



Weekly Newsletter

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Recent Supervisory Actions

Bank & Thrift

Agencies Approve Proposed Rule to Implement the Volcker Rule Prohibitions and Restrictions on Proprietary Trading and Certain Activities

On October 11, the Federal Deposit Insurance Corporation ("FDIC"), Office of the Comptroller of the Currency ("OCC") and Federal Reserve Board ("Fed") each released a joint proposed rule that would implement Section 619 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (the "Dodd-Frank Act"). The Securities and Exchange Commission ("SEC") is expected to approve the same joint proposed rule shortly. Comments are requested through January 13, 2012 and commenters are specifically encouraged to submit their written comments to all of the issuing agencies.

Section 619 of the Dodd-Frank Act, commonly referred to as the "Volcker Rule," contains certain prohibitions and restrictions on the ability of banking entities (insured depository institution, bank holding company, and their subsidiaries and affiliates) and nonbank financial companies supervised by the Fed to engage in proprietary trading and have certain interests in, or relationships with, a hedge fund or private equity fund. Certain exemptions from these prohibitions and restrictions are available. The Dodd-Frank Act also prohibits banking entities from entering into any transaction or engaging in any activity that would (i) involve or result in a material conflict of interest, (ii) result in a material exposure to high-risk assets or high-risk trading strategies, (iii) pose a threat to the safety and soundness of the banking entity, or (iv) pose a threat to the financial stability of the U.S.

Transactions in certain instruments, including obligations of the U.S. government or a U.S. government agency, the government-sponsored enterprises, and state and local governments, are exempt from the statute's prohibitions. Other activities that are exempted include market making, underwriting, and risk-mitigating hedging. The statute also permits banking entities to organize, offer, and invest in a hedge fund or private equity fund subject to a number of conditions.

Under the proposed rule, banking entities would be required to establish an internal compliance program designed to ensure and monitor compliance with the statute's prohibitions and restrictions, and the agencies' implementing regulations. The internal compliance program would be subject to oversight by the banking entity's board of directors and the appropriate Federal supervisory agency. Banking entities with significant trading operations would be required to report to the appropriate Federal supervisory agency certain quantitative measurements that are intended to assist the agencies and banking entities in the identification of prohibited proprietary trading in the context of exempt activities, as well as high-risk assets or trading strategies.

For additional information please contact Hugh Kelly, Principal: hckelly@kpmg.com or Jon Greenlee, Managing Director: jgreenlee@kpmg.com

Fed Issues Horizontal Reviews Report for Incentive Compensation; FSB Approves Peer-Review Report on Compensation Practices

In late 2009, the Federal Reserve Board ("Fed") initiated a horizontal review of incentive compensation practices at 28 large, complex banking organizations ("LSBOs"). On October 5, 2011 the Fed released a report, *Incentive Compensation Practices: A Report on the Horizontal Review of Practices at Large Banking Organizations* ("Review Report"), which summarizes its findings from this review. Broadly, the review focused on the range of compensation practices across the firms and the categories of employees affected by these practices. The review also served to guide the LCBOs in their implementation of the *Interagency Guidance on Sound Incentive Compensation Policies* ("Interagency Guidance") published by the Fed and the other bank and thrift regulators (Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation and Office of Thrift Supervision) in June 2010.

The Horizontal Reviews Report concludes that, collectively, the LCBOs subject to the review (25 were ultimately included in the final report) have made significant progress toward enhancing their incentive compensation arrangements to provide "appropriately balanced incentives to take risk and to promote safety and soundness." It also states that most LCBOs still have significant work to do to achieve full compliance with the Interagency Standards.

In a separate but related action, the Financial Stability Board ("FSB") approved, at its October 3 meeting, the report of its follow-up peer review on the implementation of principles and standards for compensation practices. The FSB states that the report finds progress has been made since last year by both national authorities and firms in implementing the FSB's *Principles for Sound Compensation Practices* and the related *Implementation Standards* but more work needs to be done. The report sets out recommendations to address remaining gaps and impediments.

The U.S. regulators' Interagency Guidance incorporates the FSB's Principles and Standards.

For additional information please contact Hugh Kelly, Principal: hckelly@kpmg.com or Jon Greenlee, Managing Director: jgreenlee@kpmg.com

Financial Stability Board Approves Measures In Anticipation of G20 November Meeting

The Financial Stability Board ("FSB") conducted a meeting on October 3 at which it approved a number of proposals to be submitted to the G20 summit in November. These measures included:

- A policy package to address "too big to fail" problems associated with systemically important financial institutions ("SIFIs"), including:
 - A new international standard for the key attributes of effective resolution regimes to enable failing financial institutions to be resolved safely and without exposing taxpayers to the risk of loss.
 - A requirement that individual globally important SIFIs (G-SIFIs) have recovery and resolution plans, informed by resolvability assessments, and that home and host authorities develop institution-specific cooperation agreements and cross-border crisis management groups.
 - Additional loss absorbency requirements for those banks determined to be G-SIFIs, based on the methodology developed by the Basel Committee on Banking Supervision for assessing the global systemic importance of banks.

- Measures to enhance the intensity and effectiveness of supervision of financial institutions, particularly SIFIs, including improved data systems for risk management at SIFIs and assessments of the adequacy of supervisory resources.
- Enhancing international standards for the robustness of core financial market infrastructures.
- Workplans to strengthen the oversight and regulation of shadow banking, including annual monitoring exercises to assess global trends and risks, as well as regulation in the areas of: i) banks' interaction with shadow banking entities; ii) money market funds; iii) other shadow banking entities; iv) securitization; and v) securities lending and repos.
- Approving the conclusions of the second progress report on implementation of OTC derivatives reforms covering standardization, central clearing, exchange or electronic platform trading, and reporting to trade repositories. The progress report, which will be published shortly, clarifies that the reforms to OTC products committed to by the G20, and set out in more detail in the FSB October 2010 report, are to be fully implemented irrespective of whether those products continue to trade OTC or are moved onto organized platforms.
- Approving two reports by IOSCO (International Organization of Securities Commissioners) on principles for the regulation and supervision of commodity derivatives markets, and on regulatory issues raised by the impact of technological changes on market integrity and efficiency.

For additional information please contact Jon Greenlee, Managing Director: jgreenlee@kpmg.com or Paul Cardon, Director: pcardon@kpmg.com

FSB Releases Proposal for a Common Data Template Applicable to SIFIs

The Financial Stability Board ("FSB") released a consultative document on October 6 that outlines requirements for a Common Data Template applicable to global systemically important financial institutions ("G-SIFIs"). The release responds to a 2009 G20 mandate that the FSB improve data collection and sharing among G-SIFIs. In particular, this data requirement related to the linkages between G-SIFIs and their exposure and funding dependencies.

As proposed, the common data template would apply only to global systemically important banks and "aims to address the key gaps identified during the [financial] crisis and to provide the authorities with a stronger framework for assessing potential systemic risks." The template would be completed by the banks, identified by the FSB and the Basel Committee on Banking Supervision in consultation with the national authorities. Parallel work to develop improved data collection for large non-bank financial institutions is ongoing in the areas of insurance, hedge funds and data reporting to trade repositories.

Comments on the template are requested by November 8, 2011.

For additional information please contact [Jon](#) Greenlee, Managing Director: jgreenlee@kpmg.com or Francis Gomez, Manager: fgomez@kpmg.com

Enterprise & Consumer Compliance

Simplifying Checking Account Disclosures

Raj Date, Special Adviser to the Secretary of the Treasury on the Consumer Financial Protection Bureau, released a statement on October 5 that addressed checking account disclosures. In particular, Mr. Date stated that a recent industry survey found three-quarters of the individuals surveyed supported greater clarity and disclosure for checking accounts. Mr. Date stated that the Bureau of Consumer Financial Protection ("CFPB") "has the ability to simplify checking account disclosures." He added that, "Making the costs transparent is good for consumers and good for competition. It allows consumers to compare the checking account options from large banks, community banks, and credit unions and pick the one that works best for them"

For more information, contact Linda Gallagher, Principal: lgallagher@kpmg.com or Kari Greathouse, Director: cgreathouse@kmg.com.

Securities & Investment Management

SEC Releases Report on Review of Nationally Recognized Statistical Rating Organizations

The Securities and Exchange Commission ("SEC") released a report on September 30 that summarizes staff findings following a review of each of the ten nationally recognized statistical rating organizations ("NRSROs"). The reviews were required pursuant to Section 932 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (the "Dodd-Frank Act"), which amended Section 15E of the *Securities Exchange Act of 1934* and imposed new reporting, disclosure and examination requirements to enhance the regulation and oversight of NRSROs.

The reviews, referred to as Section 15E reviews, are required to be conducted annually and the staff note that beginning with next year's report (the second), the report will include a summary of whether the NRSROs have appropriately addressed recommendations in previous reports. Based on the recent review, no "material regulatory deficiencies" were identified though some "notable observations and concerns" are discussed. The staff added that some NRSROs have already taken steps to address some of the concerns raised during the examination process.

For more information, contact Doug Henderson, Managing Director: douglashenderson@kpmg.com or Dan McIsaac, Director: dmcisaac@kpmg.com.

Financial Services Legislative Developments

Senate Committee Approves Nomination of Richard Cordray to Serve as Director of the CFPB

On October 6, the Senate Committee on Banking, Housing and Urban Development approved the nomination of Richard Cordray to serve as the Director of the Bureau of Consumer Financial Protection ("CFPB"). The vote was 12-10 along straight party lines. In opening remarks to the nomination hearing, Senator Shelby, Ranking Member of the Committee, reiterated the GOP position that favors, among other things, replacement of the sole position of the Director with a five-member board.

Mr. Cordray's nomination will now be considered by the full Senate.

For more information, contact Linda Gallagher, Principal: lgallagher@kpmg.com or Amy Matsuo, Principal: amatsuo@kpmg.com.

House Hearing on Annual Report of the Financial Stability Oversight Council

Timothy Geithner, Secretary of the Treasury, was the sole witness at the House Committee on Financial Services' October 6 hearing to consider the Annual Report of the Financial Stability Oversight Council. Secretary Geithner's testimony reviewed the conclusions and recommendations made by the Financial Stability Oversight Council ("Council") in its first annual report to Congress, which was submitted concurrently with the Secretary's testimony.

In particular, Secretary Geithner stated that because of the actions taken to reform the financial system, it is in a "significantly stronger position and better able to withstand the new risks we face in the global economy." He cited:

- The entities that took the most risk no longer exist or have been significantly restructured.
- The firms that survived are better capitalized - large banks have increased common equity by over \$300 billion since the beginning of 2009. The level of common equity to risk weighted assets across these banks is now approximately 10 percent, up from six percent at the beginning of 2009.
- Banks are funding themselves more conservatively and are maintaining much larger cushions of safe and liquid financial assets. Debt maturing in one year or less at the largest institutions, as a share of total liabilities, has declined to roughly 40 percent of the pre-crisis level.
- The major banks have reduced the size and overall risk in their balance sheets, compared to pre-crisis levels.
- The "shadow banking system is much smaller, with assets at roughly half the 2007 level.

The Council recommends:

- Further actions to strengthen the financial position of the core of the U.S. financial institutions, particularly the largest institutions and including heightened standards for capital and liquidity.
- Reforms to strengthen key funding markets, most importantly tri-party repo markets and money market funds.
- Reforms to the housing finance systems, including national standards for the mortgage servicing market,
- Closer cooperation and coordination in the implementation of financial reforms in the U.S. and globally.

Finally, with regard to the global financial reforms, Secretary Geithner noted, “As we act to contain risk in the United States, we want to minimize the chances that it simply moves to other markets around the world, ultimately endangering our own system. The most important challenges we face in building a level playing field lie in the design of new capital standards and liquidity rules for the largest institutions and reforms to the derivatives markets.”

For additional information please contact Hugh Kelly, Principal: hckelly@kpmg.com or Jon Greenlee, Managing Director: jdgreenlee@kpmg.com

Recent Supervisory Actions against Financial Institutions

Last Updated: October 10, 2011

Agency	Institution Type	Action	Date	Synopsis of Action
Federal Reserve Board	Bank Holding Company	Written Agreement	10/04	The Federal Reserve Board entered into a Written Agreement with a Tennessee bank holding company that addressed dividends and distributions and debt and stock redemptions to ensure that it serves as a source of strength for its state nonmember bank and nonbank subsidiaries.
Federal Reserve Board	Bank Holding Company	Written Agreement	09/22	The Federal Reserve Board entered into a Written Agreement with a Texas bank holding company that addressed dividends and distributions and debt and stock redemptions to ensure that it serves as a source of strength for its national bank and nonbank subsidiaries.
Federal Reserve Board	Bank Holding Company	Written Agreement	09/13	The Federal Reserve Board entered into a Written Agreement with a Florida bank holding company that addressed dividends and debt and stock redemptions to ensure that it serves as a source of strength for its state nonmember bank subsidiary.
Federal Reserve Board	Bank Holding Company	Written Agreement	09/08	The Federal Reserve Board entered into a Written Agreement with a Pennsylvania bank holding company that addressed dividends and distributions and debt and stock redemptions to ensure that it serves as a source of strength for its state nonmember bank and nonbank subsidiaries.
Federal Reserve Board	Bank Holding Company	Written Agreement	09/06	The Federal Reserve Board entered into a Written Agreement with a South Carolina-based bank holding company and its subsidiary bank holding companies that addressed dividends, distributions and other payments, capital, affiliate transactions and debt and stock redemptions to ensure that they serve as a source of strength for their state nonmember bank and nonbank subsidiaries
Federal Reserve Board	Bank Holding Company	Written Agreement	09/06	The Federal Reserve Board entered into a Written Agreement with a Minnesota bank holding company that addressed dividends and distributions and debt and stock redemptions to ensure that it serves as a source of strength for its state nonmember bank subsidiary.
Federal Housing Finance Agency	Financial Institutions and Financial Companies	Litigation	09/02	The Federal Housing Finance Agency, as conservator for Fannie Mae and Freddie Mac, filed lawsuits against 17 financial institutions and companies that alleged violations of Federal securities laws and common laws in the sale of private mortgage-backed securities to the government sponsored enterprises. The complaints seek damages and civil penalties.
Federal Reserve Board	Bank Holding Company; State Member Bank	Consent Order	09/01	The Federal Reserve Board entered into a Consent Order with a New York bank holding company and its state member bank subsidiary to address deficiencies related to residential mortgage loan servicing including foreclosure review, third party management, single point of contact, mortgage electronic registration system, management information systems, risk management, risk assessment and audit,

Contact Us

This is a publication of KPMG's Financial Services Regulatory Practice

Linda Gallagher, National Leader, Financial Services Regulatory Practice

Jon Greenlee, Managing Director, Bank Regulatory

Douglas Henderson, Managing Director, Broker-Dealer Regulatory

Hugh Kelly, Principal, Bank Regulatory

Amy Matsuo, Principal, Enterprise & Consumer Compliance

John Schneider, Principal, Investment Management Regulatory

David Sherwood, Director, Insurance Regulatory

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Asset Management, Trust, and Fiduciary

Bill Canellis T: 973.912.4817

Bank Regulatory Reporting

Francis Gomez T: 212.872.5662

Chris Monks T: 617.988.1718

Brett Wright T: 901.249.3809

Broker-Dealer Regulation

Lucia Baraybar T: 212.872.6477

Stefan Cooper T: 856.417.6799

Doug Henderson T: 212.872.6687

Dan McIsaac T: 212.954.5973

Capital/Basel II and III

Bill Canellis T: 973.912.4817

Paul Cardon T: 617.988.1282

Jon Greenlee T: 703.286.8032

Hugh Kelly T: 202.533.5200

Greg Matthews T: 212.954.7784

Commodities and Futures Regulation

Dan McIsaac T: 212.954.5973

Consumer & Enterprise Compliance

Linda Gallagher T: 703.286.8248

Kari Greathouse T: 636.587.2844

Amy Matsuo T: 919.380.1509

Cross-Border Regulation

Jon Greenlee T: 703.286.8032

Hugh Kelly T: 202.533.5200

Craig Stirnweis T: 212.872.5960

Foreign Banking Organizations

Francis Gomez T: 212.872.5662

Hugh Kelly T: 202.533.5200

Craig Stirnweis T: 212.872.5960

Insurance

David Sherwood T: 212.954.5861

Lisa Stimson T: 860.297.6059

Investment Management Regulation

John Schneider T: 617.988.1000

Privacy & Identity Theft

Linda Gallagher T: 703.286.8248

Kari Greathouse T: 636.587.2844

Safety & Soundness, Corporate Licensing & Governance, and ERM Regulation

Paul Cardon T: 617.988.1282

Jon Greenlee T: 703.286.8032

Hugh Kelly T: 202.533.5200

Greg Matthews T: 212.954.7784

Craig Stirnweis T 214.840.6866

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