



Weekly Newsletter

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Bank & Thrift

Agencies Publish Regulatory Capital Estimation Tool for Basel III

The Federal banking regulatory agencies (the Federal Reserve Board, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation) jointly announced the availability of a regulatory capital estimation tool to help community banking organizations and other interested parties evaluate the agencies' Basel III regulatory capital proposals published jointly in June 2012. The tool is intended to assist these organizations in estimating the potential effects of the Basel III Notice of Proposed Rulemaking ("NPR") and Standardized Approach NPR on their capital ratios.

The Basel III proposals would revise the agencies' current regulatory capital standards (comments are requested no later than October 22, 2012). The Basel III NPR focuses primarily on strengthening the level of regulatory capital requirements and improving the quality of capital. The Standardized Approach NPR proposes a number of enhancements to the risk-sensitivity of the agencies' capital standards. The tool is intended to help institutions estimate the potential effect the proposals could have on their capital ratios but the agencies caution it should not be relied on as an indicator of an institution's actual regulatory capital ratios and it is not part of the NPRs nor of any final rule(s) that the agencies may adopt. One tool is available for banks and savings associations and a second is available for bank and savings and loan holding companies.

Joint Forum Finalizes Updates to Principles for the Supervision of Financial Conglomerates

On September 24, 2012, the Joint Forum issued a final report on *Principles for the Supervision of Financial Conglomerates*, which supersedes its compendium of principles on this topic developed in 1999.

The Joint Forum describes the updated principles as "a broader and more consolidated set of internationally agreed principles." They include guidance for policymakers on the powers and authorities necessary for supervisors of financial conglomerates, as well as guidance for supervisors on the governance, capital adequacy and liquidity, and risk management frameworks of financial conglomerates. As updated, the principles are structured in a manner that is expected to facilitate their implementation across jurisdictions and over time.

The Joint Forum was established in 1996 under the aegis of the Basel Committee on Banking Supervision, the International Organization of Securities Commissions ("IOSCO") and the International Association of Insurance Supervisors ("IAIS") to deal with issues common to the banking, securities and insurance sectors, including the regulation of financial conglomerates.

Fed Begins Publication of Transaction Level Information for Discount Window Lending

On September 28, 2012, the Federal Reserve Board ("Fed") began the quarterly publication of transaction-level information related to discount window lending to depository institutions and open market transactions. The data in this initial release covers transactions between July 22, 2010 and September 30, 2010, consistent with provisions of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*, which require that transaction-level details for discount window loans and open market transactions to be made available on a quarterly basis and with an approximately two-year lag. The transaction-level detail supplements the aggregate information the Fed has previously provided in weekly, monthly, and quarterly reports.

Data on discount window loans include the name of the borrowing institution, the amount borrowed, the interest rate charged, and information about collateral pledged.

Data on open market transactions includes temporary and permanent purchases and sales of Treasury and Agency securities, securities lending activities, and foreign exchange transactions and foreign currency reserve investments. Information on each transaction includes the identity of the counterparty, the security or currency purchased or sold, and the date, amount, and price of the transaction.

OCC Issues "Refinements" to Guidance on Examiner Consideration of BSA/AML Findings for UFRS, RAS and ROCA

The Office of the Comptroller of the Currency ("OCC") released Bulletin 2012-30 on September 28, 2012 to summarize "refinements" the OCC has made to how examiners will consider *Bank Secrecy Act*/Anti-Money Laundering ("BSA/AML") examination findings for purposes of:

- The Federal Financial Institutions Examination Council's ("FFIEC") Uniform Rating Systems and the OCC's risk assessment system ("RAS") for national banks and Federal savings associations (collectively, "banks"); and
- The ROCA (i.e., Risk management, Operational controls, Compliance, and Asset quality) ratings and RAS for Federal branches and agencies of foreign banking organizations.

The OCC has incorporated these refinements into interim updates of the "*Bank Supervision Process*," "*Large Bank Supervision*," and "*Community Bank Supervision*" booklets of the *Comptroller's Handbook*. Examination procedures used to evaluate the adequacy of a bank's BSA/AML compliance remain unchanged and can be found in the FFIEC *Bank Secrecy Act/Anti-Money Laundering Examination Manual*.

Highlights of the revisions include the following:

- Effective July 18, 2012, examiners no longer consider BSA/AML examination findings when assigning a rating under the FFIEC Uniform Interagency Consumer Compliance Rating System.
- Serious deficiencies in a bank's BSA/AML compliance create a presumption that the bank's management component rating will be adversely affected because its risk management practices are less than satisfactory.
- Serious deficiencies in a branch's or agency's BSA/AML compliance create a presumption that the branch's or agency's risk management component rating will be adversely affected because its risk management practices are less than satisfactory. Examiners also

continue to consider BSA/AML examination findings when assigning the compliance component rating of ROCA.

- BSA/AML findings are still considered when assessing compliance risk under the OCC's RAS. Compliance risk reflects a bank's compliance with all applicable laws and regulations. The overall quantity of risk and quality of risk management related to BSA/AML compliance, as well as the four pillars of a bank's BSA/AML program, are considered in assessments of compliance risk. BSA/AML examination findings should also continue to be reflected in assessments of reputation, strategic, and operational risks, as warranted.

Enterprise & Consumer Compliance

CFPB Completes Comparison Study of Credit Scores Sold to Creditors and Consumers

The Bureau of Consumer Financial Protection ("CFPB" or "Bureau") released a study on September 25, 2012 that compares the credit scores sold to creditors with those sold to consumers. The study was required by Section 1078 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*, and finds that:

- A majority of consumer scores produced by different scoring models provide similar information about the relative creditworthiness of a consumer.
- Correlations across the results of scoring models were high (approximately .90).
- Given four credit-quality categories, different scoring models would place consumers in the same credit-quality category 73 to 80 percent of the time. Different models would place consumers in credit-quality categories that are off by one category 19 to 24 percent of the time and from 1 to 3 percent of consumers would be placed in categories that were two or more categories apart.
- Different scoring models did not appear to treat different groups of consumers systematically differently than other scoring models.
- There is no way for consumers to know how the score they purchase will compare to the score a creditor purchases to use in making a lending decision. Consumers cannot exclusively rely on the credit score they receive to understand how lenders will view their creditworthiness.
- Firms that sell scores to consumers should make consumers aware that the scores consumers purchase could vary, sometimes substantially, from the scores used by creditors.

The CFPB notes that it will begin oversight of consumer credit reporting agencies on September 30, 2012. The Bureau's examiners will be looking to verify that consumer reporting companies are complying with Federal consumer financial law, including that the companies are using and providing accurate information, handling consumer disputes, making disclosures available, and preventing fraud and identity theft.

FDIC Implements Three Tier System for Violations Identified in Compliance Examinations

The Federal Deposit Insurance Corporation ("FDIC") published Financial Institution Letter 41-2012 on September 25, 2012 to announce that the FDIC Division of Depositor and Consumer Protection has revised the classification system for citing violations identified during compliance examinations. The new system will be used in examinations started on or after October 1, 2012.

Under the new system, violations identified during a Compliance Examination will be assigned to one of three levels based primarily on the impact to consumers:

- Level 3/High Severity violations include violations that may result in restitution to consumers in excess of \$10,000 and pattern and practice violations of anti-discrimination laws.
- Level 2/Medium Severity violations include violations resulting in potential restitution to consumers in an amount below the Level 3 threshold and other systemic or recurring violations.
- Level 1/Low Severity violations involve isolated or sporadic violations. Level 1 violations that are adequately addressed during the examination and that do not indicate weakness in the compliance management system. These addressed violations will not be included in the Report of Examination.

The FDIC states that the new classification system and its presentation in the Report of Examination is intended "to address concerns raised by the industry in post-examination surveys and during regulatory outreach events about the focus and portrayal of violations within the context of the examination findings."

CFPB Reminds Industry of Its Civil Investigative Demand Authorities

The Bureau of Consumer Financial Protection ("CFPB") released a blog post on September 21, 2012 to remind the industry that the CFPB Office of Enforcement is permitted to issue Civil Investigative Demands ("CID") to individuals and institutions that may have materials relevant to an investigation. A recipient of a CID may challenge the CID by petitioning the CFPB Director, who can respond by 1) affirming the CID request, 2) modifying the CID, or 3) setting the CID aside. Any challenge to a CID along with the Director's response is generally considered a matter of public record and will be posted on the CFPB's Web site.

CFPB to Take Actions Related to Electronic Funds Transfer Rule

The Bureau of Consumer Financial Protection ("CFPB") released a blog post on September 26, 2012 to announce that it would be taking a number of actions to help the industry understand and comply with the requirements of its new electronic funds transfer rule, which goes into effect on February 7, 2013. In particular, the CFPB will:

- Release of a safe harbor list of countries and other areas that qualify for an exception to the rule, which permits estimated disclosure of certain figures in lieu of disclosure of exact amounts when the laws of the recipient country do not permit determination of the exact amounts.
 - The safe harbor list currently includes: Aruba, Brazil, China, Ethiopia and Libya.
 - Additions to the list on or after February 7, 2013 will be effective immediately, though no deletions will be made prior to May 1, 2013.
- Release a small business compliance guide (due out "in the coming weeks.")

- Conduct a Webinar on October 16 to provide an overview of the rule and opportunity for compliance questions. The CFPB expects the Webinar would benefit a variety of participants in the international money transfer business, including money transmitters, banks, credit unions, foreign banks, other companies that send money abroad for consumers, organizations that work with or represent consumers who send money abroad, agents and software providers.

Capital Markets & Investment Management

Agencies Reopen Comment Period for Proposed Swap Margin and Capital Requirements

On September 26, 2012, five Federal agencies reopened the comment period on a proposed rule to establish margin and capital requirements for swap dealers, major swap participants, security-based swap dealers, and major security-based swap participants as required by Sections 731 and 764 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*. The comment period, which originally ended July 11, 2011, was reopened until November 26, 2012, to allow interested persons additional time to analyze the issues and prepare their comments in light of the consultative document on margin requirements for non-centrally-cleared derivatives, which was published for comment jointly by the Basel Committee on Banking Supervision and the International Organization of Securities Commissions in July 2012.

The five Federal agencies include: the Federal Reserve Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Farm Credit System and the Federal Housing Finance Agency.

SEC's OCIE Issues Staff Report on Broker-Dealer Safeguards for Confidential Information

The Securities and Exchange Commission ("SEC") issued a staff report on September 27, 2012 that is intended to help broker-dealers safeguard confidential information from misuse, such as insider trading. The report, which was prepared by the SEC's Office of Compliance Inspections and Examinations ("OCIE"), describes strengths and weaknesses, identified through examinations, of practices broker-dealers use to keep material nonpublic information from being misused.

The SEC quotes OCIE Director Carlo di Florio as saying, "The report illustrates the types of conflicts of interest that may arise between a broker-dealer's obligations to clients that provide confidential information for business purposes and the potential misuse of such information for insider trading or other improper ends. It also describes various methods that broker-dealers use to identify and effectively manage such conflicts, including information barriers that limit the flow of sensitive information."

The SEC suggests that the types of issues identified in this report may be helpful to firms as they review their conflict of interest risk management programs. In particular, broker-dealers should be alert to changes in business practices and available compliance tools with regard to any review of information barriers control programs,

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 former chief financial officer of a company with diverting company funds to unauthorized personal uses and other uses lacking legitimate business purposes.
- The SEC charged a former investment bank analyst with insider trading for tipping a friend with nonpublic information.
- The SEC charged an investment bank and one of its former investment bankers with "pay to play" violations involving undisclosed campaign contributions. The SEC settled the charges with the investment bank including more than \$7.5 million in disgorgement, \$670,000 in prejudgment interest, and \$3.75 million penalty, which it states is the largest ever settlement imposed by the SEC for Municipal Securities Rulemaking Board pay-to-play violations. The case also marks the first SEC enforcement action for pay-to-play violations involving "in-kind" non-cash contributions to a political campaign.
- The SEC charged three former bank executives with misrepresenting a bank's financial condition and misleading investors and Federal regulators during the financial crisis. Two of the bankers were also charged with insider trading.
- The SEC charged a brokerage firm and three executives for allowing traders outside the U.S. to access the markets and conduct manipulative trading through accounts the firm controlled as part of an illegal practice known as "laying." The settlement involved the payment of disgorgement, interest and penalties.
- The SEC charged a firm with violations of the *Foreign Corrupt Practices Act* for making illicit payments to foreign officials in more than a dozen countries.
- The CFTC obtained a court order requiring an individual to pay a civil monetary penalty of \$598,000 and disgorgement of \$598,000 for aiding and abetting the willful concealment of material facts and the making of false statements to the National Futures Association, violating a previous CFTC order, and acting as an unregistered Commodity Trading Advisor. The order also imposes permanent trading and registration bans against the individual.
- The CFTC filed a civil complaint against an individual and his company for soliciting and obtaining at least \$1.8 million from approximately 30 participants and acted as Commodity Pool Operators without being registered as such or exempt from CFTC registration.
- The CFTC filed a civil action against a registered independent introducing broker and its senior executive officer for making false statements to, and concealing material facts from, the National Futures Association and failing to meet minimum financial requirements for an independent introducing broker.
- The CFTC obtained a judgment for \$5.5 million in restitution and civil money penalties against an individual and his company to settle an action charging the defendants with operating a Ponzi scheme involving foreign currency managed accounts and/or pooled investments.
- The CFTC announced the filing and settlement of several and separate charges made against multiple companies for exceeding speculative position limits in certain commodity futures. Each of the companies agreed to pay civil money penalties.

Recent Supervisory Actions against Financial Institutions

Last Updated: October 1, 2012

Agency	Institution Type	Action	Date	Synopsis of Action
Federal Reserve Board	Bank Holding Company	Written Agreement	09/25	The Federal Reserve Board entered into a Written Agreement with a Minnesota-based bank holding company to address dividends, distributions and other payments, debt and stock redemptions and capital to ensure it serves as a source of strength for its state nonmember bank and nonbank subsidiaries.
Bureau of Consumer Financial Protection; Federal Deposit Insurance Corporation	State Nonmember Bank	Civil Money Penalty	09/24	The Bureau of Consumer Financial Protection and the Federal Deposit Insurance Corporation entered into a Joint Consent Order for Restitution and Order to Pay Civil Money Penalty with a Delaware-based state nonmember bank to address deficiencies related to marketing practices engaged in by the bank which the agencies found to be misleading and deceptive. The agencies required \$200 million in restitution to be paid to approximately 3.5 million consumers and a civil money penalty of \$14 million.
Federal Reserve Board	State Member Bank	Written Agreement	09/13	The Federal Reserve Board entered into a Written Agreement with an Illinois-based state member bank to address deficiencies related to board oversight, corporate governance and management review, credit risk management, lending and credit administration, loan review, asset improvement, capital, liquidity and funds management, interest rate risk management, and dividends.
Federal Reserve Board	Bank Holding Company	Written Agreement	09/13	The Federal Reserve Board entered into a Written Agreement with a Puerto Rican-based bank holding company to address deficiencies related to management review, credit risk management, credit administration, loan grading, asset improvement, other real estate owned, allowance for loan and lease losses, accounting and internal controls, internal audit, dividends, debt and stock redemptions and capital to ensure it serves as a source of strength for its state member bank and nonbank subsidiaries.
Federal Reserve Board	Bank Holding Company	Written Agreement	08/30	The Federal Reserve Board entered into a Written Agreement with a California-based bank holding company to address dividends and distributions and debt and stock redemptions to ensure they serve as a source of strength for its national bank subsidiary.
Federal Reserve Board	Bank Holding Company	Written Agreement	08/16	The Federal Reserve Board entered into a Written Agreement with four related Connecticut-based bank holding companies to address dividends and distributions, debt and stock redemptions and capital to ensure they serve as a source of strength for their national bank and nonbank subsidiaries.
Federal Deposit Insurance Corporation	State Nonmember Bank; Institution Affiliated Party	Consent Order; Civil Money Penalties	08/08	The Federal Deposit Insurance Corporation entered into a Consent Order and Order to Pay Restitution and Order to Pay Civil Money with a state nonmember bank and its institution-affiliated party to address FDIC findings of unfair and deceptive acts and practices related to a student loan debit card program. The bank agreed to restitution of \$11 million and both parties combined will pay civil money penalties of more than \$280,000.

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