Portfolio Media. Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Loan Transparency Proposals May Bring Some Clarity

By **Chris van Heerden** (February 14, 2024, 6:07 PM EST)

Chris van Heerden

Could one of the great mysteries of the fund finance universe be on the verge of becoming less mysterious?

That's one possible question after U.S. banking regulators in December proposed[1] revisions to the Consolidated Reports of Condition and Income that would require banks to disclose more granular information about loans made to nondepository financial institutions, or NDFIs, including private equity funds.

Calling for Information

Call reports date back to the early 1830s when the secretary of the U.S. Department of the Treasury was first granted authority to call on banks for information in what started as an ad hoc, on-demand process.

Today, every U.S. bank and savings association is required to make a quarterly call report filing in a process administered by the Federal Financial Institutions Examination Council.

Three forms of the report exist: one for banks with domestic and foreign offices; one for banks with domestic offices only; and one for banks with domestic offices only and total assets below $5 billion.

U.S. branches and agencies of foreign banks separately file a different form, which parallels the call reports, but without an income report. The forms are dynamic, and updates are relatively frequent and responsive to industry developments, accounting changes and supervisory priorities.

Call reports summarize key measures of financial condition and income in a standardized template that allows for comparisons between institutions and group aggregation.

While the data is publicly available, the primary end users are federal and state banking supervisors — which is readily apparent from the data format and the web interface — who use call reports to inform bank examinations, M&A application reviews and industry regulation.

But, given that the majority of U.S. banks are not publicly listed, call reports are an indispensable tool for shaping a current, representative view of the industry.

NDFI Loans: A Recent Addition

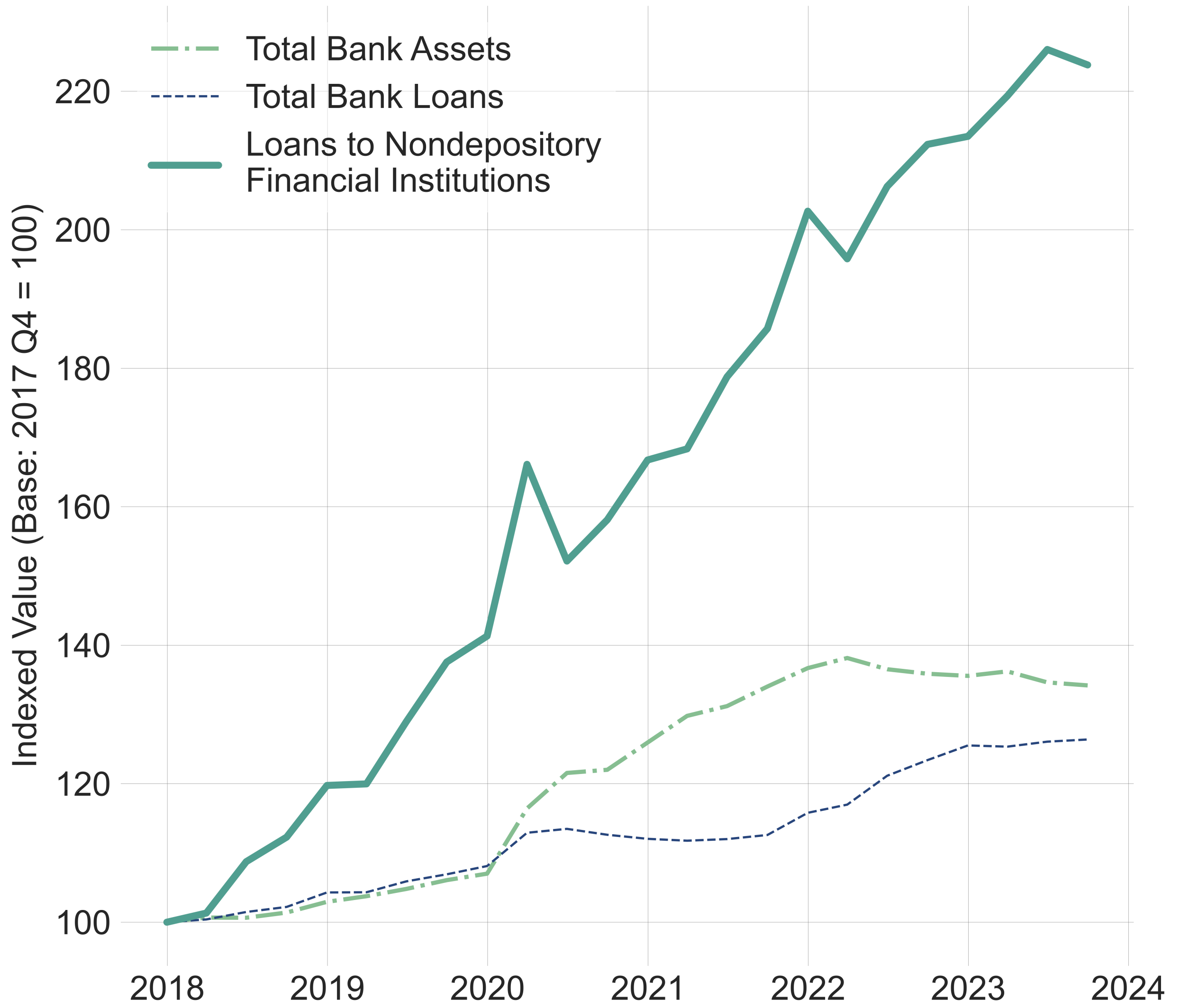
Among the loan classifications in the call report, "Loans to nondepository financial institutions" is a relatively recent addition, having been added in 2010, after the subject of bank intermediation of nonbank financial activity rose to the forefront.

The utility of the NDFI loan category, however, has been limited by its breadth: NDFIs for reporting purposes include insurance companies, mortgage lenders, business development companies, real estate investment trusts, marketplace lenders and private funds, among a range of other entities.

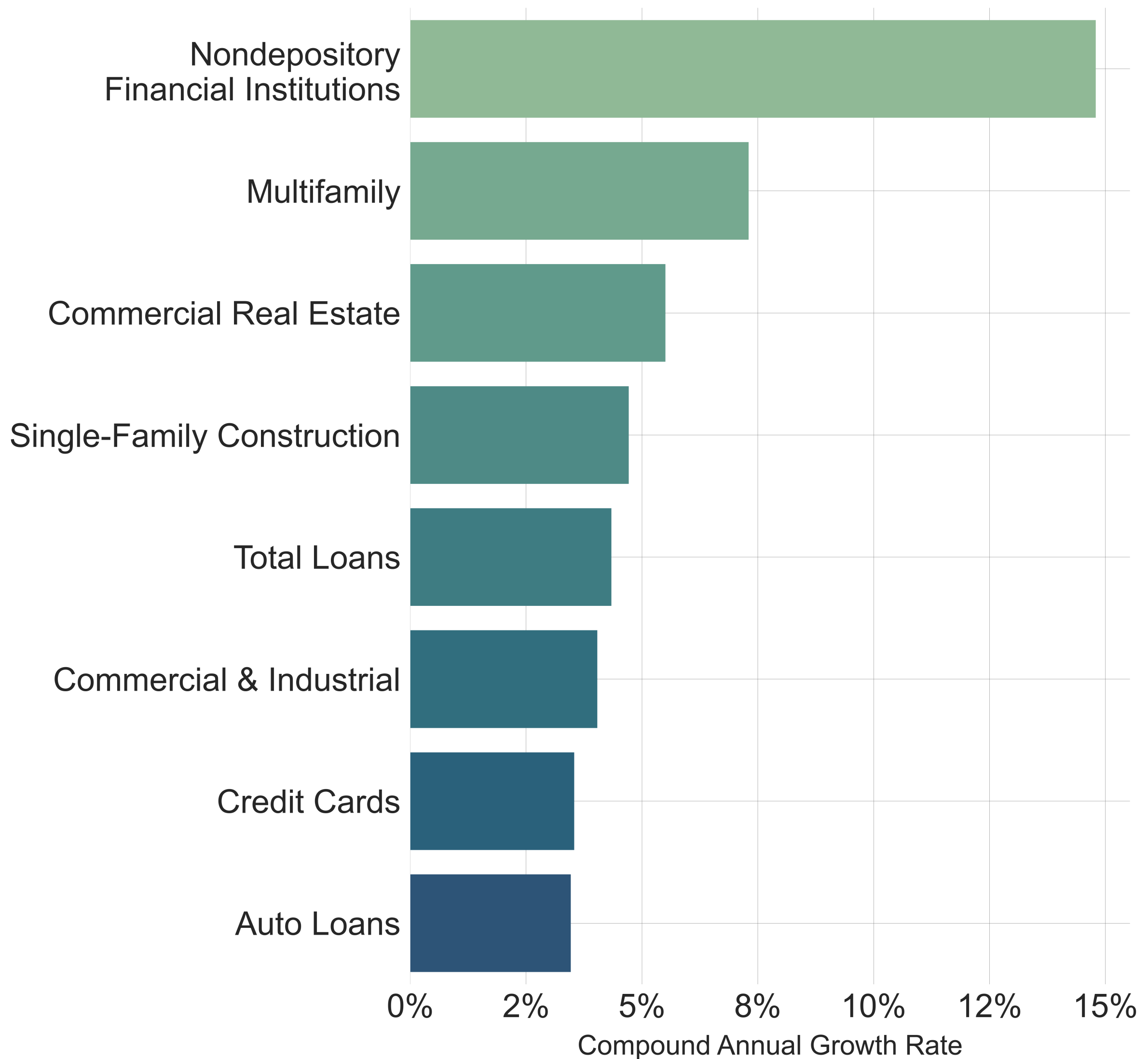
The catch-all nature of the NDFI loan category makes the results difficult to interpret, but growth in this category has attracted attention for understandable reasons.

Exhibit 1: Loans to Nondepository Financial Institutions in Context

Industrywide Indexed Asset and Loan Growth



Note: Based on call report data through Q3 2023.
Source: BankRegData and Cadwalader, Wickersham & Taft LLP.



Note: Based on call report data through Q3 2023.
Source: BankRegData and Cadwalader, Wickersham & Taft LLP.

NDFI loans have been one of the fastest growing lending categories in recent years, and the total balance of these loans is up more than 120% over the past five years.

This growth, however, has to be viewed in context: Over the same period, global private fund assets under management expanded by more than 130%, according to Preqin data, and Federal Reserve reports show a long-term shift in business and consumer lending into the nonbank financial sector. Therefore, the growth in NDFI loans is best understood within the broader trends in capital formation in the U.S.

Reading Between the Lines

Per the proposed NDFI revisions, call report filers with total assets of $10 billion or more would be required to provide additional detail regarding their lending exposure to NDFIs.

Specifically, in addition to reporting their overall lending to NDFIs — as such term would be clarified by the proposed NDFI revisions — those banks would be required to separately report their exposures to: (1) mortgage credit intermediaries, (2) business credit intermediaries, (3) private equity funds, (4) consumer credit intermediaries, and (5) other nondepository financial institutions.

Call report filers with total assets of $10 billion or more also would be required to report their unused

commitments, using those same five categories.

The proposed NDFI revisions are part of a banking agency proposal that also included proposed updates to disclosures related to guaranteed structured products and anticipated mandatory long-term debt issuance, and modifications to the attestation and electronic signature requirements. The comment period is open until Feb. 26.

Some reading between the lines of the proposed NDFI revisions may be appropriate. Another recently proposed rulemaking also calls attention to bank exposure to private equity.

Specifically, the global systemically important bank surcharge proposal[2] that accompanied the Basel III endgame rule draft revises the approach to measuring the financial system interconnectedness factors used for calculating the GSIB surcharge to specifically include private equity fund exposure.

The GSIB surcharge is an additional layer of capital a GSIB is required to maintain over and above the minimum risk-based capital standard. The proximity in time of the two in-process proposed rulemakings suggests that bank exposure to private funds has the attention of regulators.

Toward Useful Information

Back to the mysteries of the universe.

A natural question is whether the additional data under the proposed NDFI revisions will clarify the intersection between banks and private funds. On this point, the size of the fund finance market, for example, which describes loans provided to private funds most often by banks and most often on a bilateral basis, has historically been based on estimates.

Will the proposed NDFI revisions clarify the size of the fund finance market?

For now, the answer is "not completely." For one thing, the term "private equity fund" is often bandied about as shorthand for all closed-end private funds, and the proposed revisions do not clearly define this term.

Accordingly, unless the agencies provide additional clarity, individual banks are likely to land in different places on what is and what is not included under this generic heading, thereby clouding the ability to interpret the data.

Unless clarified by the agencies, overlap between the added subcategories could also hamper the usefulness of the results, particularly for private credit funds that, depending on the fund configuration, could reasonably be grouped under either private equity, business credit intermediary, mortgage credit intermediary, or other NDFI.

While full enlightenment on the intersection between banks and private funds does not look likely in the near future, it is fair to expect closer attention to this area in 2024.

Chris van Heerden is a director at Cadwalader Wickersham & Taft LLP.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of their employer, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] https://www.govinfo.gov/content/pkg/FR-2023-12-27/pdf/2023-28473.pdf.

[2] https://www.govinfo.gov/content/pkg/FR-2023-09-01/pdf/2023-16896.pdf.

All Content © 2003-2024, Portfolio Media, Inc.