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In addition, it summarizes [other notable legislative, regulatory, and judicial developments that occurred during the second quarter of 2012.](#)

Large Bank Stress Testing Guidance

On May 14, the Federal Deposit Insurance Corporation (FDIC), Board of Governors of the Federal Reserve System (FRB), and Office of the Comptroller of the Currency (OCC) (collectively referred to as the agencies) finalized the [stress testing guidance](#) that was first proposed in June 2011. The guidance advises banking organizations

on assessing risk through integrated stress testing under a wide range of adverse conditions. The agencies emphasize the importance of using stress tests to support a banking organization's ongoing risk management practices and to inform decision-making under a variety of financial and macroeconomic conditions. This stress testing guidance is separate from the Dodd-Frank Act's

stress testing requirements for large banks and savings associations and the FRB capital planning requirements for large bank holding companies.^{1,2} Those requirements either have been or will be implemented by separate proposals.

Scope of Guidance

The guidance applies to all FDIC-supervised, FRB-supervised, and OCC-supervised banking organizations that have total consolidated assets of more than \$10 billion.³ The guidance first enumerates five principles that banking organizations should use for stress testing their financial soundness and risk management practices. The guidance then discusses four possible stress testing frameworks and emphasizes the importance of stress testing capital and liquidity levels.

Five Stress Testing Principles

The first principle states that stress tests should be customized to the banking organization's unique mix of exposures and risks and should cover all on- and off-balance-sheet activities. The guidance does not prescribe a standardized set of stress tests as this could create unnecessary limitations and inadequately cover a banking organization's risk and activities. Instead, the guidance gives examples of factors banks should consider for stress tests and allows banks to use their own discretion when deciding what and how to stress test. Examples of factors to stress test include credit, market, interest rate, liquidity, operational, reputational, and country

risk. Banking organizations should simultaneously stress test these risks to evaluate their interactions and combined effects. The guidance also recommends stress testing activities at various levels of aggregation, from individual exposures, to portfolios, business lines, and enterprise-wide assessments.

The second principle emphasizes the necessity of applying multiple "conceptually sound" stress tests to achieve a more accurate measure of risk. The board and senior management must define the objective and scope of each stress test. The guidance acknowledges that there will always be some degree of uncertainty when stress testing. To address this uncertainty, banking organizations should use multiple stress testing methods and explain the potential margin of error and statistical uncertainty of the results. The guidance also requires banking organizations to document the stress testing processes, methods, assumptions, judgments, and limitations.

The third principle is that stress testing should be flexible and look forward at least two years. Stress testing flexibility is important so that the tests can quickly incorporate changes in business activity, such as adjustments in portfolio composition or asset quality, and respond to changes in macroeconomic conditions. Furthermore, stress testing should not rely just on historical scenarios but should consider numerous scenarios that have not yet occurred. For example, banking organizations should not assume that successful business lines with low risks will continue to remain so in the future. Stress tests should be conducted with different time horizons to capture both short-term and long-term risks.

The fourth principle emphasizes the importance of reporting stress test results. The guidance states that stress test results should be clear and accompanied by both quantitative data and

¹ For more information on the Dodd-Frank Act stress testing requirements, see [Dodd-Frank, Section 165\(i\)](#) and the independent FDIC and OCC proposals to implement Section 165(i) in [Federal Register, Volume 77, Number 14, Banking Legislation and Policy, Volume 31, Number 1, p.12-13](#), and [Federal Register, Volume 77, Number 15](#), respectively.

² For more information on the FRB's capital planning proposal, see [Federal Register Volume 76, Number 231](#) and [Banking Legislation and Policy, Volume 30, Number 2, p.9](#).

³ These banking organizations include national and state banks, federal savings associations, bank holding companies, and savings and loan holding companies.

qualitative descriptive information. The stress testing report should include all of the assumptions and documentation created in the process so that the analysis can be duplicated if necessary. The stress testing process and results should be clear and shared throughout different levels of the organization to inform decision-making. If the stress test results reveal weaknesses in the banking organization, then proposals should be made to address this weakness and follow-up action should be documented.

Finally, the fifth principle states that stress tests should be conducted under a system of strong internal governance and controls. Strong governance and control procedures help ensure that the stress testing's objectives are met and the recommended actions are carried out. To create such an environment, senior management and the board of directors should work together to create and implement the stress testing framework. The banking organization's board of directors and an independent party should review the stress test framework, procedures, and performance annually. The independent party may be a third-party vendor or an independent internal group.

Four Stress Testing Frameworks

The guidance provides four stress testing frameworks that banking organizations should use: scenario analysis, sensitivity analysis, enterprise-wide stress testing, and reverse stress testing. Each framework has its own strengths and weaknesses, and the frameworks should be applied in tandem to achieve their stress testing objectives.

In scenario analysis, stress testing uses historical or hypothetical scenarios (including extreme ones) to quantify the effect of adverse circumstances on the performance of individual positions, portfolios, and business lines. Scenario analysis should provide an explanatory narrative for how an adverse scenario may be realistically arrived at and

address a banking organization's particular vulnerabilities. For example, if a banking organization has concentrated activities in the oil and gas industry, then it should consider how a scenario such as an oil embargo would affect its activities, exposures, and risks.⁴

Under sensitivity analysis, stress testing evaluates how sensitive a banking organization's exposures, activities, and risks are to various shocks. Sensitivity analysis differs from scenario analysis in that it changes variables, parameters, and/or inputs without creating an underlying reason or narrative for the changes. This gives banking organizations the flexibility to assume a wider range of inputs and parameters than under scenario analysis. Through using sensitivity analysis, banking organizations may gain a better understanding of how their business lines and vulnerabilities will be affected by extreme shocks.

Enterprise-wide stress testing evaluates how certain macroeconomic and firm-specific conditions may affect the banking organization as a whole, rather than specific exposures, portfolios, or business lines. Enterprise-wide testing requires consultation with individuals in different departments and management levels throughout the organization. The guidance recommends using enterprise-wide scenarios to evaluate the viability of the banking organization under prolonged and severe adverse financial conditions. Enterprise-wide scenarios should include a combination of firm-specific, market-wide, and macroeconomic changes. An example of a scenario would be if a price shock increased portfolio losses, which led to a ratings downgrade and limited access to funding. Finally, reverse stress testing assumes an adverse situation, such as insolvency, and applies deductive analysis to find out the possible causes of the situation. For example, a banking organization

⁴ VaR analysis shows the risk of loss on the bank's positions for a given probability and time horizon in a dollar amount.

may assume that it suffers a severe credit loss, which causes it to fall below regulatory capital ratios. The bank then must think beyond its normal business assumptions to create explanations for how such a situation may arise and then create mitigation strategies. Reverse stress testing helps banking organizations explore severe “break the bank” events while disregarding their likelihood to focus directly on evaluating threats to the banking organization’s viability.

Stress Testing Capital and Liquidity

The agencies emphasize how the stress testing principles and frameworks outlined above should be applied to evaluate capital and liquidity adequacy. The guidance gives priority to stress testing capital and liquidity, as these two factors are critical to a banking organization’s viability. Capital stress testing can help banking organizations evaluate the quantity and quality of their capital and how well they can absorb losses. In addition, liquidity stress testing can help banking organizations explore effects such as liquidity shortages, the inability to issue debt, the effect of ratings downgrades on funding, and credit freezes. The guidance further asserts that stress tests should analyze the effects of both capital and liquidity problems arising at the same time. For example, if a banking organization is under liquidity stress due to a macroeconomic shock, it may have to sell assets at a loss, which would decrease its capital holdings.

Finalized and Proposed Capital Requirements for Banking Organizations

On June 7, 2012, the Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (FRB), and Federal Deposit Insurance Corporation (FDIC) (collectively, the agencies) finalized the [market risk rule](#) and released three separate [notices of proposed rulemakings](#) (NPRs) on capital requirements. Altogether, the finalized rule and NPRs aim to

advance regulatory capital standards for U.S. banking organizations by increasing minimum capital ratios and buffers, improving measurements of market risk, and enhancing governance and disclosure requirements. The final rule and NPRs would carry out [sections 171](#) and [939A](#) of the Dodd-Frank Act, which requires the agencies to establish new leverage and risk-based capital requirements and alternative credit ratings, respectively. The final rule and NPRs would also bring U.S. banking organizations into compliance with international capital standards as established by Basel II and Basel III.

Finalized Market Risk Capital Rule

The finalized market risk rule implements the Basel Committee on Banking Supervision’s (BCBS) [2005](#), [2009](#), and [2010](#) market risk rule revisions. The rule improves regulatory capital standards by making risk-based capital requirements more sensitive to market risk, establishing alternative creditworthiness standards, and increasing transparency through enhanced disclosures. The agencies calculate that the final rule will triple capital requirements for exposures in all banking organizations’ trading books from the current level of \$15.8 billion to \$47.4 billion. The higher capital requirements established by the final rule lower the probability of systemic catastrophic losses arising from market risk and decreases the procyclicality of capital requirements by ensuring that banking organizations hold enough capital to survive periods of financial distress.⁵ The rule will take effect January 1, 2013.

Scope of Market Risk Rule

The rule applies to banks and banking holding companies (BHCs) with trading assets and

⁵ Procyclicality refers to policies that intensify financial fluctuations. For example, during recessions, banks may be reluctant to lend in order to retain enough capital to meet requirements; however, this may lead to a credit crunch, which would intensify the recession.

liabilities of at least \$1.0 billion or 10 percent of its total assets. Based on Call Report data as of December 31, 2011, 25 banking organizations fall under this rule. The rule covers trading position assets and liabilities that are held for short-term resale, with the intent to benefit from short-term price movements, lock in arbitrage profits, or hedge trading positions. The rule also covers foreign exchange and commodity positions.

Internal Modeling Standards

The market risk rule requires banking organizations' primary federal regulator to approve of the internal models they use for calculating market risk capital requirements. Internal models must be reapproved if the banking organization extends or changes the models in a way that affects the calculation of trading position or portfolio risks. To ensure that internal models remain relevant and accurate, banking organizations are required to routinely validate their models and to report their findings to the board of directors at least annually. The audit does not need to be done by an external organization, but it must be done by personnel independent from the development, implementation, operation, and management of the models.

Standard and Stressed Value-at-Risk Capital Requirements

The rule requires banking organizations to use internal models to calculate daily value-at-risk (VaR) measures for trading positions. The finalized rule sets the VaR parameters at 10 business days with a one-tail 99.0 percentile confidence level.⁶ The rule also requires banking organizations to use the stressed VaR analysis. The stressed VaR is similar to the standard VaR, but the parameters of the stressed VaR are adjusted to reflect financial stress.

⁶ This means that there must be a 99 percent chance that a banking organization will not lose more than the amount predicted by VaR over the next 10 days.

The stressed VaR analysis must be calculated at least weekly.

Incremental, Specific, and Comprehensive Risk Capital Requirements

In addition to VaR analysis, banking organizations must also calculate incremental risk, which measures a position's or portfolio's price movements due to factors such as, but not limited to, default and credit migration risk. The rule also requires banking organizations to identify the specific risk of trading positions. Specific risk, also known as nonsystematic risk, refers to the risk of loss on a specific position for idiosyncratic reasons. The rule instructs banking organizations on how to measure specific risk and establishes new specific risk weights. The specific risk weights range from 0 percent to 100 percent, depending on the position's creditworthiness. The final rule also introduces new requirements for calculating comprehensive risk, which measures the risk associated with having trading positions in correlated markets.⁷

Market Risk-Based Capital Requirements

The final rule also changes requirements for the risk-based capital ratio, which is the ratio of total capital to market risk. Market risk is measured as the sum of risk-weighted assets (RWAs) and market risk equivalent assets.^{8,9} The final rule maintains the current minimum capital ratio of 8.0 percent but changes how the ratio is calculated by expanding the definition of market risk equivalent assets to also include the stressed VaR, incremental, and comprehensive risk capital requirements

⁷ For information on what qualifies as a correlation trading position, see [Revisions to the Basel II Market Risk Framework, 2011](#).

⁸ RWAs measure a banking organization's assets, weighted according to risk. For more information on risk weights and the general risk-based capital rules, see [12 CFR part 3 appendix A, part 167](#), [part 208 appendix A, part 225 appendix A](#), and [part 325](#)

⁹ Market risk equivalent assets measure the risk of loss resulting from market price movements.

discussed above. The expansion of market risk equivalent assets makes the capital ratio more sensitive to market risk. The final rule further changes risk-based capital ratio calculations by prohibiting banking organizations from including tier 3 capital in total capital.¹⁰

Alternative Credit Standards

The rule deviates from the BCBS market risk rules by avoiding credit rating agencies' creditworthiness ratings. This complies with section 939A of the Dodd-Frank, which requires federal banking regulators to use alternative ratings of creditworthiness. The final rule uses various alternative methods to evaluate the creditworthiness of different positions. For example, to evaluate sovereign debt positions, the rule requires banking organizations to use the country risk classifications data published by the Organization for Economic Cooperation and Development in their models. The rule also provides methods for assessing the creditworthiness of supranational entities and multilateral development bank debt; depository institutions, foreign banks, and credit union debt; public sector debt; and corporate debt.

Governance and Disclosure

The rule requires senior management to approve the scope of a banking organization's trading positions and hedging strategies. The rule also requires banking organizations to establish a risk control unit that is independent of the trading business unit to monitor positions, assess the ability to hedge the position, and determine the extent of market liquidity on a daily basis. On an annual basis, banking organizations must review their established limits on positions and evaluate the soundness of model assumptions and parameters. The rule also implements additional disclosure requirements in order to increase market

¹⁰ Tier 3 capital includes subordinated securities and unsecured debt and has a minimum maturity of two years.

risk calculation transparency. The rule requires banks to publicly disclose quantitative and qualitative information on components of their market risk capital models quarterly.¹¹ The board of directors must approve a banking organization's disclosure policy, and senior management must verify the accuracy of the disclosures.

Proposed Capital Rules

In addition to the final market risk capital rule, the agencies also released three separate capital requirement notice of proposed rulemakings (NPRs) on June 7, 2012. The purpose of the three NPRs is to implement Basel II and III capital reforms and Dodd-Frank requirements. The three NPRs are:

1. Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action ([Basel III NPR](#));
2. Regulatory Capital Rules: Standardized Approach for Risk-weighted Assets, Market Discipline and Disclosure Requirements ([Standardized Approach NPR](#));
3. Regulatory Capital Rules: Advanced Approaches Risk-based Capital Rule, Market Risk Capital Rule ([Advanced Approaches and Market Risk NPR](#)).

The sections below provide a broad overview of the purpose, scope, and proposals of the three NPRs.

Basel III NPR

The Basel III NPR proposes to implement the Basel III Accord's higher risk-based capital and leverage ratio requirements, more stringent capital standards, capital conservation buffers, and

¹¹ This includes, but is not limited to, information on VaR measures and performance; measures of interest rate, credit spread, and equity price; validation methods of internal models; and governance policies for reducing risk.

countercyclical buffers.¹² The Basel III NPR proposes the following minimum capital ratios:

1. A tier 1 capital ratio, which is the ratio of tier 1 capital to total risk-weighted assets (RWA), of 6 percent;
2. A common equity tier 1 capital ratio, which is the ratio of the common equity component of tier 1 capital to total RWA, of 4.5 percent;
3. A total capital ratio, which is the ratio of total capital to total risk-weighted assets, of 8 percent;
4. A tier 1 leverage ratio, which is the ratio of tier 1 capital to average total consolidated assets, of 4 percent; and
5. A supplementary tier 1 leverage ratio, which is the ratio of tier 1 capital to total leverage exposure, of 3 percent¹³

The first four capital ratio requirements apply to all banking organizations, which include depository institutions, bank holding companies with total consolidated assets of \$500 million or more, and savings and loan holding companies. The last ratio applies only to banking organizations that have consolidated total assets of at least \$250 billion or consolidated total on-balance-sheet foreign exposures of at least \$10 billion (referred to as “advanced approaches banking organizations”). The NPR proposes this additional capital ratio for advanced approaches banking organizations because of their greater exposures and systemic importance in the financial industry.

The NPR also proposes more stringent Tier 1 capital qualifications by requiring its dominant component to be voting common stockholders’

equity.¹⁴ The common stockholder equity proposal helps ensure that banking organizations use high-quality capital when calculating their capital ratios.

The NPR also proposes to add an additional capital conservation buffer on top of the minimum capital requirements to help prevent capital ratios from falling below minimum requirements during times of financial stress. The NPR proposes to set the capital conservation buffer, which will be composed of tier 1 common equity, at greater than 2.5 percent of a banking organization’s RWAs.¹⁵ If a banking organization does not maintain the buffer, the agencies can place limits on its capital distributions, such as dividends and bonuses to executive officers. In addition, the NPR proposes a countercyclical buffer for advanced approaches banking organizations as a precaution against systemic banking failure in adverse financial conditions. The countercyclical buffer proposal gives regulators the authority to increase the capital conservation buffer up to an additional 2.5 percent during favorable economic conditions so that these banking organizations will have the capital to weather adverse conditions. The countercyclical buffer will initially be set at zero, and any increase will be announced 12 months prior to implementation. The Basel III NPR would be implemented gradually between 2013 and 2019.

Standardized Approach and Advanced Approaches and Market Risk NPRs

The Standardized Approach NPR applies to the same institutions as the Basel III NPR. The Standardized Approach NPR proposes to enhance the risk sensitivity of RWAs by increasing the number of risk weight categories and risk weights of exposures. Currently, the risk weights used for

¹² The Basel III Accord was published by the Basel Committee on Banking Supervision in December 2010 and revised in June 2011.

¹³ The NPR proposes to adopt the same definition of total leverage exposure as in the Basel III Accord. For information on the calculation of total leverage exposure, see [Basel III, Section V, part B.2.](#)

¹⁴ Voting common stockholders’ equity is composed of common stock plus retained earnings.

¹⁵ The capital buffer would increase the tier 1 capital ratio to 8.5 percent, the common equity tier 1 capital ratio to 7 percent, and the total capital ratio to 10.5 percent.

calculating capital requirements range from 0 percent to 100 percent. The NPR proposes to revise this range from 0 percent to 600 percent. When assigning risk weights, the NPR considers characteristics such as creditworthiness, obligor type, delinquency status, and underwriting attributes.

The Advanced Approaches and Market Risk NPR applies only to advanced approaches banking organizations and proposes to revise counterparty risk models, securitization exposure calculations, and risk weights. The NPR proposes to revise counterparty risk calculations by implementing more stringent criteria on what qualifies as financial collateral and stressing counterparty risk model inputs.¹⁶ The NPR also proposes to redefine security exposures to include indirect securitization exposures to broaden the scope of activities considered when calculating market risk. The NPR also proposes to increase the risk weight used to calculate the RWAs of certain securitization exposures. Furthermore, the NPR proposes to expand the scope of the finalized market risk rule and current advanced approaches rules to include federal and state savings associations and savings and loan holding companies.

The Standardized Approach and Advanced Approaches and Market Risk NPR are similar in that they both propose to increase disclosure requirements and use alternative credit rating methods. The Standardized Approach disclosure proposal applies to top-tier banking organizations with \$50 billion or more in total assets, whereas the Advanced Approaches and Market Risk disclosure proposal applies only to advanced approaches banking organizations. The NPRs would require these banking organizations to disclose information

such as corporate and capital structure, securitization and investment activities, and interest risks of nontrading activities. Furthermore, both NPRs propose to use the same alternative credit rating methods as the finalized market risk rule in order to comply with section 939A of the Dodd-Frank Act. Comments on all three NPRs are due by September 7, 2012.

¹⁶ The proposal revises the definition of financial collateral to exclude less liquid collateral such as re-securitizations, conforming residential mortgages, and non-investment-grade debt securities

Federal Regulation

Multiple Sponsors

Swap Definitions and Regulation

On April 18, the Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC) issued a [joint final rule and interim final rule](#) to define certain swap activities and participants. The rules implement Title VII of the Dodd-Frank Act, which directs the SEC and CFTC to regulate over-the-counter (OTC) derivatives. The final rule defines the terms swap dealer, security-based swap dealer, major swap participant, and major security-based swap participant. The interim final rule establishes exclusions from the definition of swap dealer. Entities that fall under at least one of these definitions must register with either the SEC or CFTC and comply with new OTC derivative regulations. The sections below discuss the definition of these terms and the scope of the two agencies' authority. The final rule and the interim final rule became effective July 23, 2012.

Title VII of the Dodd-Frank Act grants the CFTC and the SEC the authority to govern swap dealers and security-based swap dealers, respectively.^{17, 18} The final rule defines a swap dealer (and security-based swap dealer) as someone who is a dealer in swaps (or security-based swaps); creates a market in swaps (or security-based swaps); regularly enters into swaps (or security-based swaps) with counterparties; or engages in activities known in the trade as a dealer or market maker in swaps (or security-based swaps).

The final rule exempts swap dealers and security-based swap dealers from regulation if they fall below certain monetary thresholds. The threshold is set at \$3 billion notional per year for swaps and security-based swaps that are credit default swaps and \$150 million notional for other security-based swaps.¹⁹ The interim final rule establishes further exemptions by excluding swaps entered for hedging commodity positions from being considered when determining swap dealer status. For example, an airline that uses a swap to hedge against changes in fuel prices would not be considered a swap dealer. The rationale for this exclusion is that swaps entered for hedging purposes are entered by end-users on their own behalf rather than on behalf of third parties or for speculation, and thus swaps for such purposes are not considered dealing activities.²⁰ Comments on the interim final rule were due July 23, 2012.

Title VII of Dodd-Frank also directs the CFTC and SEC to regulate major swap participants and major security-based swap participants, respectively. Major participants are subject to CFTC and SEC regulation because of their potential systemic risks. The final rule defines a major swap and major security-based participant as someone who is not a swap or security-based swap dealer and who satisfies any of the three following conditions:

- Someone who maintains a "substantial position" in any of the major categories of swaps or security-based swaps, excluding positions held for the purpose of hedging or mitigating commercial risk;

¹⁷ A swap is a type of derivative in which two parties agree to exchange cash flows of financial instruments. A few examples of common swaps are interest rate, currency, commodity, and credit default swaps.

¹⁸ A security-based swap is a swap that is either based on a single security, a loan, or a security index.

¹⁹ During the phase-in period, the threshold for swaps and security-based credit default swaps is set at \$8 billion and \$400 million, respectively. The phase-in period will automatically expire after five years.

²⁰ Swaps entered for hedging physical positions are defined in the CFTC's [Commodity Exchange Act, Section 1.3\(ggg\)\(6\)\(iii\)](#).

- Someone whose swap or security-based swap positions create “substantial counterparty exposure” that could threaten the stability of financial markets; or
- Someone who is a nonbank financial entity that is “highly leveraged” relative to its capital and maintains a substantial position in any of the major categories of swaps or security-based swaps.²¹

Memorandum of Understanding on Supervisory Coordination

On Jun 4, the five federal supervisory agencies—the Consumer Financial Protection Bureau (CFPB), the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC) the National Credit Union Administration (NCUA), and the Office of the Comptroller of the Currency (OCC)—released a [memorandum of understanding](#) (MOU) on coordinating supervision over insured depository institutions with more than \$10 billion in assets. The MOU was released in compliance with section 1025 of the Dodd-Frank Act, which requires the five agencies to coordinate their supervisory activities. The MOU discusses how the agencies will coordinate examinations and share information regarding compliance with federal regulations on consumer financial products and services; consumer compliance risk management programs; activities related to consumer financial products or services; and other related matters the agencies may later agree to share. The MOU aims to streamline supervision among the agencies and decrease the burden on regulated depository institutions.

TALF Credit Protection Reduction

On June 28, the Federal Reserve Board of Governors (FRB) and the Treasury [announced](#) a reduction in credit protection for the Term Asset-Backed Securities Loan Facility (TALF) from \$4.3 billion to \$1.4 billion. The decision to decrease credit protection was motivated by the decrease in outstanding TALF loans. The FRB created TALF during the financial crisis to encourage credit lending, especially in asset-backed securities markets. To encourage credit lending, the New York Federal Reserve lent \$71 billion under TALF to investors in highly rated asset-backed securities (such as auto, student, credit card, and small business loans) and commercial mortgage-backed securities. TALF began operation in March 2009 and ended June 2010. When the program ended in 2010, outstanding TALF loans totaled \$43 billion, and the FRB agreed to guarantee \$4.3 billion of the debt. Since then, outstanding TALF loans have dropped rapidly as borrowers finished paying off the loans. As of June 20, 2012, outstanding TALF loans totaled \$5.3 billion.

Federal Reserve

Supervision of Securities Holding Companies

On June 4, 2012 the Federal Reserve Board of Governors (FRB) released the [finalized procedures](#) for how securities holding companies (SHCs) voluntarily elect to be supervised by the FRB.²² An SHC may elect to be supervised by the FRB in order to comply with regulatory requirements of foreign countries in which the SHC operates. The final rule explains that to register for supervision, the SHC must submit information on its organizational structure, subsidiaries, upper management personnel, internal regulations, and financial statements to the FRB. Once the information has been submitted, the SHC will be registered as an FRB-supervised entity in 45 days or less. A registered SHC will be supervised similar to a banking holding company (BHC), which means that the SHC must submit the same reports and undergo the same supervisory

²¹ The final rule defines the terms “substantial position,” “substantial counterparty exposure,” and “highly leveraged” using various quantitative metrics and thresholds.

²² An SHC is a nonbank that owns at least one registered broker or dealer.

and examination procedures described in the [BHC Act](#). However, an SHC will not be subject to the same nonbanking restrictions described in section 4 of the BHC Act. The rule became effective July 20, 2012.

Consumer Financial Protection Bureau

Privileged Bank Information Protection

On June 28, the Consumer Financial Protection Bureau (CFPB) [finalized the rule](#) that codifies the protection of privileged banking information it collects for supervisory purposes. This rule was adopted to assure financial institutions regulated by the CFPB that privileged information will not be subject to waivers authorizing disclosure to third parties. This rule gives privileged information submitted to the CFPB the same statutory protections as information submitted to prudential regulators. The rule will be effective 30 days after publication in the *Federal Register*.

Department of the Treasury

Bank Assessment Fees

The Treasury Department released a [final and interim final rule](#) to implement section 155 of the Dodd-Frank Act on May 21. The final rule imposes assessment fees on bank holding companies (BHCs) with total consolidated assets of \$50 billion or more. The assessment fees will cover the expenses for the Office of Financial Research, the Financial Stability Oversight Council, and certain Federal Deposit Insurance Corporation activities, all of which were previously funded by the Federal Reserve. It explains that assessment fees will be collected semi-annually, with the first collection set for July 20, 2012. The fee rates will be published a month before collection, and values will range from \$280,000 to \$12.5 million for every \$100 million, depending on the total consolidated assets of the company. The interim rule applies to nonbank financial companies supervised by the Federal Reserve Board of Governors. The interim rule subjects these nonbank financial companies to the same fees as BHCs, however, is waiting for additional comments from the Financial Stability Oversight Committee.

Securities and Exchange Commission

Clearing Agency Supervision

On June 28, the SEC released a [final rule](#) explaining how it will review clearing agencies' security-based swaps clearing procedures. Title VII of the Dodd-Frank Act grants the SEC authority to determine which security-based swaps must be cleared by a clearing agency.²³ By supervising clearing agencies, regulators can gather information on various transactions and positions. Under the final rule, clearing agencies must submit quantitative and qualitative information to the SEC on any type of security-based swap that they plan to clear.²⁴ The rule also requires systemically important clearing agencies to submit advance notice to the SEC if they make any changes to rules, procedures, or operations that may affect risk management practices or core functions. The Dodd-Frank Act gives the Financial Stability Oversight Council the authority to decide whether a clearing agency is systemically important.²⁵ The final rule will be phased in starting 60 days after publication in the *Federal Register* and will be completely phased in by December 10, 2012.

²³ For the definition of a security-based swap, see footnote 18.

²⁴ Required information includes, but is not limited to, the amount of outstanding notional exposures, liquidity, and pricing data; credit support infrastructure; effect on systemic risk; effect on competition; and insolvency plans. The rule requires clearing agencies to publish submissions on their public websites within two business days.

²⁵ For information on the criteria that the Financial Stability Oversight Council uses to evaluate the systemic importance of a financial institution, see [Authority to Designate Financial Market Utilities as Systemically Important](#).

Office of the Comptroller of the Currency

National Bank and Savings Association Lending Limits

On June 21, the Office of the Comptroller of the Currency (OCC) published [the interim final rule](#) on lending limits for national banks and savings associations to implement section 610 of the Dodd-Frank Act. The interim final rule affects lending limits by expanding the definition of loans and extensions of credit to include credit exposures from repurchase and reverse repurchase agreements, securities lending transactions, and securities borrowing transactions (referred to collectively as securities financing transactions). As a result, banks now need to include the amount of their exposure to securities financing transactions in their calculation of loan limits. Comments on the interim rule were due August 6, 2012. Banks and savings associations have until January 1, 2013, to comply with the interim rule.