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The Washington Report
for the week ended May 20, 2016

In This Issue

Safety & Soundness

FDIC Extends Comment Period for Proposed Rule Governing Recordkeeping Requirements for Institutions with a Large Number of Deposit Accounts

On May 20, 2016, the Federal Deposit Insurance Corporation (FDIC) announced a 30-day extension to the comment period for its proposed rule on recordkeeping requirements for FDIC-insured institutions with a large number of deposit accounts. Comments on the proposed rule will now be accepted through June 25, 2016. The goal of the proposed rule is to facilitate the rapid payment of insured deposits to customers in the event a large institution fails. It would apply to insured depository institutions with at least 2 million deposit accounts. [Press Statement] [Extension Notice]

Financial Stability Board Disbands Enhanced Disclosure Task Force

On May 13, 2016, the Financial Stability Board (FSB) announced the closure of its Enhanced Disclosure Task Force (EDTF), which was established in May 2012 with the goal of making recommendations to improve the quality, comparability and transparency of risk disclosures made by banks. In December 2015, the FSB published the EDTF's third progress report on the implementation of its recommendations on bank risk disclosures by 40 global or domestic systemically important banks. The third progress report reinforced the continued increase in implementation of the EDTF's recommendations by banks, and the improvements made in bank disclosures. Consequently, the FSB found that it did not find the need to conduct any further surveys on this matter, and formally disbanded the Task Force. [Press Statement]

Agencies Issue Joint Proposed Rule on Incentive-Based Compensation Arrangements

On May 16, 2016, six federal regulatory agencies - the Federal Reserve Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the Securities and Exchange Commission, and the National Credit Union Administration - issued a joint press statement inviting public comments on their joint proposed rule to prohibit incentive-based compensation arrangements that encourage inappropriate risk taking at financial institutions. As proposed, the rule would apply to covered institutions (including depository institutions, broker-dealers, investment advisers, credit unions, and other financial institutions under the supervision of the issuing agencies) with average total consolidated assets of $1 billion or more that offer incentive-based compensation. It would establish general qualitative requirements applicable to all covered institutions, as well as specific requirements for institutions based on the size of their total assets. Larger institutions would be subject to more prescriptive requirements related to their incentive compensation practices, including incentive award limits, deferral requirements, downward adjustments and forfeitures, and clawbacks. Comments will be accepted by each of the agencies through July 22, 2016.
[Joint Press Statement] [Joint Proposed Rule]

Enterprise & Consumer Compliance

CFPB Releases Research Report on Auto Title Loan Market

On May 18, 2016, the Consumer Financial Protection Bureau (CFPB or Bureau) released a research report shedding light on the single-payment auto title loan market and borrower behavior in that market. Auto title loans / vehicle title loans, are high-cost, small-dollar loans typically used by borrowers to cover an emergency cash-flow shortage. Based on its review of approximately 3.5 million anonymized, single-payment auto title loan records from nonbank lenders between 2010 through 2013, the CFPB states the average loan amount is $700 and the typical borrowing interest rate is about 300 percent per annum. The borrower agrees to pay the full amount owed in a lump sum plus interest and fees by a certain day. Key findings that emerged in the CFPB's research were:

- Auto title loans have issues similar to payday loans, including high rates of consumer re-borrowing, which can create long-term debt traps. A borrower who cannot repay the initial loan by the due date must re-borrow or risk losing his vehicle. Such re-borrowing triggers high costs in fees and interest.
- One-in-five borrowers with a single-payment auto title loan have their vehicle seized for a failure to repay the debt.
- More than four-in-five of these loans are renewed as borrowers cannot afford to repay them in a single payment.
- More than two-thirds of auto title loan business comes from borrowers who take seven or more consecutive loans.

The CFPB acknowledged that it is considering proposals to end "payday debt traps by requiring lenders to take steps to determine whether borrowers can repay their loan, while also being able to meet other financial obligations."
[Press Statement] [Report]

Agencies Issue Joint Interagency Guidance on Customer Account Deposit Reconciliation Practices to Assure Fair Treatment of Customers

On May 18, 2016, the Office of the Comptroller of the Currency, the Federal Reserve Board, the Consumer Financial Protection Bureau (CFPB or Bureau), the Federal Deposit Insurance Corporation, and the National Credit Union Administration jointly issued interagency guidance to convey their supervisory expectations regarding customer account deposit reconciliation practices. In particular, the agencies expect financial institutions to:

- Adopt deposit reconciliation policies and practices designed to avoid deposit discrepancies or resolve discrepancies such that customers are not disadvantaged;
- Effectively manage their deposit reconciliation practices to avoid violations of the *Expedited Funds Availability Act* as implemented by Regulation CC, which requires financial institutions to make funds deposited in a transaction account available for withdrawal within prescribed time limits, as well as violations of Section 5 of the *Federal Trade Commission Act*, which prohibits a financial institution from engaging in unfair or deceptive acts or practices (UDAP) and, as appropriate, the CFPB's provisions regarding unfair, deceptive, or abusive acts or practices under the *Consumer Financial Protection Act*; and
- Implement effective compliance management systems, including appropriate policies, procedures, internal controls, training, oversight, and review processes, to ensure compliance with applicable laws and regulations and fair treatment of customers. [CFPB Press Statement] [Interagency Guidance]

CFPB Releases Spring 2016 Regulatory Agenda

Under the *Regulatory Flexibility Act*, federal agencies are required to publish an update of their regulatory agendas twice a year. In line with this requirement, the Consumer Financial Protection Bureau (CFPB) posted a semiannual update of its rulemaking agenda on May 18, 2016. Some of the CFPB's major current initiatives and timeframes identified in the CFPB's notice include:

- Arbitration: The CFPB recently issued a proposed rule on the use of arbitration agreements for disputes between companies and consumers with respect to the provision of certain consumer financial products or services.
- Payday, auto title, and similar lending products: A proposed rule is expected to be released in the coming weeks to address consumer protections related to payday loans, auto title loans, and other similar credit products.
- Prepaid accounts: A final rule is expected to be released to create a comprehensive set of consumer protections for prepaid financial products, such as general purpose reloadable cards and other similar products, which are increasingly being used by consumers instead of traditional checking accounts.
- Mortgage servicing: A final rule is expected to be released this summer to amend certain aspects of mortgage servicing rules that took effect in 2013. The proposal will address topics such as enhanced loss mitigation requirements, and compliance with certain rules when the borrower is a successor in interest or is in bankruptcy.
- Know Before You Owe mortgage disclosure rule: A proposed rule is expected to be released to make clarifications and provide further regulatory guidance with respect to the CFPB rule that combines federal mortgage disclosures that consumers receive while applying for and closing on a mortgage loan under the *Truth in Lending Act* (TILA) and the *Real Estate Settlement Procedures Act* (RESPA).
- Overdraft: The CFPB is working on pre-rule making activities to consider potential regulation of overdraft services on checking accounts.
- Debt collection: The CFPB is engaged in developing proposed rules to regulate debt collection practices.
- Larger participants and non-depository lender registration: The Bureau is continuing rulemaking activities to establish its nonbank supervisory authority, by defining larger participants of certain markets for consumer financial products and services
- Women-owned, minority-owned, and small businesses data collection: The Bureau is working to implement section 1071 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which amends the *Equal Credit Opportunity Act* to require financial institutions to report information concerning credit applications made by women-owned, minority-owned, and small businesses.
- Implementation of other mortgage rules: The Bureau is actively working on implementation of its rule amending the *Home Mortgage Disclosure Act* (HMDA), which will go into effect in January 2018, as well as to streamline and modernize HMDA mortgage reporting processes.

Apart from these, the CFPB also has a long term rulemaking agenda, which primarily address issues related to credit reporting and student loan servicing. [Rulemaking Agenda]

FHA Proposes Rule to Amend Reverse Mortgage Program

The Department of Housing and Urban Development (HUD) published a proposed rule on May 18, 2016, that would amend its Federal Housing Administration (FHA) Home Equity Conversion Mortgage (HECM) Program (i.e., the FHA's reverse mortgage program) to codify several changes made to the program over the past several years and implemented through Mortgagee Letters. These changes were intended to increase the sustainability of the HECM program and to provide enhanced consumer protections to the elderly that are extended credit under the program. These features include, among others, requirements for: HECM counseling, full disclosure of loan features, lifetime caps on adjustable interest rate increases, and smaller annual caps on interest rate increases. Comments are requested through July 18, 2016. [Proposed Rule]

Insurance

Federal Reserve Board Governor Tarullo Outlines Regulatory Initiatives for Insurance Companies: Regulatory Reporting, Enhanced Prudential Standards, and Capital

On May 20, 2016, Federal Reserve Board Governor Daniel Tarullo addressed the National Association of Insurance Commissioners' (NAIC) 10th annual International Insurance Forum. He spoke about the Federal Reserve's statutory role in supervising and regulating insurance firms, and stressed the importance of the partnership between the Federal Reserve and state regulators (the primary functional regulators for U.S. insurance companies) in carrying out that role. Governor Tarullo also acknowledged three major regulatory initiatives the Federal Reserve has underway for its supervised insurance firms. The initiatives address:

- Reporting requirements for the nonbank financial firms designated as systemically important by the Financial Stability Oversight Council (FSOC). A proposed rule was published on April 25. 2016 and comments are requested through June 24 2016. [Reg Reporting PR]
- Enhanced corporate governance, risk management, and liquidity standards for insurance companies designated as systemically important by the FSOC. Governor Tarullo anticipates a proposed rule will be released by the Federal Reserve "in the coming weeks."
- Capital requirements for all supervised insurance. An advance notice of proposed rulemaking (ANPR) is expected to be "issued in the coming weeks" and Governor Tarullo expects the ANPR will likely put forward two different methodologies--one for the insurance firms that the Federal Reserve supervises solely because they own a bank or thrift and another for those firms designated as systemically important. [Press Statement] [Speech]

Capital Markets and Investment Management

OCC Issues Guidance for Banks Involved in Money Market Funds Activities

On May 19, 2016, the Office of the Comptroller of the Currency (OCC) issued Bulletin 2016-17 to highlight actions that national banks and federal savings associations (collectively, Banks) should take and factors they should consider with regard to the Securities and Exchange Commission's (SEC) revised money market fund (MMF) rules. In 2014, the SEC revised the rules for MMFs registered under the *Investment Company Act of 1940* and although these rules apply directly to MMFs, the OCC states they indirectly affect:

- Banks that make MMFs available to their customers through their fiduciary and custody activities;
- Bank programs that automatically sweep funds between deposit accounts and MMFs; and
- Banks that invest in MMFs.

The OCC states that Banks involved in any of these activities will likely be affected by compliance, liquidity, operational, and strategic risks related to the SEC's revised rules, each of which is discussed more fully in the Bulletin.
[OCC Bulletin 2016-17]

Treasury and SEC Exploring Means to Collect Data for U.S. Treasury Cash Market; FINRA to Propose Reporting of Treasury Cash Market Transactions

The U.S. Department of the Treasury (Treasury) and the Securities and Exchange Commission (SEC) jointly announced on May 16. 2016, that they are working together to explore efficient and effective means of collecting data surrounding the U.S. Treasury cash market. As part of these efforts, the Treasury and SEC are requesting the Financial Industry Regulatory Authority (FINRA) consider issuing a rule that would require its member brokers and dealers to report Treasury cash market transactions to a centralized repository. The agencies hope that such reporting could provide new information about day-to-day activity in both the inter-dealer and dealer-to-client markets. The Treasury indicates that it intends to work with other agencies to develop a plan to collect data from institutions that actively trade U.S. Treasury securities but are not FINRA members. A comprehensive plan to collect cash market data is anticipated to be in place by year-end 2016. [Press Statement]

SEC Announces Whistleblower Awards

During the week ended May 20, 2016, the Securities and Exchange Commission (SEC) separately announced two whistleblower awards. The first award, an amount between $5 and 6 million, will be paid to a former company insider whose tip helped the SEC uncover securities violations that it says would have otherwise been extremely difficult to detect. The second award, totaling more than $450,000, will be shared by two individuals whose tip helped the SEC to initiate a corporate accounting investigation, and for their assistance throughout the investigation. Sean X. McKessy, Chief of the SEC's Office of the Whistleblower, is quoted as saying, "The recent flurry of awards reflects the high-quality nature of the tips the SEC is receiving as public awareness of the whistleblower program grows."

SEC whistleblowers become eligible for an award when they voluntarily provide the SEC with information that leads to a successful enforcement action. Awards can range from 10 percent to 30 percent of the money collected when the monetary sanctions exceed $1 million. These payments are made out of an investor protection fund established by the Congress that is financed by the monetary penalties paid to the SEC by securities law violators. The SEC also ensures that the confidentiality of whistleblowers is protected. [Press Statement] [Press Statement]

Enforcement Actions

During the week ended May 20, 2016, the Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA) announced the following enforcement actions:

- The SEC announced fraud charges against a city official for connections to a series of fraudulent bond offerings. The SEC found that city officials diverted at least $1.7 million in bond proceeds to fund the city's payroll and other operational costs unrelated to the stated purpose of the bond offerings. The city official agreed to settle the charges without admitting or denying the SEC's allegations and to pay $10,000, subject to court approval, and to never participate in a municipal bond offering again.
- The SEC announced insider trading charges against a professional gambler who allegedly made $40 million based on illegal stock tips from a former board member of a public company who regularly shared inside information about his company with the gambler in advance of market-moving events. The individuals were charged with violating sections of the *Securities Exchange Act of 1934*. The SEC sought a final judgment ordering the return of ill-gotten gains plus interest and penalties, permanent injunctions from future violations of the Act, and an officer-and-director bar against the board member. Criminal charges have also been brought against the two individuals. A third individual, who was named as a relief defendant, agreed to pay full disgorgement of his trading profits totaling more than $930,000 plus interest of approximately $105,000.
- FINRA charged a securities firm, its President and CEO, and it's CFO, with securities fraud in connection with the sale of millions of dollars of municipal revenue bonds to customers. The complaint alleges the defendants fraudulently hid from the bond purchasers, the financial stress faced by the municipal revenue bond conduit borrowers. Additionally, the CEO and the CFO of the firm were also charged with abusing their positions as co-trustees of a charitable trust and misusing the funds to prop up the struggling offerings. FINRA has initiated a formal proceeding against the firm

and its executives and indicates that possible remedies could include a fine, censure, suspension or bar from the securities industry, disgorgement of gains associated with the violations and payment of restitution.

Financial Crimes

FINRA Fines Firms for AML Program Failures

On May 18, 2016, the Financial Industry Regulatory Authority (FINRA) fined a financial services firm and its affiliate a total of $17 million to address its allegations of widespread failures related to the firms' anti-money laundering (AML) programs. FINRA alleged that since the institutions' systems and processes did not keep pace with its growth, the firms were unable to establish AML programs tailored to each firm's business; relying instead upon a patchwork of written procedures and systems across different departments to detect suspicious activity. In addition, the firms are alleged to have failed to conduct the required due diligence and periodic risk reviews for its foreign financial institution clients and the affiliate failed to establish and maintain an adequate Customer Identification Program.

In addition to AML deficiencies, FINRA alleges both firms failed to establish, maintain, and enforce a supervisory system reasonably designed to achieve compliance with Section 5 of the *Securities Act of 1933* for transactions involving large blocks of low-priced securities. The affiliate was also found to have failed to establish and maintain reasonable written supervisory procedures with respect to its review of variable annuity exchange transactions and suitability reviews.

The former AML Compliance Officer of the financial services firm was individually fined $25,000 and suspended for three months. In concluding these settlements, the firms and the former AML Compliance Officer consented to the entry of FINRA's findings without admitting or denying the charges.

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