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In This Issue

Safety & Soundness

OFR Paper Highlights Challenges in Interpreting the Liquidity Coverage Ratio

On October 7, 2015, the Office of Financial Research (OFR) released a working paper entitled, *The Difficult Business of Measuring Banks' Liquidity: Understanding the Liquidity Coverage Ratio*. The paper is intended to highlight some of the complexities associated with interpreting the Liquidity Coverage Ratio (LCR) and, in particular, uses a series of increasingly complex examples to demonstrate differences in the LCRs computed under the standards established by the Basel Committee on Banking Supervision (Basel Committee) in 2013 and as implemented by the U.S. regulators in 2014. The authors suggest that LCRs calculated under the U.S. standard are more volatile and difficult to interpret than LCRs calculated under the Basel Committee standard because "the U.S. rule adds a time dimension to the LCR's volatility through the inclusion of a maturity mismatch add-on term in the denominator to account for the peak-day net cash outflow during the 30-day window." The paper is part of the OFR's broader work monitoring and assessing the impact of changes in liquidity and capital regulations on the stability of the U.S. banking system. [Press Statement] [OFR Research Paper]

CPMI Issues Consultative Report on Correspondent Banking

The Committee on Payments and Market Infrastructures (CPMI) issued a consultative report on correspondent banking on October 6, 2015. The report is a response to the observation that there is a reduction in the number of banks providing correspondent banking services, and the reasons given for this reduction include compliance costs with AML/CFT (anti-money laundering/combatting the financing of terrorism) regulations, an increased perception of risk, and uncertainties surrounding the potential impact of noncompliance. The report provides an overview of correspondent banking arrangements and reviews certain technical measures relating to: i) know-your-customer (KYC) utilities, ii) use of the Legal Entity Identifier (LEI), iii) information-sharing mechanisms, and iv) improvements in payment messages. The report also includes four recommendations for consideration by the industry and authorities that the CPMI believes might alleviate some of the concerns and costs associated with correspondent banking. Comments are requested no later than December 7, 2015. [Press Statement] [Correspondent Banking Report]

Enterprise & Consumer Compliance

CFPB Releases Outline of Proposed Rules to Amend Arbitration Agreements

The Consumer Financial Protection Bureau (CFPB or Bureau) announced on October 7, 2015, that it is considering the issuance of proposed rules that would ban companies from including arbitration clauses that block class action lawsuits in their consumer contracts. An outline of the proposals currently under consideration was released concurrently with the announcement. The CFPB's action is informed by findings from its study on the use of arbitration clauses in consumer financial markets, which was released in March 2015, and would apply to most consumer financial products and services that the CFPB oversees, including credit cards, checking and deposit accounts, prepaid cards, money transfer services, certain auto loans, auto title loans, small dollar or payday loans, private student loans, and installment loans. [Press Statement] [Outline of CFPB's Proposal] [CFPB's 2015 Arbitration Study]

CFPB Bulletin Addresses RESPA Compliance and Marketing Services Agreements

On October 8, 2015, the Consumer Financial Protection Bureau (CFPB or Bureau) issued Compliance Bulletin 2015-05 to remind participants in the mortgage industry that kickbacks and referral fees are prohibited under the *Real Estate Settlement Procedures Act* (RESPA) and to describe the risks that could potentially arise by entering into marketing services agreements (MSAs). The Bureau states that, based on its investigation, "it appears that many MSAs are designed to evade RESPA's prohibition on the payment and acceptance of kickbacks and referral fees." The Compliance Bulletin summarizes existing RESPA requirements and general information on MSAs, examples of market behavior identified through the Bureau's enforcement activity, and the legal and compliance risks the Bureau has observed from these arrangements. [Press Statement], [CFPB Compliance Bulletin 2015-05]

Insurance

IAIS Concludes Development of Higher Loss Absorbency Requirement

The International Association of Insurance Supervisors (IAIS), on October 5, 2015, announced that it has concluded initial development of the Higher Loss Absorbency (HLA) requirement for global systemically important insurers (G-SIIs). The development of the HLA is the second step of a long-term project to develop risk-based, group-wide global insurance capital standards, and follows the development of Basic Capital Requirements (BCR) in 2014. The third step will be the development of a risk-based group-wide global Insurance Capital Standard (ICS), which is due to be adopted by the end of 2019. Beginning in 2016, the HLA will be reported on a confidential basis to group-wide supervisors and be shared with the IAIS for purposes of improving the HLA. The IAIS plans to annually review the design and calibration of the HLA as well as the BCR and to recommend any necessary changes. Beginning in 2019, G-SIIs will be expected to hold qualifying regulatory capital that is not less than the sum of the required capital amounts of the HLA and BCR. [Press Statement]

FIO Issues Report on Certifying an Act of Terrorism

The U.S. Department of the Treasury's Federal Insurance Office (FIO) released a report entitled *The Process for Certifying an "Act of Terrorism" under the Terrorism Risk Insurance Act of 2002* on October 9, 2015. The report provides an overview of the Terrorism Risk Insurance Program, which provides a federal backstop for certain U.S. property and casualty insurance losses resulting from a certified act of terrorism, and findings related to FIO's study of the processes employed by the Secretary of the Treasury, in consultation with United States Attorney General and Secretary of Homeland Security, to certify an "act of terrorism." The FIO concludes that, in light of the "potentially unlimited sets of facts that may give rise to a certification," the certification process must allow for flexibility to obtain and consider all relevant information and that public communication concerning the status of an act being considered for certification can and should be improved through amendments to current regulations. [Press Statement] [Report]

Capital Markets and Investment Management

SEC Approves New FINRA Rule Expanding Its Transparency Initiative

On October 8, 2015, the Financial Industry Regulatory Authority (FINRA) announced that the Securities and Exchange Commission (SEC) had approved FINRA's proposal to expand its transparency initiative for over-the-counter (OTC) equity securities. Under the newly approved rule, FINRA will supplement the alternative trading system (ATS) volume it currently publishes with all other equity volume executed over-the-counter by FINRA members. A notice announcing the timing of this change will be forthcoming. FINRA states that the rule is intended to bring additional transparency to this area of the financial markets, as part of an ongoing initiative to help enhance investor confidence. [Press Statement] [Final Rule]

Enforcement Actions

The Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA) announced the following enforcement actions in the past week:

- The SEC announced that a broker-dealer and its investment adviser affiliate agreed to pay more than $1.1 million ($750,000 civil money penalty and $400,000 in disgorgement and prejudgment interest) to settle the SEC's charges they failed to maintain and enforce policies and procedures to prevent the misuse of material nonpublic information by repeatedly sharing information.
- The SEC announced that three related equity fund advisers consented to the entry of the SEC's order finding that they breached their fiduciary duty to the funds, failed to properly disclose information to the funds' investors, and failed to adopt and implement reasonably designed policies and procedures in association with accelerated monitoring fees and discounts on legal fees. Without admitting or denying the findings, they agreed to cease and desist from further violations, to disgorge $26.2 million of ill-gotten gains plus prejudgment interest of $2.6 million, and to pay a $10 million civil penalty. The SEC states the remedial action reflects the firms' voluntary and prompt cooperation with the Division of Enforcement's investigation.
- The SEC announced that a public company has agreed to settle charges that its joint venture in a foreign country made cash payments and provided other benefits to individuals at state-owned and state-controlled facilities in exchange for sales. The company has agreed to pay more than $14 million to settle the SEC's finding that it violated the *Foreign Corrupt Practices Act* (FCPA) and reaped more than $11 million in profits from its misconduct. The company also agreed to report to the SEC for a two-year period on the status of its remediation and implementation of FCPA and anti-corruption compliance measures.
- FINRA announced that it has expelled a firm and barred its Chief Executive Officer and Chief Compliance Officer from the securities industry to address FINRA's findings they engaged in fraud, sales practice abuses, and widespread supervisory and anti-money laundering (AML) failures in association with a scheme to conceal a kickback of private placement fees. The parties consented to the entry of FINRA's findings but did not admit or deny the charges. Brad Bennett, FINRA's Executive Vice President and Chief of Enforcement, is quoted as saying that the findings "…were consistent with the culture of non-compliance fostered by [the firm] and its principals, which manifested itself in widespread sales practice abuses and AML violations that are also detailed in this case."

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