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# The Washington Report

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## In This Issue

# Bank & Thrift

## Federal Reserve Approves Capital Plans of 14 Institutions in the CCAR

On March 14, 2013, the Federal Reserve Board (Federal Reserve) announced that it has approved the capital plans of 14 financial institutions in the Comprehensive Capital Analysis and Review (CCAR). Two other institutions received conditional approval, while the Federal Reserve objected to the plans of two firms.

In the CCAR, the Federal Reserve evaluates the capital planning processes and capital adequacy of the largest bank holding companies, including the firms' proposed capital actions such as dividend payments and share buybacks and issuances. When considering an institution's capital plan, the Federal Reserve considers both qualitative and quantitative factors, including the firm's capital ratios under severe economic and financial market stress, the strength of the firm's capital planning process, and the institution's plans to meet new Basel 3 capital requirements as they would be implemented in the United States. After the Federal Reserve objects to a capital plan, the institution may only make capital distributions with prior written approval from the Federal Reserve.

## Federal Reserve Determines Not to Propose Changes to Interchange Fees

The Federal Reserve Board (Federal Reserve) published a report on March 5, 2013 that summarizes information on debit card transactions in 2011, including information on volume and value, interchange fee revenue, certain debit card issuer costs, and fraud losses. The report is the second in a series to be published every two years pursuant to section 920 of the *Electronic Fund Transfer Act* (EFTA).

The Federal Reserve's Regulation II (*Debit Card Interchange Fees and Routing*), which implements this provision of the EFTA, provides that a debit card issuer subject to the interchange fee standard (a covered issuer) may not receive an interchange fee that exceeds 21 cents plus 5 basis points multiplied by the value of the transaction, plus a 1-cent fraud-prevention adjustment, if eligible. The regulation does not apply to debit card issuers with consolidated assets of less than $10 billion, certain government-administered debit cards, and certain prepaid cards. The interchange fee standard became effective on October 1, 2011.

The report found that covered issuers' costs of authorizing, clearing, and settling (ACS) debit card transactions, excluding fraud losses, varied greatly across respondents and that the;

- Median issuer had an average ACS cost of 11 cents;
- Issuer at the 75th percentile had an average ACS cost of 36 cents;
- Issuers with the highest debit card transaction volume had an overall average cost of 5 cents per transaction; and
- Issuers with the smallest debit card programs generally had the highest ACS costs per transaction.

The Federal Reserve estimated debit-card fraud losses for all parties (merchants, cardholders, and issuers) totaled $1.38 billion in 2011, with an average loss of approximately 8 basis points per debit card transaction. The median covered issuer's average fraud loss per transaction was nearly 5 basis points, as well as average fraud prevention and data security costs of slightly less than 1.5 cents per transaction.

The Federal Reserve states that, based on the report results, it does not plan to propose revisions to the Regulation II interchange fee standard or the fraud-prevention adjustment, adding that sixty-seven percent of covered issuers had average ACS costs below 21 cents (the base component of the interchange fee standard) and these issuers processed well over 99 percent of all reported covered transactions.

### OCC Releases Guidance for Required Electronic Disclosures Related to Short-Term Collective Investment Funds

The Office of the Comptroller of the Currency (OCC) released Bulletin 2013-8 on March 5, 2013, to provide guidance to national banks and Federal branches of foreign banks (collectively, banks), as well as certain Federal savings associations (FSAs), on the process for making electronic disclosures to the OCC. The guidance is related to a final rule published in October 2012 that revised the requirements imposed on banks that offer short-term collective investment funds (STIF).

Under the final rule, a bank managing a STIF is required to disclose information about the fund and its portfolio holdings to the OCC within five business days after the end of each month. To facilitate this reporting requirement, the OCC has established a secure file transfer protocol (FTP) Web site and created a standardized data collection template. Banks and FSAs that offer STIFs must request access to the FTP site and are encouraged to visit the OCC's Asset Management STIF Web site for registration information. The site also contains the data collection template and line-by-line template instructions.

Banks and FSAs are required to comply with the STIF final rule, including the monthly STIF disclosure requirement, beginning July 1, 2013, with the first monthly disclosures due to the OCC by August 7, 2013.

## Enterprise & Consumer Compliance

### CFPB Proposes Rule to Define Larger Participants of Student Loan Servicing Market for Supervision

The Consumer Financial Protection Bureau (CFPB or Bureau) released a proposed rule on March 14, 2013 that would amend the regulations defining larger participants of certain consumer financial product and service markets to add a new section defining larger participants of a market for student loan servicing. Under the rule, any nonbank student loan

servicer that handles more than 1 million borrower accounts would be subject to CFPB supervisory authority. The Bureau estimates that this account threshold would provide the CFPB with authority to supervise the seven largest student loan servicers who, combined, service the loans of 49 million borrower accounts, representing "most" of the activity in the student loan servicing market.

The proposed rule would cover servicing of both Federal and private student loans. The CFPB will continue to coordinate closely with the U.S. Department of Education, which conducts reviews of companies handling loans in accordance with the Federal student aid program.

Comments will be requested for a period of 60 days following publication in the *Federal Register*. The CFPB "is considering a final rule within the coming year."

# Regulatory Reporting

## FDIC Guidance Outlines Proposed Revisions to June 30 Call Report

The Federal Deposit Insurance Corporation (FDIC) released Financial Institution Letter 9-2013 on March 12, 2013 to announce that several proposed revisions to the Consolidated Reports of Condition and Income (Call Report) have been approved by the Federal Financial Institutions Examination Council (FFIEC).

Call Report revisions proposed for the June 30, 2013 reporting period would include new and revised items for:

- Consumer deposit account balances, which would be reported by institutions with total assets of $1 billion or more that offer deposit account products intended for use solely by consumers;
- Certain types of service charges on consumer deposit accounts, which would be reported by all institutions that offer such deposit account products;
- Types of international remittance transfers offered, the settlement systems used, and the applicability of the Consumer Financial Protection Bureau's safe harbor and, for institutions not qualifying for the safe harbor, the number and amount of international remittance transfers;
- Trade names an institution uses to identify physical branches and public-facing Internet Web sites that differ from the institution's legal title;
- Certain higher-risk loans, foreign office real estate loans and commitments, and U.S. government-guaranteed assets plus a new table of consumer loans by loan type and probability of default, which would be completed by large institutions and highly complex institutions (generally, institutions with $10 billion or more in total assets); and
- Certain capital transactions with stockholders.

Call Report revisions proposed for the December 31, 2013 reporting period would require institutions whose parent holding company is not a bank or savings and loan holding company would report the parent company's total consolidated liabilities annually beginning December 31, 2013.

Comments are requested by April 22, 2013.

# Capital Markets & Investment Management

## SEC Proposes New Rules, Regulation SCI, to Address Systems Compliance and Integrity

The Securities and Exchange Commission (SEC) proposed new rules to require certain key market participants to have comprehensive policies and procedures in place surrounding their technological systems. The SEC's proposal, Regulation Systems Compliance and Integrity (Regulation SCI), would replace the agency's current voluntary compliance program with enforceable rules intended to better insulate the markets from vulnerabilities posed by systems technology issues.

Under the proposed rule, self-regulatory organizations, certain alternative trading systems, plan processors, and certain exempt clearing agencies would be required to carefully design, develop, test, maintain, and surveil systems that are integral to their operations. The proposed rules would require them to ensure their core technology meets certain standards, conduct business continuity testing, and provide certain notifications in the event of systems disruptions and other events.

A comment period of 60 days will be available following publication in the *Federal Register*.

## SEC Issues Risk Alert and Investor Bulletin on Adviser Custody of Investor Assets

On March 4, 2013, the Securities and Exchange Commission (SEC) released a Risk Alert and an Investor Bulletin that address Adviser custody of investment assets.

The Alert is based on a review of recent examinations conducted by the SEC's Office of Compliance Inspections and Examination (OCIE), which the SEC's says identified custody-related deficiencies in approximately one-third of firms examined. These deficiencies related to failure to comply with the SEC's custody rule for investment advisers and included failures to:

- Recognize situations where the adviser has custody, such as situations where the adviser:
  - Serves as trustee,
  - Is authorized to write or sign checks for clients, or
  - Is authorized to make withdrawals from a client's account as part of bill-paying services.
- Meet the custody rule's surprise examination requirements.
- Satisfy the custody rule's qualified custodian requirements, such as by:
  - Commingling client, proprietary, and employee assets in a single account, or

- Lacking a reasonable basis to believe that a qualified custodian is sending quarterly account statements to the client.
- Achieve compliance with audit approach requirements.

The Alert notes that the recent findings of custody deficiencies have resulted in a range of actions. These included remedial measures by advisers, such as drafting, amending or enhancing their written compliance procedures, policies or processes, changing their business practices, or devoting more resources or attention to custody issues. OCIE's National Exam Program also has made referrals to the SEC's Division of Enforcement where appropriate.

The SEC's Office of Investor Education and Advocacy (OIEA) released a companion Investor Bulletin that describes the requirements of the custody rule, including a note that it is not a substitute for investors' own oversight and monitoring of their investments.

## CFTC Announces the Commencement of Mandatory Clearing

The Commodity Futures Trading Commission (CFTC) announced that as of March 11, 2013, swap dealers and private funds active in the swaps market began mandatory clearing of certain credit default swaps (CDS) and interest rate swaps that they entered into on or after March 11, 2013. The clearing requirement applies to newly executed swaps, as well as to changes in the ownership of a swap. Five swap classes are required to be cleared including those meeting certain specifications in the categories of fixed-to-floating swaps, basic swaps, forward rate agreements, overnight index swaps, and North American untranched CDS indices. Accounts managed by third party investment managers, as well as ERISA pension plans, have until September 9, 2013, to begin clearing swaps entered into on or after that date. All other financial entities are required to clear swaps beginning on June 10, 2013, for swaps entered into on or after that date. Market participants electing an exception from mandatory clearing do not have to comply with the reporting requirements for electing the exception until September 9, 2013.

## Enforcement Actions

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

- The SEC announced that a hedge fund advisory firm had agreed to pay $14 million to settle charges that the firm engaged in insider trading based on nonpublic information obtained by one of its analysts.
- The SEC announced that a hedge fund advisory firm had agreed to pay more than $600 million in disgorgement, prejudgment interest and penalties to settle charges that it participated in an insider trading scheme.
- The SEC charged a group of foreign- and US-based stock promoters, attorneys, broker-dealers and others with fraud for their participation in an international "pump and dump" scheme involving two US companies.
- The SEC charged two investment advisers with misleading investors about the valuation policies and performance of a private equity fund they managed. Their firm agreed to pay more than $2.8 million to settle the charges and the SEC announced that further penalties were pending against the firm.
- The SEC charged a State with securities fraud for misleading municipal bond investors about the State's approach to funding its pension obligations. The State agreed to the SEC's cease and desist order without admitting or denying guilt.

- The SEC announced charges against a private equity firm, a former senior executive and an unregistered broker for violating securities laws when soliciting capital commitments for private funds managed by the firm.
- The CFTC announced that it had received Federal court orders for more than $3.5 million in restitution and civil money penalties against an individual and his companies who were charged with commodity pool and managed account fraud.
- The CFTC filed charges against an individual and his company alleging the defendants orchestrated a fraudulent scheme to trade off-exchange foreign currency.

# Financial Services Legislation

## GAO Report Indicates Additional Effort Needed to Strengthen Financial Stability Oversight Council and Office of Financial Research

Nicole Clowers, Director of Financial Markets and Community Investment for the General Accountability Office (GAO) provided testimony before the House Committee on Financial Services' Subcommittee on Oversight and Investigations on March 14, 2013 on the topic of Financial Stability. Her testimony generally summarized the findings of a September 2012 GAO report on the Financial Stability Oversight Council (Council) and the Office of Financial Research (OFR), which was updated in March 2013 based on interviews with Department of Treasury and OFR officials. Ms. Clowers indicated that the Council and OFR still have work to do to address the GAO's September 2012 recommendations and to strengthen their efforts to meet the statutory requirements for identifying systemic risks and systemically important entities as well as emerging risk. The GAO's recommendations included, among others:

- Developing a systematic approach to help identify potential threats to financial stability that includes collecting and sharing key financial risk indicators;
- Developing more systematic approaches that are forward-looking and help to prioritize threats to the financial system in its annual reports.
- Improving transparency by keeping detailed records of closed-door sessions at the Council, and developing a communication strategy for both the Council and OFR to improve communications with the public.
- Suggestions the Council develop policies to clarify when formal collaboration or coordination should occur, more fully incorporate key practices for successful collaboration, and clarify with OFR responsibility for implementing requirements to monitor risks to the financial system.
- Developing a comprehensive framework for the Council to assess the impact of its designation decisions.

## Recent Supervisory Actions against Financial Institutions

Last Updated: March 18, 2013

| Agency | Institution Type | Action | Date | Synopsis of Action |
|---|---|---|---|---|
| Federal Reserve Board | Savings and Loan Holding Company | Written Agreement | 02/12 | The Federal Reserve Board entered into a Written Agreement with an Alabama-based bank holding company to address dividends and distributions and debt and stock redemptions to ensure it serves as a source of strength for its Federal savings bank and nonbank subsidiaries. |
| Federal Reserve Board | Bank Holding Company | Written Agreement | 02/07 | The Federal Reserve Board entered into a Written Agreement with a Montana-based bank holding company to address dividends and distributions and debt and stock redemptions to ensure it serves as a source of strength for its national bank and nonbank subsidiaries. |
| Office of the Comptroller of the Currency | National Bank | Civil Money Penalty | 01/25 | The Office of the Comptroller of the Currency assessed a $10 million civil money penalty against a South Dakota-based national bank to address violations of the Bank Secrecy Act. |
| Federal Reserve Board | Bank Holding Company | Written Agreement | 01/22 | The Federal Reserve Board entered into a Written Agreement with a Montana-based bank holding company to address dividends and distributions and debt and stock redemptions to ensure it serves as a source of strength for its state nonmember bank subsidiary. |
| Federal Reserve Board | State Member Bank | Civil Money Penalty | 01/17 | The Federal Reserve Board assessed civil money penalties against an Ohio-based state member bank for violations of the National Flood Insurance Act. |
| Federal Reserve Board; Office of the Comptroller of the Currency | Bank Holding Company; National Bank | Civil Money Penalty | 12/11 | The Federal Reserve Board and the Office of the Comptroller of the Currency assessed civil money penalties against a bank holding company and its national bank, respectively, to address unsafe and unsound practices related to insufficient compliance with Bank Secrecy Act and anti-money laundering requirements. The combined penalties totaled $565 million, which the agencies states is reflective of the severity of the issues identified. In combination with other U.S. agency actions, the entities have agreed to more than $1.9 billion in forfeitures and civil money penalties associated with money laundering and sanctions violations. |
| Federal Reserve Board | Foreign Bank and Branch | Cease and Desist Order; Civil Money Penalty | 12/10 | The Federal Reserve Board entered into a consent order to cease and desist and a civil money penalty assessment of $100 million with a foreign bank and its U.S. branch. The orders address unsafe and unsound practices related to inadequate and incomplete responses to examiner inquiries as well as insufficient oversight of its compliance program for U.S. economic sanctions, Bank Secrecy Act, and anti-money-laundering requirements. |
| Federal Reserve Board | S&L Holding Company | Written Agreement | 12/04 | The Federal Reserve Board entered into a Written Agreement with a Missouri-based savings and loan holding company to address dividends and distributions and debt and stock redemptions to ensure it serves as a source of strength for its Federal savings association and other nonbank subsidiaries. |

## Contact Us

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


Douglas Henderson, Managing Director, Capital Markets Regulatory

Hugh Kelly, Principal, Bank Regulatory

Amy Matsuo, Principal, Enterprise & Consumer Compliance

John Schneider, Partner, Investment Management Regulatory

David Sherwood, Director, Insurance Regulatory


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## Additional Contacts


**Asset Management, Trust, and Fiduciary**
Bill Canellis T: 973.912.4817

**Bank Regulatory Reporting**
Francis Gomez T: 212.872.5662

**Capital Markets Regulation**
Stefan Cooper T: 856.417.6799

**Capital/Basel II and III**
Paul Cardon T: 617.988.1282

**Commodities and Futures Regulation**
Dan McIsaac T: 212.954.5973

**Consumer & Enterprise Compliance**
Kari Greathouse T: 636.587.2844

**Cross-Border Regulation & Foreign Banking Organizations**
Philip Aquilino T: 703-286-8029

**Insurance**
Solomon Abuliak T: 212.954.7709

**Safety & Soundness, Corporate Licensing & Governance, and ERM Regulation**
Greg Matthews T: 212.954.7784