



## Weekly Newsletter

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# Bank & Thrift

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## Financial Stability Oversight Council Designates Financial Market Utilities as Systemically Important; Fed Affirms Payments Systems Policies and Expectations

On July 18, 2012, the Financial Stability Oversight Council ("Council") approved the designation of eight financial market utilities ("FMUs") as systemically significant under Title VIII of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* ("Dodd-Frank Act"). Such a designation requires these FMUs to be supervised by the Federal Reserve Board ("Fed").

On July 19, 2012, the Fed released a statement reaffirming its long-standing policy of applying relevant international risk-management standards to the Federal Reserve Banks' Fedwire funds and Fedwire securities services. The Fed states these services play a critical role in facilitating the safe and efficient settlement of private-sector FMUs. The Fed stated that its examination framework for Fedwire is consistent with the framework that will be used for FMUs supervised by the Fed pursuant to designation as systemically important by the Council. In addition, the Fed is ensuring that the Reserve Banks are held to procedural requirements with respect to Fed review of proposed material changes to Fedwire rules, procedures, and operations that are the same as, or higher than, the requirements for designated FMUs.

The statement notes that the Fed will be seeking comment on revisions to its *Payments System Risk* ("PSR") policy to take into account the new *Principles for Financial Market Infrastructures* that were issued in April by the Committee on Payment and Settlement Systems and the Technical Committee of the International Organization of Securities Commissions. The PSR policy, among other things, sets forth the Fed's views and risk-management expectations for various payment and settlement systems, including those operated by the Reserve Banks.

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## Treasury Releases First Report of Office of Financial Research

The Department of the Treasury released the first annual report of the Office of Financial Research ("OFR"), which was created within the Treasury by the *Dodd-Frank Wall Street Reform and Consumer Protection Act* to support the Financial Stability Oversight Council and to "collect and standardize financial data, to perform essential research, and to develop new tools for measuring and monitoring risk in the financial system."

The report outlines the OFR's work in four areas: 1) analyzing threats to financial stability; 2) conducting research on financial stability; 3) addressing data gaps; and 4) promoting data standards. Going forward, the OFR expects to "focus on the forces that promote the migration of financial activities, including maturity transformation and the creation of money-like liabilities, into unregulated or lightly regulated markets—the so-called shadow banking

system". It will also "investigate in depth the behavior of short-term funding markets and collect better data on repo markets."

The OFR notes that earlier this year it published its strategic framework and that it will also publish a second annual report later this year on its human resources practices.

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## Enterprise & Consumer Compliance

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### CFPB Finalizes Rule on Supervision of Larger Participants in the Credit Reporting Industry

The Bureau of Consumer Financial Protection ("CFPB" or "Bureau") issued a final rule on July 16, 2012 that outlines its supervision of the larger participants of the credit reporting industry. In particular, beginning September 30, 2012, the CFPB will supervise credit reporting companies that have more than \$7 million in annual receipts from credit reporting activities. The CFPB estimates that approximately 30 companies will be covered by the rule, representing approximately 94 percent of the market revenues.

Coincident with the release of the final rule, CFPB Director Richard Cordray spoke at a CFPB Credit Reporting Field Hearing about the Bureau's newest supervisory role. He said, "Because no federal agency has previously had the kind of broad access to information about the operations of the credit reporting companies that the Bureau will now have, there is much we do not know yet about the true risks that consumers face in this market. As we go forward, we will be gathering data to determine how the various parts of the Consumer Bureau can best act to protect consumers." He explained that the CFPB would initially focus on three areas of concern:

- The accuracy of information received by the credit reporting companies.
- The accuracy of the credit reporting companies in assembling and maintaining that information; and
- The processes that govern error resolution.

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### CFPB Submits Study of Private Student Loan Market to Congress and Lists Recommendations

The Bureau of Consumer Financial Protection ("CFPB") and the U.S. Department of Education jointly submitted a report to Congress summarizing their review of the private student loan market and related consumer protection issues, as required by Section 1077 of the *Dodd-Frank*

*Wall Street Reform and Consumer Protection Act* (the “Dodd-Frank Act”). Key findings highlighted in the report include:

- Over the past ten years, the private student loan market grew from less than \$5 billion in 2001 to more than \$20 billion in 2008 and declined again to less than \$6 billion in 2011.
- During the growth period of 2005 to 2008, private student lender underwriting standards loosened and school financial aid offices were less involved in the lending process.
- Since 2008, underwriting standards have tightened and include features such as co-signers and school certifications regarding student financial need.
- Many borrowers do not fully understand the differences between Federal and private student loans and do not exhaust their Federal borrowing limits before turning to private loans.
- A significant percentage of private student loan borrowers attended for-profit colleges.
- Loan defaults have increased since the 2008 financial crisis.
- Private student lenders are generally heterogeneous, though small programs also exist to target specific sectors.

As required by the Dodd-Frank Act, the study included recommendations to modernize the Federal consumer financial laws, including the following:

- Require lenders to obtain an affirmative certification from the institution of higher education that the loan amount does not exceed the student need.
- Consider modifications to the U.S. Bankruptcy Code that would permit greater flexibility for restructuring payment options.
- Clarify the definition of a private student loan to incorporate products currently in use.
- Explore how to facilitate greater transparency of existing private student loan obligations, similar to the National Student Loan Data System applicable to Federal student loans.
- Determine whether additional data is needed to enhance consumer decision-making and lender underwriting, such as post-graduation outcomes for employment and wages by program of study, to better inform a consumer’s decision regarding which school to attend or continue attending.

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## CFPB Issues First Public Enforcement Action and Related Supervisory Bulletin

The Bureau of Consumer Financial Protection (“CFPB” or “Bureau”) announced its first public enforcement action on July 18, 2012. The action resulted in a Consent Order with a national bank to address marketing practices engaged in by the bank and its vendors that were identified as deceptive by the CFPB. In particular, credit card consumers were said to be pressured or misled into purchasing “add-on products,” such as payment protection and credit monitoring, when activating new credit cards. Without “admitting or denying the findings of fact or conclusions of law,” the bank agreed to the Order, which, among other things, requires total restitution of approximately \$140 million to be paid to approximately 2 million consumers and the payment of a \$25 million civil money penalty.

Also on July 18, the Office of the Comptroller of the Currency (“OCC”) announced a separate but related enforcement action against the same bank for the same identified deficiencies and ordering the bank to repay approximately \$150 million to approximately 2.5 million consumers and to pay a \$35 million civil money penalty. The restitution payments made pursuant to the OCC’s order will serve to satisfy the CFPB’s requirements against the same obligations.

The CFPB also announced the release of Bulletin 2012-06 on the topic of *Marketing Credit Card Add-On Products*. The Bulletin outlines the CFPB's expectations for entities supervised by the CFPB and their service providers regarding the marketing and sales of credit card add-on products in a manner that mitigates the potential for statutory and regulatory violations of Federal consumer financial law and related consumer harm.

In the releasing announcement, CFPB Director Richard Cordray stated "We know these deceptive marketing tactics for credit card add-on products are not unique to a single institution. The compliance bulletin puts all financial institutions on notice about these prohibited practices and reinforces that they must make sure their service providers are complying with the law. We expect announcements about other institutions as our ongoing work continues to unfold. Regardless, the best time for all institutions to be reviewing and ensuring their practices in this area is right now. Consumers deserve to be treated fairly by their credit card issuers, and that is our objective."

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## Capital Markets & Investment Management

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### Enforcement Actions

The Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC") recently announced the following enforcement actions:

- The SEC charged a company and two of its former executive officers with accounting violations that misstated the company's earnings over several years. The company agreed to pay a \$1 million penalty and the officers to pay a total of \$300,000 in disgorgement and penalties.
- The SEC charged the Chairman and CEO of a company with insider trading for making trades based on confidential information.
- The SEC charged the U.S. subsidiary of a foreign firm and three of its former employees with misleading investors related to sales of certain financial assets. The SEC states the firm made approximately \$10 million in structuring and marketing fees on the scheme and the firm has agreed to pay \$127.5 million to settle the SEC's charges.
- The CFTC issued an order settling charges against a firm that exercised discretionary trading authority over customers' accounts in retail, leveraged foreign currency transactions, without being registered with the CFTC as a Commodity Trading Advisor (CTA). The firm agreed to pay a \$140 million penalty.
- The CFTC announced a court judgment against an individual and his companies based on a 2011 CFTC complaint that the defendants were operating an illegal off-exchange foreign currency scheme. The order imposed a \$250,000 civil money penalty and imposed permanent trading and registration bans against the defendants.
- The CFTC announced a court judgment against an individual and his companies in connection with a commodity pool Ponzi scheme in which the defendants defrauded over

100 participants in the United States and Canada of over \$14 million. The Order imposes permanent trading and registration bans against the defendants and requires them jointly and severally to pay restitution of over \$9.5 million to defrauded pool participants and a \$31.8 million civil monetary penalty.

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## Financial Service Legislation

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### President Obama Signs Law Reauthorizing the National Flood Insurance Program; House Passes Law Aimed at Frivolous ATM Lawsuits

On July 6, 2012, President Obama signed the *Biggert-Water Flood Insurance Reform and Modernization Act of 2012* into law. The law reauthorizes the National Flood Insurance Program ("NFIP") through September 30, 2017 and makes several other reforms to the NFIP.

On July 9, 2012, the House of Representatives passed H.R. 4367, which is intended to stop frivolous lawsuits over missing transaction fee notices at ATMs. ATMs are currently required to provide such notices on both the outside of the machine and also on the transaction screen. The legislation would continue to require ATMs to maintain the on-screen notice about transaction fees and provide consumers the opportunity to decline those fees and terminate the transaction but remove the redundant exterior notice requirement.

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## Recent Supervisory Actions against Financial Institutions

Last Updated: July 23, 2012

Agency	Institution Type	Action	Date	Synopsis of Action
Bureau of Consumer Financial Protection; Office of the Comptroller of the Currency	National Bank	Civil Money Penalty	06/18	<p>The Bureau of Consumer Financial Protection entered into a Consent Order with a national bank to address deficiencies related to marketing practices engaged in by the bank and its vendors and which the CFPB determined to be deceptive . The CFPB required \$140 million in restitution to be paid to approximately 2 million consumers and a civil money penalty of \$25 million.</p> <p>In a separate but related action, the Office of the Comptroller of the Currency entered into a Consent Cease and Desist Order with the bank. The OCC required \$150 million in restitution to be paid to approximately 2.5 million consumers and a civil money penalty of \$35 million.</p> <p>The CFPB’s restitution payments may be satisfied with the restitution payments required by the OCC.</p>
Federal Reserve Board	Bank Holding Company	Written Agreement	07/05	The Federal Reserve Board entered into a Written Agreement with an Indiana-based bank holding company to address dividends and distributions, debt and stock redemptions, capital and affiliate transactions to ensure that it serves as a source of strength for its national bank and Federal savings bank subsidiaries in addition to its various nonbank subsidiaries.
Federal Reserve Board	Bank Holding Company	Written Agreement	07/03	The Federal Reserve Board entered into a Written Agreement with a Maryland-based bank holding company to address 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	06/28	The Federal Reserve Board entered into a Written Agreement with a Virginia-based bank holding company to address dividends and distributions, debt and stock redemptions, capital and affiliate transactions 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	06/26	The Federal Reserve Board entered into a Written Agreement with a Minnesota-based bank holding company to address dividends, distributions and other payments, 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	06/26	The Federal Reserve Board entered into a Written Agreement with a Delaware-based bank holding company to address dividends as well as 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	06/21	The Federal Reserve Board entered into a Written Agreement with an Arkansas-based bank holding company to address 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.

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