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Safety & Soundness

FDIC Approves Final Rule to Impose Assessments Surcharge on Large Institutions

On March 15, 2016, the Federal Deposit Insurance Corporation (FDIC) approved a final rule that imposes a surcharge on the quarterly assessments of insured depository institutions with total consolidated assets of $10 billion or more. The surcharge will equal an annual rate of 4.5 basis points applied to the institution's assessment base (with certain adjustments). It will begin July 1, 2016, if the Deposit Insurance Fund (DIF or fund) reserve ratio reaches 1.15 percent before July 1, 2016, or the first day of the calendar quarter after the reserve ratio reaches 1.15 percent, if it does. The surcharge will continue through the quarter that the reserve ratio first reaches or exceeds 1.35 percent, but not later than December 31, 2018. If the reserve ratio does not reach 1.35 percent by December 31, 2018, the FDIC will impose a shortfall assessment on March 31, 2019, on insured depository institutions with total consolidated assets of $10 billion or more. The rule becomes effective July 1, 2016. [Press Statement] [Final Rule]

Basel Committee Publishes Guidance to Assess Basel III Compliance by Jurisdiction

On March 17, 2016, the Basel Committee on Banking Supervision (Basel Committee) published a *Handbook for Jurisdictional Assessments*, which sets out guidance, principles, and processes for assessing a particular jurisdiction's compliance with the Basel III standards under the Regulatory Consistency Assessment Programme (RCAP). The RCAP assesses the consistency and completeness of a jurisdiction's capital and liquidity rules against the globally agreed Basel III standards and calls out the significance of any deviations. The Basel Committee also published RCAP Questionnaires that jurisdictions can use as a self-assessment of their efforts to implement the Basel III risk-based capital, liquidity coverage ratio (LCR), and Pillar 3 disclosure requirements. These questionnaires serve as a starting point for the RCAP and are intended to help Basel Committee member jurisdictions and other regulators check and improve the alignment of their domestic regulations with corresponding Basel standards. [Press Statement] [RCAP Questionnaire] [Handbook]

FSB Releases Thematic Review of Resolution Regimes

The Financial Stability Board (FSB) published a peer review report for the *Second Thematic Review on Resolution Regimes* on March 18, 2016. The report forms part of a series of peer reviews to support timely and consistent implementation of the FSB's *Key Attributes of Effective Resolution Regimes for Financial Institutions* (Key Attributes), which set out the core elements of effective resolution regimes that allow authorities to resolve financial institutions in an orderly manner without taxpayer exposure to loss. The peer review examines the range and nature of resolution powers available to banking sector authorities in FSB jurisdictions, as well as any requirements for recovery and resolution planning and resolvability assessments for domestically incorporated banks. Main findings of the review are as follows:

- Only a subset of the FSB membership – primarily home jurisdictions of global systemically important banks – currently have a bank resolution regime with a comprehensive set of powers broadly in line with the Key Attributes. The bank resolution powers that are most often lacking are explicit continuity powers, bail-in powers, and powers to impose a temporary stay on the exercise of early termination rights. The reforms underway in a number of FSB jurisdictions address some, but not all, of the gaps in bank resolution powers compared with the Key Attributes.
- While resolution regimes generally apply to all types of commercial banks, the coverage of bank holding companies, branches of foreign banks, and material non-regulated operational entities within a financial group is more variable across FSB jurisdictions.
- There is significant variation across FSB jurisdictions in the conditions for the use of resolution powers and their level of detail.

- More progress has been made in terms of putting in place processes for recovery planning compared to resolution planning or resolvability assessments. Only nine jurisdictions currently have explicit statutory powers to require banks to adopt appropriate measures to improve their resolvability.

The peer review makes a number of recommendations to FSB jurisdictions to address identified gaps, including, among others, introducing missing powers and recovery and resolution planning requirements for all banks that are potentially systemic in failure, and adopting powers to require banks to take measures to improve their resolvability. Jurisdictions are expected to report to the FSB by December 2016 regarding what actions they have taken, or plan to take (including implementation time frames), in order to address these gaps. [Press Statement]

OCC Proposes Rules to Reduce Regulatory Burden

The Office of the Comptroller of the Currency (OCC) released proposed rules on March 14, 2016, that would remove "outdated or unnecessary provisions" of certain rules to reduce regulatory burden. The proposal is part of the OCC's decennial review of its rules, as required under the *Economic Growth and Regulatory Paperwork Reduction Act* (EGRPRA), and is limited exclusively to OCC rules and that agency's supervision of national banks and federal savings associations. In particular, the agency proposes to:

- Remove approval requirements for certain changes in permanent capital involving national banks;
- Simplify licensing rules for business combinations involving federal mutual savings associations;
- Clarify oath requirements for the national bank director;
- Remove unnecessary burdens with respect to federal savings associations' fidelity bond activities;
- Revise certain fiduciary activity requirements including increasing the asset size limit for mini-funds;
- Remove certain financial disclosure requirements for national banks;
- Remove unnecessary regulatory reporting, accounting, and management policy requirements for federal savings associations;
- Remove unnecessary requirements in the electronic activities rule for federal savings associations;
- Integrate and update OCC rules relating to municipal securities dealers, *Securities Exchange Act of 1934* disclosures, securities offering disclosures, and insider and affiliate transactions;
- Permit the electronic submission of filings required under the *Securities Act of 1933* and the *Securities Exchange Act of 1934*; and
- Update recordkeeping and confirmation requirements for securities transactions.
  [Press Statement] [Federal Register Notice]

Enterprise & Consumer Compliance

Enforcement Actions

The Consumer Financial Protection Bureau (CFPB) and Federal Trade Commission FTC) announced the following enforcement actions in the past week:

- The CFPB announced that a federal district court had entered a final judgment against a debt relief company resolving a lawsuit filed by the CFPB in August 2013 alleging the company charged illegal upfront fees and deceived consumers in violation of the *Telemarketing Sales Rule* and the *Consumer Financial Protection Act*. The final judgment orders the company to pay more than $132 million in restitution to borrowers that paid illegal upfront fees, and $40 million in civil penalties. However, the company has declared bankruptcy and any payments related to the judgment will be made through the bankruptcy process.

- The CFPB announced that it had requested a federal district court to enter a final judgment against a student debt relief scheme that would ban the company and its sole owner from any future involvement in debt relief and student loan services, as well as require it to pay refunds to harmed consumers and a civil money penalty. The proposed final judgment follows a court ruling in favor of the CFPB's claims the defendants violated the *Telemarketing Sales Rule* and the *Consumer Financial Protection Act* by charging consumers illegal upfront enrollment fees before providing any services, deceiving customers about the costs of their services, and falsely representing an affiliation with the Department of Education.
- The FTC announced that it had obtained a court order banning an individual involved in a mortgage modification scam from selling debt relief and mortgage-related products and services, as well as from telemarketing. The scheme was perpetrated by two companies that promised consumers help in getting mortgage modifications, but instead stole their mortgage payments, leading some to foreclosure and bankruptcy. The individual subject to the current court order was found to have participated in the scheme by contracting with the companies and assisting them in procuring payments from clients despite knowing they were engaged in violations of the FTC's *Mortgage Assistance Relief Services Rule* and the *Telemarketing Sales Rule*. In addition to the bans, the individual is prohibited from making misrepresentations about any products or services and from making unsubstantiated claims about any financial product unless they are "non-misleading and based on reliable evidence." The order imposes a penalty of more than $2 million.

Capital Markets and Investment Management

FINRA Publishes Report on Effective Practices for Digital Investment Advice

On March 15, 2016, the Financial Industry Regulatory Authority (FINRA) released a report that provides guidance to financial services firms offering digital investment advice. The report is intended to share effective practices related to digital investment advice services, including digital investment advice tools frequently referred to as "robo advisors," and to remind member firms of their obligations under FINRA rules. Regulatory principles and effective practices are outlined in the following five areas:

- Governance and supervision of algorithms, including initially assessing the methodology of digital tools and the quality and reliability of data inputs, as well as ongoing evaluation such as testing to ensure the tools are performing as expected, and determining whether models used by a tool remain appropriate as market conditions change;
- Customer profiling, including assessing a customer's risk capacity and risk willingness, and addressing inconsistent responses in customer-provided information;
- Governance and supervision of portfolios and conflicts of interest, including determining the risk, return and diversification characteristics of a portfolio suitable for a given investor profile, and mitigating any conflicts that might arise through the selection of securities for a portfolio;
- Rebalancing, including providing descriptions of how the rebalancing works and procedures that define how the tools will act in the event of a major market movement; and
- Training, including training that enables financial professionals to understand the key assumptions and limitations of individual digital investment advice tools, and to determine when the use of a tool may not be appropriate for a client. [Press Statement] [Report]

CFTC Extends Relief in Connection with Swap Trade Confirmations

The Commodity Futures Trading Commission (CFTC) issued a no-action letter, Staff Letter 16-25, on March 14, 2016, extending relief with respect to swap trade confirmation requirements previously provided in CFTC Staff Letter 15-25 but

is set to expire on March 31, 2016. The Staff Letter 16-25 extends the relief to the earlier of March 31, 2017, or until revised CFTC regulations are issued to establish a permanent solution. Such relief is provided to:

- Swap execution facilities (SEFs) from CFTC's Regulation 37.6 that requires an SEF to obtain documents in a trade confirmation issued by an SEF, prior to issuing the confirmation.
- SEFs from the requirement to maintain such documents as records under Regulations 37.1000, 37.1001 and 45.2(a).
- SEFs from the requirement to report confirmation data contained in the documents under Regulation 45.3(a). [Press Release] [CFTC Staff Letter 16-25]

CFTC Approves Substituted Compliance Framework between the U.S. and the EU

On March 16, 2016, the Commodity Futures Trading Commission (CFTC) approved a substituted compliance framework for dually-registered central counterparties (CCPs) located in the European Union (EU), together with a comparability determination (Determination) of U.S. rules with respect to certain EU rules. The Determination identifies those European Market Infrastructure Regulation (EMIR) requirements that provide "a sufficient basis for an affirmative finding of comparability with respect to certain regulatory obligations applicable to derivative clearing organizations (DCOs) that are registered with the CFTC and are authorized to operate as CCPs in the EU. The Determination permits EU CCPs already registered with the CFTC as DCOs and those seeking registration to provide services to U.S. clearing members and clients while complying with certain corresponding EU requirements." The CFTC also issued a no-action letter (Staff Letter 16-26) providing limited relief from the application of CFTC regulations to discrete aspects of a DCO/CCP's non-U.S. clearing activities. The CFTC states these actions follow the agreement between the CFTC and the European Commission regarding dually-registered DCOs/CCPs, and represents a major step in paving the way for the EU's recognition of U.S. CCPs. [Press Statement] [Notice of Comparability Determination] [No-Action Relief]

CFTC Eliminates Reporting and Recordkeeping Requirements for End-Users that Transact in Trade Options in Connection with Their Businesses

The Commodity Futures Trading Commission (CFTC) approved a final rule that removes reporting and recordkeeping requirements for trade option counterparties that are neither swap dealers nor major swap participants (Non-SD/MSPs), including commercial end-users that transact in trade options in connection with their businesses. The final rule became effective March 21, 2016, upon publication in the *Federal Register.* With respect to reporting, the final rule provides that:

- The requirement to report Form TO (Trade Options) annually for otherwise unreported trade options in CFTC regulation 32.3(b) has been eliminated; and
- Non-SD/MSPs will not be subject to Part 45 reporting requirements in connection with their trade options.

The proposed requirement that a commercial participant would need to provide notice to the CFTC of its trade options activities if such activities have a value of more than $1 billion in any calendar year has not been adopted.

With respect to recordkeeping, the CFTC has eliminated the swap-related recordkeeping requirements for Non-SD/MSPs in connection with their trade option activities. However, Non-SD/MSPs transacting in trade options with SDs or MSPs must obtain a legal entity identifier and provide it to their SD/MSP counterparties. [Press Statement] [Final Rule]

CFTC Announces Delivery Method for CEO Attestation under the Volcker Rule

The Commodity Futures Trading Commission's (CFTC's) Division of Swap Dealer and Intermediary Oversight issued a press statement on March 15, 2016, to announce the method of delivery for CEO attestations required under Part 75 of the CFTC's regulations, which implement section 619 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*, commonly referred to as the Volcker Rule. Banking entities meeting certain conditions must provide a CEO attestation regarding their Volcker Rule compliance program and must submit such attestation to the CFTC through this email address: VolckerAttestation@cftc.gov. [Press Statement]

Enforcement Actions

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

- The SEC announced charges against three affiliates of an international insurance company for steering mutual fund clients toward more expensive share classes to increase fees. Based on its investigation, the SEC alleges the firms placed clients in share classes that charged fees for marketing and distribution despite the clients being eligible to buy shares in fund classes without those additional charges. The firms failed to disclose their conflict of interest in selecting share classes that would generate higher revenues and, as a result, the firms collected approximately $2 million in additional fees. The SEC also found the firms failed to monitor advisory accounts on a quarterly basis to prevent reverse churning despite having compliance policies to ensure that fee-based or "wrap" advisory accounts that charged an inclusive fee for both advisory services and trading costs remained in the best interest of clients that traded infrequently, the firms failed to implement them. The firms agreed to pay more than $9.5 million, including disgorgement of more than $2 million in improper fees plus prejudgment interest and a $7.5 million penalty, to settle the SEC's charges.
- The SEC charged a municipal advisor, its CEO, and two employees for breaching their fiduciary duty by failing to disclose a conflict of interest to a municipal client. The case is the first SEC action to enforce the fiduciary duty for municipal advisors created by the *Dodd-Frank Wall Street Reform and Consumer Protection Ac*t. The defendants agreed to the SEC's order to cease and desist from similar future securities-law violations and violations of Rule G-17 of the Municipal Securities Rulemaking Board (MSRB) that requires advisors to deal fairly with their clients, and MSRB Rule G-23 that bars those acting as municipal advisors on a bond offering from underwriting that same offering. The firm agreed to pay more than $289,000 in disgorgement and interest and a $25,000 in civil penalty. Fines and bars were also imposed individually on the employees involved.
- The CFTC issued an order filing and simultaneously settling charges against a registered Retail Foreign Exchange Dealer for failing to meet minimum capital requirements, failing to notify the CFTC of its undercapitalization, and failing to diligently supervise its employees in violation of CFTC Regulations. Under the order, the firm is required to pay a $1 million civil monetary penalty and fulfill certain undertakings relating to its retail foreign exchange dealer operations. The penalty accounted for the dealer's "substantial remedial actions after it discovered its deficiencies as well as its cooperation with the CFTC."
- The CFTC announced that a federal district court had unsealed a civil complaint the CFTC had filed against two foreign web-based binary options firms for illegally soliciting and accepting more than $1 million from at least 50 U.S. customers to trade off-exchange binary options contracts, defrauding those customers, and operating as an unregistered Futures Commission Merchant. According to the CFTC's complaint, to be lawfully offered in the United States, binary options must be traded on a registered board of trade. However, the complaint alleges that two firms did not execute transactions on a registered board of trade. In this case, neither the options nor the firms were registered with the CFTC in any capacity. In addition, the CFTC alleges the firms misrepresented the likelihood of profit and loss that a customer makes while trading binary options, falsely claimed that customer funds were insured against losses, fraudulently induced customers to send more money before initial funds could be returned, and misappropriated customer funds.
- The CFTC issued an Order filing and settling charges against a commodity pool operator for making material misstatements and omissions in its disclosure documents and annual and quarterly reports with respect to its operation of a multi-advisor commodity fund. The firm was found to have wrongly disclosed the basis on which management fees were charged, leading to overcharges in the amount of $5.4 million. Additionally, the fund's annual and quarterly reports misstated the methodology it followed in valuing certain options. The firm was ordered to pay a $250,000 civil monetary penalty and disgorge $5.4 million to settle charges. The Order also required the firm to cease and desist from further violations of the *Commodity Exchange Act*.

Financial Crimes

OFAC and Department of Commerce Expand Access for Cuba and Cuban Nationals to U.S. Financial Institutions and U.S. Dollar

On March 15, 2016, the U.S. Department of the Treasury's Office of Foreign Assets Control (OFAC) and the Department of Commerce's Bureau of Industry and Security announced amendments to the Cuban Assets Control Regulations (CACR) and Export Administration Regulations (31 CFR 515). These amendments took effect on March 16, 2016, and, among other things, are intended to expand the access of Cuba and Cuban nationals to U.S. financial institutions and the U.S. dollar as prescribed in the amendments. In particular, the banking and financial services provisions set forth at 31 CFR 515, specifically Section 515.584(d), (e), (g), and (h), authorize U.S. banking institutions to:

- Process "U-turn" transactions in which Cuba or a Cuban national has an interest as long as neither the originator nor the beneficiary is subject to US jurisdiction *and* these transfers originate and end outside the United States (emphasis added).
- Unblock and return funds to the originator or originating financial institution under specific prescribed circumstances, provided the institution submits a report to OFAC within 10 days of unblocking and returning the underlying funds.
- Process U.S. dollar monetary instruments, including cash and travelers' checks, when these are presented indirectly through a third-country financial institution holding a corresponding account for a Cuban financial institution, *and* when these monetary instruments are not otherwise prohibited, exempt and are authorized. Correspondent accounts at third-country financial institutions used for such transactions may be denominated in U.S .dollars as well. Importantly, the new section created by OFAC (31 CFR 515.584(g)) does not authorize the opening of correspondent banking accounts for Cuban financial institutions at US financial institutions.
- Open and maintain accounts in the name of a Cuban national located in Cuba *solely for the purposes of receiving payments in the United States* for authorized or non-exempt transactions, *and* for remittance of those moneys to Cuba. [Press Statement] [Treasury Regulations] [Commerce Regulations] [FAQs]

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This is a publication of KPMG's Financial Services Regulatory Risk Practice and KPMG's Americas FS Regulatory Center of Excellence

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