to ERBA banks and 40% (\$31B) to Standardized Approach banks.

Resulting RWA for such facilities under Proposed Rules determined to be ~\$62.4 billion, based on (i) \$60 billion in on-balance sheet loans (allocated \$36B to ERBA banks and \$24B to Standardized Approach banks), plus \$14 billion of off-balance sheet exposure after applying a 40% CCF to \$35 billion in undrawn revolving commitments (allocated \$8.4B to ERBA banks and \$5.6B to Standardized Approach banks), (ii) a total investment-grade portion of ~65% (as described above), relevant only to ERBA bank exposures and assumed to be allocated proportionally among the \$44.4 billion of combined drawn and undrawn ERBA bank exposure amounts, (iii) a 65% risk weight applied to the ~\$28.9 billion of ERBA bank investment-grade exposures, and a 100% risk weight applied to the ~\$15.5 billion of ERBA bank non-investment grade exposures, and (iv) a 95% flat risk weight applied to the ~\$29.6 billion of Standardized Approach bank exposures.

¹² Average risk weight determined by dividing the resulting \$62.4 billion in resulting RWA for such facilities under the Proposed Rules by the total \$95 billion in non-risk-weighted commitments for such facilities.

SECURITIES FINANCING TRANSACTIONS

Current capital rules allow banking organizations to recognize credit risk-mitigation benefits of collateral received by banks in SFTs (including repo-style transactions and margin loans) by adjusting the bank's exposure amount based on the amount of such collateral. The risk-mitigating benefits of financial collateral is adjusted through a formula that includes standard supervisory price volatility haircuts, to account for market price volatility in the value of the collateral.

The 2023 NPR would have tightened capital rules applicable to SFTs by applying mandatory minimum haircut floors to financial collateral exchanged in an SFT with an "unregulated" financial institution (explicitly including hedge funds and private equity firms), effectively requiring banks to receive a minimum amount of overcollateralization (depending on the quality of collateral) when engaging in repos or margin lending with such entities. If the collateral received on a repo or margin loan did not meet this mandatory minimum, the bank would have been required to treat the transaction as if it were entirely unsecured (thus negating the risk-mitigating capital benefits of any collateral the bank did receive).

In a significant reversal, the banking agencies will *not* adopt minimum haircut floors for collateral backing repos and margin loans with funds and other non-bank financial firms. However, the Proposed Rules would still modernize the collateral haircut approach by partially recognizing the netting and diversification benefits of instruments exchanged within a netting set. This is expected to improve risk sensitivity compared to the current "simple" approach.

Bank and non-bank industry participants had argued that STF activity is important for price discovery, market liquidity and hedging strategies, and that the blunt "cliff" effects of the 2023 NPR's would have disrupted the functioning of these critical markets. A quantitative impact study conducted by SIFMA and ISDA estimated that this removal of the minimum haircut floor framework would result in a 26% reduction in RWAs for all securities financing transactions with unregulated financial institutions.

Bank Asset Management-Related Operations

Consistent with the Basel international standards, the Proposed Rules would introduce a standardized capital requirement for operational risk applicable to banks subject to the ERBA framework. This framework replaces the internal models-based "Advanced Measurement Approach" to operational risk (currently applicable to Category I and II banks under "advanced approaches" standards) with a standardized methodology based on the "business indicator," a financial statement proxy for a bank's volume of different component businesses.

While the 2023 NPR included a punitive scalar (the internal loss multiplier) that could have increased (but never decreased) operational risk capital charges based on a firm's ten-year loss history, the Proposed Rules eliminate this multiplier, so that operational risk capital charges vary based solely on business volume (using the "business indicator" proxy) and are not adjusted upwards or downwards due to historical losses.

The Proposed Rules also recalibrate the measurement of the “business indicator” to mitigate impacts of operational risk capital charges on fee-based businesses like asset management and custody services. For example, while the 2023 NPR would have measured services income and expenses on a *gross* basis without any netting or cap (for purposes of determining the scale of a bank’s service-related operational risk), the Proposed Rules measure service-related operational risk using fee income and expenses on a *net* basis. The Proposed Rules would also simplify the “business indicator” calculation by collapsing the separate business indicator subcomponents from three to two (interest and non-interest components).

Significantly, the Proposed Rules would also introduce a targeted reduction in operational risk capital requirements for a variety of bank asset management-related functions that have been determined to exhibit lower historical loss rates relative to their revenue. In particular, the Proposed Rules would apply a *70% discount* for a bank’s net income attributable to the following services when calculating “business indicator” volume for purposes of operational risk capital charges:

- *Investment Management Activities*: Businesses related to asset and wealth management, private banking, and investment advisory services;
- *Investment Services*: Businesses related to asset servicing, such as custody, fund services, securities lending, liquidity services, and collateral management;
- *Treasury Services*: Businesses related to cash management, global payments, and deposit services (other than lending activities).

The Proposed Rules estimate that the new operational risk charges for “other banking services” (consisting largely of investment management, advisory and custody services) would increase bank risk weighted assets by \$144 billion. However, this operational risk capital impact under the Proposed Rules would be significantly reduced compared to the 2023 NPR and, when compared to the operational risk charges across all business lines under the current “advanced approaches” rules, would result in an over-\$800 billion reduction in aggregate risk weighted assets attributable to operational risk (from \$1.745 trillion to \$927 billion).

Similar to other aspects of the Proposed Rules, the proposed capital relief for bank investment management functions relative to the 2023 NPR could present double-edged impacts for non-bank asset managers. On the one hand, lower capital costs for services businesses may allow funds and their investors to avoid additional fees for bank-provided fund services (such as securities custody services for registered funds) that would otherwise have been passed on to the fund. On the other hand, this operational capital relief may strengthen banks’ ability to compete with non-bank managers for investment or wealth management clients.

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