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Safety & Soundness

Basel Committee Releases FAQs on Basel III Countercyclical Capital Buffer

The Bank for International Settlements' Basel Committee on Banking Supervision (Basel Committee) issued Frequently Asked Questions (FAQs) and other supporting information on the Basel III countercyclical capital buffer on October 19, 2015. The release includes questions and information related to national buffer decisions, jurisdictional reciprocity, identification and calculation of geographic credit exposures, calculation of the final bank-specific capital buffer add-on, public disclosure requirements, and timing and frequency of changes in buffer rates. The report also includes a list of all prevailing and pre-announced buffers, as well as developments related to domestic rule-making for both Basel Committee member jurisdictions and select non-member jurisdictions. [Press Statement] [FAQs]

Comptroller Curry Highlights Increasing Credit Risk

Thomas J. Curry, Comptroller of the Currency, spoke before the Exchequer Club on October 21, 2015, on the topic of increasing credit risk in the federal banking system. Comptroller Curry noted that examiners were seeing banks "reach for growth" following steady loan growth over the past several years, adding that it was a time when supervisors and bank risk officers need to be most vigilant. He said consideration should be given to whether banks have the appropriate risk management processes and structures in place to measure, monitor, and control for the increased credit risk. [Press Statement] [Curry Remarks]

FDIC Approves Proposal to Impose Surcharge on Large Institution and Increase DIF Reserve Ratio

The board of the Federal Deposit Insurance Corporation (FDIC) adopted a proposed rule on October 22, 2015, to impose a surcharge on the quarterly assessments of insured depository institutions with total consolidated assets of $10 billion or more. The surcharges would begin the quarter after the reserve ratio of the Deposit Insurance Fund (DIF) first reaches or exceeds 1.15 percent and would continue through the quarter the reserve ratio first reaches or exceeds 1.35 percent. The surcharge would equal an annual rate of 4.5 basis points applied to the institutions assessment base (after certain adjustments). The FDIC anticipates the surcharges will commence in 2016 and the 1.35 reserve ratio will be reached in eight quarters. The proposal is consistent with requirements of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*. Comments are requested within 60 days following publication in the *Federal Register*. [Press Statement] [Proposed Rule}

OFR Working Paper Considers Risks from Interconnectedness in Financial Networks

The Department of the Treasury's Office of Financial Research (OFR) released Working Paper 15-21 on October 20, 2015, to provide reviews of current research on network models of the financial system. Network models are tools to analyze interconnectedness between financial firms, which has been identified as a potential amplifier of financial shocks. The OFR's paper, *Contagion in Financial Networks*, focuses on networks of payment obligations between financial firms created through lending, derivatives transactions, and other financial contracts. Based on the research reviewed, the authors conclude that the potential for contagion depends on network structure and factors such as the size, leverage, and asset quality of individual financial institutions. [Press Statement] [Working Paper 15-21]

Insurance

IAIS Releases Assessment Report for ICPs 9, 10, and 11

The International Association of Insurance Associations (IAIS) released an *Aggregate Report from Assessment* on Insurance Core Principles (ICPs) 9 (*Supervisory Review and Reporting*), 10 (*Preventive and Corrective Measures*), and 11 (*Enforcement*). The report was prepared by the "Expert Team Conducting the Self-Assessment and Peer Review of ICPs 9, 10 and 11" in consultation with the Implementation Committee and Technical Committee, and includes their recommendations for enhancing observance and understanding of the ICPs. [Press Statement]

Capital Markets and Investment Management

Agencies Approve Joint Final Rule for Swap Margin Requirements

On October 22, 2015, the Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corporation (FDIC) each announced the approval of a joint final rule released in cooperation with the Federal Reserve Board, the Farm Credit Administration, and the Federal Housing Finance Agency that establishes minimum margin and capital requirements for entities that are registered with the Commodity Futures Trading Commission (CFTC) or the Securities and Exchange Commission (SEC) as swap dealers, major swap participants, security-based swap dealers, or major security-based swap participants and for which one of the issuing agencies is the primary federal regulator (swap margin rule). The rule becomes effective April 1, 2016 and compliance will be phased-in beginning September 2016.

Coincident with the release of the final rule, the agencies released a joint interim final rule that exempts from their swap margin rule "certain non-cleared swaps and certain non-cleared security-based swaps with certain counterparties" that qualify for an exception or exemption from clearing under the initial and variation margin requirements. Under this rule, financial institutions with $10 billion or less in total assets that enter into swaps for hedging purposes would not be required to provide margin collateral, nor would commercial end-users that enter into swaps to hedge commercial risk. The interim final rule becomes effective April 1, 2016, though comments are requested no later than January 31, 2016. [Press Statement] [Joint Final Rule] [Joint Interim Final Rule]

SEC Releases Enforcement Activity Results for Fiscal Year 2015

On October 22, 2015, the Securities and Exchange Commission (SEC) released summary results for the enforcement actions initiated by the agency in fiscal year 2015, noting as highlights that 807 enforcement actions were filed covering a wide range of misconduct, and the orders obtained totaled approximately $4.2 billion in disgorgement and penalties. Of the 807 enforcement actions filed, 507 were independent actions for violations of the federal securities laws and 300 were either actions against issuers who were delinquent in making required filings with the SEC or administrative proceedings seeking bars against individuals based on criminal convictions, civil injunctions, or other orders. The agency's "first-of-their-kind" cases included actions involving: a private equity adviser for misallocating broken deal expenses; an underwriter for pricing-related fraud in the primary market for municipal securities; a "Big-Three" credit rating agency; violations arising from a dark pool's disclosure of order types to its subscribers; a *Foreign Corrupt Practices Act* action against a financial institution; an admissions settlement with an auditing firm; and an SEC rule prohibiting the use of confidentiality agreements to impede whistleblower communication with the SEC. [Press Statement]

House Subcommittee Conducts Oversight Hearing of SEC's Investment Management Division

On October 23, 2015, the House Committee on Financial Services, Subcommittee on Capital Markets and Government Sponsored Enterprises conducted an oversight hearing of the Securities and Exchange Commission's (SEC) Division of Investment Management, which is responsible for the regulation of investment companies, variable insurance products, and federally registered investment advisers. Mr. David Grimm, Director of the Division of Investment Management, was the sole witness. Among other things, his testimony highlighted potential regulatory initiatives to address: the use of derivatives by investment companies, transition plans for investment advisers, stress testing for large investment advisers and large investment companies, and third party compliance review. Mr. Grimm's prepared testimony did not indicate timing for a proposed rule that would establish a uniform fiduciary standard of conduct for broker-dealers and investment adviser when providing investment advice about securities to retail investors. [Subcommittee Hearing]

Enforcement Actions

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

- The SEC announced that it had reached a settlement with two related advisory firms to address the SEC's charges they failed to disclosure a change in the investment strategy employed by a closed-end fund they both advised, resulting in misrepresentations to investors and the board of directors as well as in regulatory filings. The two firms have agreed to pay a total of approximately $17.5 million toward settlement of charges, including $8.2 million in disgorgement of advisory fees, $1.4 million in pre-judgment interest, a $3 million penalty, and $4.9 million to compensate investors for losses.
- The CFTC issued an order instituting and simultaneously setting charges against a registered futures commission merchant to address violations of the CFTC's regulations governing concentration limits applicable to the investment of segregated commodity customer funds. The order requires the futures commission merchant to pay a $140,000 civil monetary penalty, and to regularly review its policies and procedures and provide training to ensure compliance with applicable regulations.
- The CFTC filed a civil complaint in a U.S. District Court charging an individual and his proprietary trading company with spoofing and employment of a manipulative and deceptive device while trading at least five futures products on four different futures exchanges. The complaint explains that the scheme created the appearance of false market depth that the two exploited to their benefit while "harming other market participants."
- The CFTC announced that a U.S. District Court judge entered an Order for Final Judgment by Default against an individual, and a Consent Order against his company, imposing restitution requirements of more than $6.2 million. In addition, the Orders require the two to pay civil monetary penalties totaling more than $24.8 million for their fraud, misappropriation, embezzlement, and operation of a Ponzi scheme, while illegally acting as Commodity Trading Advisors and Commodity Pool Operators without registering as such with the CFTC. The Orders also impose permanent trading and registration bans on the defendants and prohibit them from further violations of the *Commodity Exchange Act*, as charged. In a related criminal action brought by the U.S. Attorney's Office, the individual pleaded guilty to one count of wire fraud and one count of money laundering and was sentenced to 100 months (8 years and 4 months) in prison and ordered to pay criminal restitution totaling more than $6 million.
- FINRA ordered 12 firms to pay restitution totaling more than $4 million and fines totaling more than $2.6 million for failure to apply available sales charge discounts to customers' purchases of Unit Investment Trusts and for related supervisory failures by these firms.

Financial Crimes

Federal and State Agencies Reach Agreements with Foreign Bank and Its Subsidiary to Address Sanctions Violations

The Department of the Treasury's Office of Foreign Assets Control (OFAC) announced that it had entered an agreement with the subsidiary of a foreign bank with operations in the United States to pay more than $329 million to settle charges the entity violated U.S. sanctions regulations by engaging in transactions that involved countries and/or individuals and/or entities subject to OFAC sanctions. The settlement was made in conjunction with actions by the Department of Justice, the New York Department of Financial Services, the New York District Attorney's Office, and the Federal Reserve Board, which resulted in total penalties by all of the agencies of more than $787 million.

The Federal Reserve Board's action was directed at the foreign bank and its subsidiary to address unsafe and unsound practices related to the compliance program for U.S. sanctions laws. The two entities are required to implement an enhanced program to ensure global compliance with the U.S. sanctions administered by OFAC. The Federal Reserve Board has also prohibited the bank from re-employing the individuals involved in the past actions that resulted in the enforcement action or from retaining them as consultants or contractors.

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