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Safety & Soundness

Basel Committee Releases Proposed Supervisory Guidelines for Identifying and Dealing with Weak Banks

The Bank for International Settlements' (BIS) Basel Committee on Banking Supervision (Basel Committee) is seeking comment on a consultative document released June 18, 2014 that outlines proposed Supervisory Guidelines for Identifying and Dealing with Weak Banks. The guidelines include problem identification, corrective action, resolution techniques and exit strategies. The Basel Committee states the guidelines also highlight the importance of:

- Implementing an operating framework to facilitate supervisory action and lessen the risk of legal and accounting gaps or "political interference."
- Using financial reporting and monitoring, on-site examination, and regular interaction with auditors and bank management to prevent, or identify early, problems before a bank's solvency is threatened.
- Preparing in advance, including communication strategies and recovery and resolution plans, to support a quick response to a problem bank and limit disruption to the financial system.
- International cooperation among supervisors and other relevant authorities.

Comments are requested no later than September 19, 2014.

OCC Schedules Workshops for Community Bank Directors and Directors of Federal Savings Associations

The Office of the Comptroller of the Currency (OCC) announced that it will conduct a three-day workshop in Columbus, Ohio, beginning July 28, 2014 that is intended to provide directors of community banks and federal savings associations with "practical information" on the roles and responsibilities of a bank director. The workshop will also cover "the regulatory environment, board reports, bank ratings, and resources available exclusively for OCC-regulated institutions."

The OCC will also host two additional workshops targeted to directors of community banks and federal savings associations on July 22, 2014 in Minneapolis, Minnesota. The *Compliance Risk* workshop will focus on major compliance risks and consumer protection regulations, such as the Qualified Mortgage Rule, *Bank Secrecy Act*, and *Community Reinvestment Act*, as well as cover the key elements of an effective compliance risk management program. The *Risk Assessment* workshop will cover the OCC's approach to risk-based supervision, and best practices to identify, measure, monitor and control risk. Topics addressed will include "industry hot topics, such as credit risk, interest rate risk, and the regulatory environment."

House Committee on Financial Services Approves Bills to Extend TRIA and Modify FSOC

The House Committee on Financial Services approved H.R. 4871, the *TRIA Reform Act of 2014*, by a vote of 32 to 27. The bill would reauthorize the *Terrorism Risk Insurance Act* (TRIA) for a period of five years. In addition, the bill would modify the TRIA to distinguish between terrorism events resulting from nuclear, biological, radiological, and/or chemical (NBCR) attacks from other acts of terrorism. NCBR attacks would be subject to a $100 million trigger and a 15 percent co-pay requirement for insurance companies. Non-NCBR attacks would be subject to an increase in the trigger amount from $100 million to $500 million over the five-year period and a corresponding increase from 15 percent to 20 percent in the co-pay requirement for insurance companies.

The U.S. Senate Committee on Banking, Housing, and Urban Affairs approved S. 2244, the *Terrorism Risk Insurance Program Reauthorization Act of 2014*, on June 3, 2014. The provisions of this bill would extend the TRIA for a period of seven years, increase the mandatory recoupment threshold from $27.5 billion to $37.5 billion, and increase the insurance company copayment amount for losses resulting from acts of terrorism from 15 percent to 20 percent over a five-year period.

Also on June 20, the House Committee on Financial Services approved two bills that would affect the operations of the Financial Stability Oversight Council (FSOC). H.R. 4881 would impose a six-month moratorium on the authority of the FSOC to make financial stability determinations, which would require non-bank financial services companies determined to be "systemically important" to be supervised by the Federal Reserve Board. (Note: the bill text states this is a six-month moratorium though press statements indicate the duration of the moratorium would be one year.)

The Committee also approved H.R. 4387, the *FSOC Transparency and Accountability Act*. The bill would require the FSOC to hold open meetings and comply with the requirements outlined in the *Federal Advisory Committee Act*.

Enterprise & Consumer Compliance

FHA Guidance Reminds Lenders of Advertising Prohibitions Related to Reverse Mortgages

The Federal Housing Administration (FHA) published a Mortgagee Letter, #14-078, on June 19, 2014 to remind lenders participating in the agency's Home Equity Conversion Mortgage (HECM) Program to ensure that senior borrowers are fully informed of their options when applying for reverse mortgages. The Letter reinforces the agency's prohibition against misleading or deceptive advertising and the fact this prohibition extends to misleading or deceptive descriptions of the HECM program. The Letter also states that mortgagees may not state or imply that, as a result of their approval to participate in FHA programs, any of their products have been endorsed by FHA or the Department of Housing and Urban Development.

CFPB Director Testifies Before the House Committee on Financial Services

Richard Cordray, Director of the Consumer Financial Protection Bureau (CFPB or Bureau), presented the Bureau's fifth semi-annual report to the House Committee on Financial Services on June 18, 2014. He previously presented the report to the Senate Committee on Banking, Housing, and Urban Affairs on June 10. In response to the Committee member questions following his prepared remarks, Director Cordray indicated:

- The Bureau is working on a white paper that is expected to be released later this summer, detailing its proxy methodology for disparate impact used in indirect automotive lending.
- A proposed rule governing prepaid cards is expected to be released at the end of the summer.
- A final rulemaking related to the *Military Lending Act* is close to completion.
- The National Mortgage Database will not include personally identifiable information.

CFPB, Other Federal Agencies and State Attorneys General Reach Agreement with Mortgage Lender and Servicer to Pay Nearly $1 Billion In Combined Penalties and Relief to Borrowers

On June 17, 2014, the Consumer Financial Protection Bureau (CFPB or Bureau), Department of Justice (DOJ), Department of Housing and Urban Development (HUD), and attorneys general in 49 states and the District of Columbia announced they had reached an agreement with a Virginia-based mortgage lender and servicer (Company) to pay $550 million to address findings of unfair, deceptive, and abuse acts and practices related to its mortgage origination, servicing, and foreclosure activities. The payments would include: $500 million in loss-mitigation relief to be paid over a three year period to underwater borrowers; $40 million in refunds to consumers whose loans were serviced by the defendant and who lost their homes to foreclosure; and $10 million to the federal government. The agreement would also require the Company to implement changes in its mortgage servicing practices, including foreclosure processing, third-party vendor oversight, and bankruptcy protections.

Also on June 17, the DOJ separately announced that, as part of the settlement, the Company had agreed to pay $418 million to resolve its potential liability under the federal False Claims Act for originating and underwriting loans that violated its obligations as a participant in the Federal Housing Administration (FHA) insurance program.

CFPB Takes Action to Address Deceptive Credit Card and Discriminatory Practices

The Consumer Financial Protection Bureau (CFPB or Bureau) announced on June 19, 2014 that it had taken an enforcement action against a federal savings bank (Bank) to address the CFPB's findings of deceptive marketing and discriminatory practices related to the Bank's credit card business. The consent order requires the Bank to end these practices, and also to:

- Refund $56 million to the approximately 638,000 consumers who were affected by its deceptive marketing of the credit card add-on products;
- Provide $169 million in relief to approximately 108,000 borrowers (in the form of monetary payments and the reduction, or complete waiver, of borrowers' credit card balances) found to have been excluded from debt relief offers on the basis of their national origin;
- Work with credit reporting agencies to ensure that any negative information associated with the consumer's credit card account that is related to the fact the consumer did not

receive a debt relief offer is deleted from their credit history;

- Forgive the debt on consumer credit card accounts that were not extended debt relief offers;
- Take affirmative steps to strengthen fair lending compliance; and
- Pay a $3.5 million penalty to the CFPB Civil Penalty Fund based on the deceptive marketing practices. The CFPB states it has determined not to assess a penalty for the charges of illegal discrimination (in violation of the *Equal Credit Opportunity Act*, or ECOA) based on "a number of factors, including that the company self-reported the violation, self-initiated remediation for the harm done to affected consumers, and fully cooperated with the Bureau's investigation.

The enforcement action was taken jointly by the CFPB and the Department of Justice (DOJ). The DOJ concurrently filed a complaint and proposed consent decree.

Capital Markets & Investment Management

IOSCO Research Department Releases Results to Annual Survey on Securities Markets Risk Trends

The Research Department of the International Organization of Securities Commissions (IOSCO) published a Staff Working Paper entitled *A Survey of Securities Markets Risk Trends 2014: Methodology and Detailed Results* (Survey). The document provides a detailed analysis of responses to the Research Department's annual survey on market trends and emerging risks, which is intended "to gather views on emerging trends within securities markets and to help identify or highlight pockets of risk that may not be captured by normal statistical analysis or desk research."

IOSCO summarizes the following as main points identified by the survey respondents:

- "Macro-prudential" issues, especially in the areas of banking vulnerabilities and capital flows.
- "Micro-prudential" risks clustered around the areas of corporate governance, financial risk disclosure, shadow-banking activities and regulatory uncertainty.
- Regulator respondents see risk emanating from illegal conduct, corporate governance, financial risk disclosure, and benchmarking issues. Market participant respondents are concerned with risk arising from the search for yield, resolution and resolvability plans, central counterparties (CCPs), and market fragmentation.
- Few "risks" are sourced within securities markets. The role of securities markets with regard to risk was more likely to transmit and/or amplify shocks from outside than to originate risk.
- The fallout from banking vulnerabilities and capital flow volatility could have considerable consequences for the real economy; concerns about trends in the housing market continue to increase.
- The perception of risks can change quickly.
- The impact of cross-border capital flows, financial risk disclosure and CCPs s has drawn more attention between 2013 and 2014.

IOSCO also states that three trends have been repeatedly and consistently cited as major concerns in each of the past three years of the survey: regulatory uncertainty; banking vulnerabilities; and volatile capital flows. Other areas of concern include cybercrime or cyber-related issues and their potential to threaten systemic stability, financial risk disclosures, and resolution and resolvability frameworks.

Senate Subcommittee Conducts Hearing on the Impact of High Frequency Trading

The Securities, Insurance, and Investment Subcommittee of the Senate Committee on Banking, Housing and Urban Affairs conducted a hearing on June 18, 2014 on the topic of High Frequency Trading (HFT) and its impact on the U.S. economy. Three witnesses provided testimony, including representatives from the securities industry and academia. In general, the witnesses all acknowledged the industry derived certain benefits from HFT, including increased liquidity and decreased transaction costs. They also suggested that, despite a recent heightened awareness of HFT, not all HFT is detrimental to the market and that increases in market risk are related more to issues in the structure of the markets rather than HFT in particular. One witness offered the following recommendations that he thought "would be helpful in ensuring the safety and security of our automated world:"

- Mandating and harmonizing exchange level kill switches;
- Establishing order to trade ratios; and
- Abolishing the immunity from liability that exchanges losses from market disruptions based on their self-regulatory organization status.

In addition, the witness also highlighted two items the Securities and Exchange Commission (SEC) has said it will be working on at the request of SEC Chair White, including an anti-disruptive trading rule, which he suggested would require careful formulation, and a requirement to hold unregistered active proprietary traders to the SEC's rules as dealers, which he suggested should be coordinated and streamlined with other registration requirements.

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 New York-based hedge fund advisory firm with engaging in prohibited principal transactions. The SEC also charged the firm for retaliating against the employee who reported the trading activity to the SEC. The firm agreed to pay $2.2 million, representing disgorgement, prejudgment interest, and a $300,000 penalty.
- The SEC charged Pennsylvania-based private equity firm with violating the SEC's pay-to-play rules for investment advisers, which prohibit investment advisers from providing compensatory advisory services – either directly to a government client or through a pooled investment vehicle – for two years following a campaign contribution by the firm or certain associates to political candidates or officials in a position to influence the selection or retention of advisers to manage public pension funds or other government client assets. The firm agreed to settle the charges by paying a $35,000 penalty in addition to disgorgement of advisory fees and prejudgment interest.
- The SEC charged a hedge fund advisory firm and its founder with fraud for transferring funds from a hedge fund to an alternate investment in contravention to the hedge fund's stated investment strategy and without the knowledge of the fund's investors. In addition, the firm and its founder diverted some of the transferred proceeds to their

personal use. The SEC is seeking permanent injunctive relief, disgorgement and prejudgment interest, and civil money penalties.

- The CFTC obtained a federal court Order requiring two individuals and their companies to pay a civil monetary penalty of $32,370,000 and restitution for defrauded customers totaling $12 million in conjunction with the operation of a commodity futures pool. The court's Order also imposes permanent trading and registration bans against the defendants and prohibits them from violating provisions of the *Commodity Exchange Act*, as charged

Recent Supervisory Actions against Financial Institutions

Last Updated: June 20, 2014

Agency	Institution Type	Action	Date	Synopsis of Action
CFPB	Federal Savings Bank	Administrative Action	06/19	The Consumer Financial Protection Bureau and the Department of Justice initiated an enforcement action against federal savings bank to address findings of deceptive marketing and discriminatory practices related to the bank's credit card business. The bank is required to pay $56 million in refunds, $169 million in relief, and $3.5 million penalty.
CFPB, DOJ, HUD, State Attorneys General	Mortgage Lender and Servicer	Consent Order	06/17	The Consumer Financial Protection Bureau, Department of Justice, Department of Housing and Urban Development, and 49 state attorneys general proposed a consent agreement with mortgage lender and servicer to address their findings of unfair, deceptive, and abusive acts and practices engaged in by the company. The proposed agreement would require nearly $1 billion in total payment of relief, refunds, and penalties.
Federal Reserve Board	State Member Bank	Civil Money Penalty	06/17	The Federal Reserve Board entered into an Order of Assessment of Civil Money Penalty with a Florida-based state member bank to address violations of the National Flood Insurance Act.
Federal Reserve Board	Bank Holding Company	Written Agreement	06/03	The Federal Reserve Board entered into a Written Agreement with an Arizona-based bank holding company to ensure that it serves as source of strength for its state nonmember bank and nonbank subsidiaries. The agreement addressed dividends and distributions, and debt and stock redemptions.
Federal Reserve Board	State Member Bank	Written Agreement	05/29	The Federal Reserve Board entered into a Written Agreement with an Iowa-based state member bank to address deficiencies impacting it safety and soundness including: board oversight, management review, credit risk management, lending and credit administration, loan review, asset improvement, allowance for loan and lease losses, capital, and dividends and distributions,.
Consumer Financial Protection Bureau	Nonbank - Real Estate Company	Consent Order	05/28	The Consumer Financial Protection Bureau entered into a Consent Order with a nonbank financial services company – a real estate brokerage and settlement services company – to address violations of the Real Estate Settlement Procedures Act related to disclosures regarding a consumer's use of the companies affiliated service providers.
Federal Deposit Insurance Corporation	State nonmember bank	Consent Order; Order for Restitution; Civil Money Penalty	05/13	The Federal Deposit Insurance Corporation entered into Consent Order, Order for Restitution, and Civil Money Penalty with an insured state member bank and its institution-affiliated party to address unfair and deceptive acts and practices provisions of the Federal Trade Commission Act and violations of the Servicemembers Civil Relief Act. Total payments of $96.6 million will be required.
Federal Reserve Board	State member bank	Civil Money Penalty	04/15	The Federal Reserve Board issued an Order of Assessment of Civil Money Penalty against a Wyoming-based state member bank to address violations of the National Flood Insurance Act.

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