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Financial Institution Accounting: Changes for 2011

by Ivy M. Washington, Supervising Examiner

The accounting world is always changing. Recent proposals to some accounting practices may touch Third District financial institutions, so this article discusses some of those proposals, related reporting requirements, and supervisory implications recently issued by the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB).[1] It also highlights other accounting considerations being proposed in 2011.

New Accounting Proposals

Accounting Treatment of Financial Instruments

The accounting treatment of financial instruments has been the topic of much deliberation for the FASB. In May 2010, the FASB issued an exposure draft entitled "Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities."[2] Proposal comments received by the FASB by the September 2010 deadline (over 2,800 letters) were overwhelmingly negative, as the majority of the feedback centered on the more controversial elements of draft—the proposed requirement to measure loans at fair value and to impose artificial limits for the estimate of expected credit losses. A decision under the impending standard is the classification and measurement of certain financial assets to be valued at amortized cost rather than fair value. This decision would include most "plain vanilla" assets held for investment loans resident on a financial institution's balance sheet.

In light of this negative feedback, it is understandable that the final standard significantly differs from the proposal. One part of the standard where it seems the FASB has changed its direction is the classification and

[1] www.fasb.org.

[2] "Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities," FASB, May 26, 2010, www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175820761372&blobheader=application/pdf.

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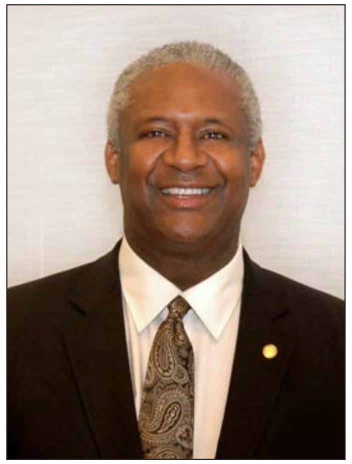
Supervision Spotlight on Michael E. Collins



Executive Vice President Mike Collins has written a Supervision Spotlight in every issue of *SRC Insights* since its inception 16 years ago. After serving the Federal Reserve Bank of Philadelphia for 37 years, he has decided to retire from the Bank, effective June 1, 2011. Throughout his tenure, Mike has seen various peaks and valleys in the nation's financial system. His perspectives on banking, the economy, and the Federal Reserve offer great insight into how strong leadership can help an institution overcome difficult challenges. For this, his final "Spotlight," the tables are turned, and he becomes the subject, not the author, of this regular feature.

Integrity in Supervision

Though it is rare for a leader to remain in one business area for the duration of their career, Mike has done just that, starting as an assistant bank examiner and working his way to executive management. He has been an instructor at the Board of Governors, led business and technology special projects, worked in collaboration with various departments and other Reserve Banks, led Systemwide projects, and even served as a consultant for the Central Bank of Trinidad and Tobago. As the bank's chief lending officer, he has also been responsible for oversight of Discount Window operations.

What has helped him to stay interested in the business for such a long time? Part of it is his desire to take on new challenges and accept risk. "A way to keep fresh, even if you're in the same area," he says, "is to say 'I'll take that on, I'll do this.' The ability to continuously rebuild yourself and get exposure to new things keeps you fresh. I make it a habit to continuously scan the business environment to gain fresh perspectives on things and understand the megatrends that impact our work."

Mike's career at the Federal Reserve is a testament to both his personal motivation and his commitment to banking supervision, a function that he believes reaches beyond the economy. To Mike, banking supervision impacts much of society, whether it's economic in terms of financial conditions and financial stability or social in terms of the ability to ensure integrity in consumer transactions and fair and equal access to credit. And while the function has certainly evolved to meet ever-changing needs, many of the fundamentals remain the same as when he first became an examiner. "At the end of the day, our mission as a central bank supervisor hasn't changed," he says. "Our mission in supervision is still to promote safe and sound banking through effective supervision and to ensure consumer protection so that there's integrity in our financial system."

The biggest change Mike has noted throughout his career is an expanded emphasis on consolidated supervision and the integration of risk management and corporate governance to facilitate effective oversight at financial institutions. Consolidated supervision of financial groups is one of the most challenging endeavors bank supervisors can face as firms grow in complexity, geographic footprint, and size. A more recent trend is the emphasis on macroprudential supervision as a complement to firm-specific supervision. This means a more explicit consideration of threats to markets and the stability of the financial system as a whole, together with traditional supervision and regulation. Another trend is the expanded integration of consumer protection and financial stability, which became very evident during the recent financial crisis.

During his career, Mike has also noted significant changes in the types of products available across the industry, the increased use of technology in product delivery, and sophistication in data mining and risk management. There is more complexity, and technology has transformed the industry in many ways, especially regarding more customized products. But in the midst of such developments, certain responsibilities, such as sound credit underwriting, disciplined but innovative thinking, and strong management information systems remain important for bank management.

"Concentrations are always important, and as a result of the crisis, we are much more aware of their propensity to cause problems if not prudently managed," he says. This includes concentrations on both the asset and liability or funding side. Mike notes, "I also think integrity is still critical and avoiding conflicts of interest. Banks and banking supervisors should never lose sight of the important role of a financial intermediary in serving customers and the critical nature of the public's trust as it relates to reputation risk and confidence in our financial system. In addition, the need to think in a more integrated or interdisciplinary fashion is also now a staple of effective supervision. A number of things may change, but many things are still fundamental in what makes a good financial system, a good bank, or a good supervisor."

These fundamentals are what help SRC provide its institutions with a more consistent, firm, but fair application of supervision throughout the various cycles.

Experience in Crisis

During his tenure, Mike has worked through numerous business cycles, including the most recent financial crisis. Mike notes that these events throughout his career have been different, but also have some similar core features, such as financial imbalances, credit imperfections, and excess leverage, and they are usually preceded by periods of complacency and deregulation. These crises are usually resolved in three stages. When a crisis emerges, initially there is a containment phase designed to address and contain problems in the financial markets, such as central bank intervention to alleviate interbank liquidity strains. A second step centers on loss recognition, restructuring, and recapitalization. Finally, a third stage seeks to implement fundamental reforms. This is a long process, but it should ultimately strengthen the financial system and improve the way the system responds to future crises.

The impact on our financial system can be longstanding. For example, it took a decade for the banking industry to fully recover from the commercial real estate crisis in the early 1990s. The S&L crisis of the 1980s resulted in the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) and numerous changes in bank supervision.

In response to the 1990s crisis, Mike created SRC's Enforcement Unit, a dedicated team, to oversee the 20 or so struggling banks that required more supervision. The unit became an early example of outreach, helping SRC explain to institutions what happens when things don't go well. Mike explains that, "Whenever you have problems in the industry, such as the financial crisis or the S&L crisis, Congress enacts laws to make sure that future risks are mitigated. So, we had a lot of new legislation that we had to implement and receive that was designed to try to prevent this from happening again, with some areas of measurable success." Much like today, as SRC implements the Dodd-Frank Act, the challenge is to balance a stronger set of financial industry and consumer protections with the need for innovation.

Mike has learned that when hard times fall, it's not just the technical work that needs to be assessed, but the human side of things. In 1992, he saw the first Third District state member bank failure occur since the 1940s. The bank was very customer-oriented, but it had weak internal controls, and fraud occurred, which led to the failure. As expected, detailed conversations amongst staff followed, expressing what could have been done differently and why it happened. But the part that Mike recalls most vividly is the impact on the bank's employees, management team, and directors.

"In many instances, as supervisors, we can look at these events in isolation," Mike says. "But to look at the impact on employees who lost their jobs, a management team who was shocked at what happened, and directors who had committed huge financial resources to keep the bank open, it gives you an idea about the human aspect of this work."

When the events of September 11, 2001, occurred, Mike was at the Board of Governors in Washington, D.C., but he met with his staff via conference calls. Mike emphasized the importance of keeping the financial system functioning, but also ensured that the safety of employees was given equal priority. During critical periods like September 11, strong communication is essential, as staff look to their leaders to set the tone for response to events.

"Leading in a crisis situation requires a combination of skills and behaviors, both professional and personal," Mike notes. "The primary role of a leader is to build effective teams, inspire trust, and motivate staff to discover answers to our most difficult questions. Leaders must also ensure that the basic or mechanistic aspects of running the business are in place for an organization to run effectively and efficiently. After this foundation is laid, leaders are free to focus on the organic activities or the more human aspects that emphasize flexibility, creativity, and new ways of doing things. A model and culture of collective leadership is essential to navigating through tragedies like September 11."

Keeping SRC Vibrant

Another component that Mike has learned is the importance of quality of financial sector supervision as a way of ensuring that the industry and Third District banks are resilient enough to get through credit and business cycles. This requires appropriate resources, authority, and constructive relationships with other agencies, together with the will to act. In addition, this often means delivering difficult messages in a timely manner.

"When you're in a crisis, you really don't have time to reflect," he says. "You're dealing with the issues in front of you. Even though we're still challenged by the issues that arose from the crisis, I make time for reflection, so that SRC is positioned for continuous improvement."

As part of that reflection, Mike notes that, to ensure that SRC has an effective supervisory response to future dislocations, it needs fresh ways of thinking about financial markets, risk, and consumer protection. One objective going forward will be to ensure that the necessary data are readily available to make educated decisions about complex and interconnected markets. Greater attention will also be given to reducing cyclical tendencies that tend to exacerbate problems. There will also be an increased focus on capital and liquidity reforms, as well as firmwide risk management. These changes are aimed at reinforcing banks' capital buffers and liquidity standards to help the system better withstand future crises. The cumulative effect of changes can adversely impact bank lending if not applied prudently. Therefore, policymakers will need to consider transitional periods as rules are implemented.

As the department continues to evolve and grow from such varied experiences, Mike finds it is increasingly important to take time to reflect on successes, too. He advises staff to step back and picture the future, to give themselves a compelling view of what it should look like in order to help them work toward a goal and succeed. For instance, he reflects on some of the many innovations that have occurred during his tenure, including the implementation of the Retail Risk Analysis Unit, the Infrastructure Office, the Partnership for Progress program, and *Consumer Compliance Outlook*. "All of those things really reflect important initiatives because they allow the department to grow. They've helped transform the department to keep it vibrant while maintaining our focus on core supervision."

Even as times change, the department's biggest asset will continue to be its people. New staff members make up a large part of the team, and Mike believes the department's strong reputation in the Bank and System makes it attractive to employees. "I think people like working for a place that is well-regarded. The biggest factor distinguishing strong performance at firms is the quality of its people. It's a competitive advantage to have the right staff that has the capacity to execute and perform well." Again, the "human side" of the work is a focal point, telling people that their contributions are noticed, ensuring employee engagement, and building a sense of community. For Mike and SRC, it's about being an integral part of our nation's central bank and contributing to a sound banking system and strong regional economy. This is the essence of public service.

SRC's outreach programs and publications provide an ideal venue to share perspectives and facilitate the exchange of valuable feedback regarding policy.

Important Conversations

While the department has evolved alongside Mike's career, so has its relationship with bankers. Mike has been a big proponent of outreach events, such as Bankers' Forums and Directors' Workshops. SRC's outreach efforts have been instrumental, and Mike values the benefits of such open dialogue.

SRC's outreach programs and publications provide an ideal venue to share perspectives and facilitate the exchange of valuable feedback regarding policy. "We can all learn, and we should all learn all the time," he says. "At the end of the day, we all want the same thing: a safe and sound banking system that includes a strong value proposition for consumers."

To Expect More, Be More

Creating and maintaining safety and soundness requires strong leadership, and Mike has certainly honed such leadership skills in his 37 years. Though the Fed is an expertise-oriented organization where technical skills are key, he believes a desire for intellectual curiosity is vital for a leader. In addition, team-building skills are crucial; building the right teams and understanding how teams work help leaders set a tone and provide direction toward a shared vision. Leaders need to be able to paint a picture of the future, align staff with the mission and values of the organization, and let them lead.

But leaders can't be afraid to repeat themselves; people need clarity around a mission or strategy to adopt it. On the other hand, listening can have a great impact. "You need to be accessible for your staff," Mike has learned. "When you do that, people understand that you are in the moment with them, that you're invested in what they're doing, and that you want to see them succeed. It's important to support their dreams and aspirations."

Another trait Mike finds important to leaders is the ability to learn from failure. "It's easy to love learning, and it's fun to dream, but dealing with unexpected setbacks is the real challenge in life," Mike remarks. "When you have passion about high standards and striving for excellence and are willing to put in the time and effort, you can be a role model for the type of work ethic you want. I always try not to expect more from my staff than I expect of myself."

There is a well-known story in the Federal Reserve of a bank president who was once asked the secret of his success. "Right decisions," he replied. The follow-up question was: "How do you know how to make right decisions?" "Experience," was his answer. "Well, how do you get experience?" asked his interviewer. His reply? "Wrong decisions."

History has shown that even the most successful people experience failure. Mike believes that people should live their lives with a good amount of pragmatism, a recognition that, if one approach does not work, another might. It is not the absence of failure in life, but rather one's response to failure that matters. "Failures are great teachers," Mike notes. "If you never fail, you never learn, and if you never learn, you will never grow." Failure also teaches empathy for others. Without that, people may be prone to the arrogant notion that they are self-sufficient and superior, when in fact, they may just be lucky—for the time being.

The Mold of a Role Model

So who were the leaders in Mike's life that inspired him? His parents set the foundation, keeping him focused on life-long learning, work ethic, character, and motivation. "They really kept me grounded," Mike says. "When I was growing up, it wasn't cool to be smart in high school. You were supposed to sit there and not participate. If I'd actually started to value those traits, I'd go home, and they'd bring me back to reality."

He also admires the perseverance of Nelson Mandela, as well as the integrity and intellect of people like Colin Powell. He deeply appreciates the confidence in him that Philadelphia Fed President Ed Boehne showed by putting him in the position to run the department.

As he leaves the Fed, Mike reflects on the colleagues and bankers who have worked with him and shared his vision. He is grateful for people who embraced him as a leader and worked hard to achieve successes. He hopes that his legacy is one of a professional, balanced, consistent voice who helped people to understand the rules and also to grow. "I think the main goal is to make sure that people have very productive lives and meaningful lives and are capable of taking care of their families; that they like what they do; that they feel good about coming into work every day; and that they see that they benefit our District, our industry, and society at large. I hope people feel that the time I've spent here has been mutually beneficial for them and the department."

Mike also hopes to inspire other African-Americans and other minorities in the department and in the System to know that they can achieve meaningful leadership roles in the Central Bank. "The door is open to anyone who is trying to achieve things and is willing to put the work in," Mike says. It is well-known that the best organizations and teams are diverse ones. "As a nation, we need everyone contributing at an optimum level if we are to be great."

SRC's Next Chapter

Transitions are rarely easy, but they represent opportunity. When he transitioned to senior officer in 1994, Mike was the first new leader in 25 years. While one goal was to honor the legacy of his predecessor, he also wanted to excite staff about the future. Understanding people and their motivations and knowing what is important to his stakeholders helped him to establish a foundation for leading the department. "It took me a while to understand that you can't just put your head down and work hard," he admits. "You have to understand the informal channels."

As for SRC going forward, he believes the department should continue to do the things it does very well and to stay invested in and focused on the idea of continuous improvement. "If you're not always learning and reinventing yourself and thinking about new ways or better ways to do things, you fall behind," he says. He has worked to create an environment of collective leadership and to recognize staff for their leadership roles. "I try to give people the tools and create conditions for them to be successful," he says. "I enjoy watching people succeed at things and getting recognized for that."

Mike is optimistic that he is leaving SRC in good hands. Senior Vice President Bill Lang succeeds him as just the third leader of the department in nearly 42 years. The two share many of the same values, and they have worked together for nine years, which will make the department's transition as smooth as possible. "I hope Bill will take from me the types of things that he thinks are valuable and can leverage going forward. He is invested in the legacy of the department and keeping it strong," Mike says. "He's the right person at the right time. And now is the time for him to take the department forward."

As Bill leads SRC in opening its next chapter and Mike opens his own next chapter, SRC is poised for success with fresh leadership and a strong legacy. Mike feels it is time to do something new and to give other people opportunities that he was given. He leaves with a good feeling about the reputation of the department that he has shaped for so long. "I think we have a lot of great people, with great momentum," he says, "The future is bright." ■

From the

Examiner's Desk

Municipal Bonds: The Importance of Understanding Institutional Exposure

by Becky Goodwin, Examiner

With so much buzz in the media about the recession, recovery, congressional stalemates, and state and local budget cuts, it's no coincidence that the municipal bond market is being scrutinized by investors and strategists alike. Many believe the municipal bond market may be an area of emerging risk, given today's national economic environment. This article highlights current concerns associated with municipal bonds, defines credit risk and the criteria used by rating agencies, and revisits board and senior management responsibilities regarding investment portfolio management.

What is a Municipal Bond?

Essentially, a municipal bond is a loan made to a state or local government body. It is also referred to as a tax-exempt bond, since the interest paid to investors is not subject to federal, state, or local tax (some states, however, only exempt interest if the bond is issued in the state). According to www.publicbonds.org, "What makes a bond different from other loans is that it is a security that can be bought and sold and has a value that fluctuates. Debt securities with a maturity of 13 months or less are known as *notes*. The maturity of bonds is most often 30 years."[1] Municipal bonds have typically been considered a relatively stable investment, following securities issued by the federal government.

Types of Municipal Bonds

Risks vary based on municipal bond type. General obligation bonds are thought to carry less risk, as they are supported by the full faith, credit, and taxing authority of the issuing government, while revenue bonds are supported by revenue streams generated through user fees or lease payments associated with specific projects. Therefore, revenue bonds issued on behalf of private entities are characteristic of additional risk, as private organizations can declare bankruptcy, making them unable to service debt obligations, yet under no legal obligation to pay the debt.

Why the Concern?

According to CNBC.com writer Paul Toscano, it is a cause for some guarded concern that many banking organizations include municipal bonds in their investment strategies and portfolios.[2] This is with good reason, as municipal bonds are issued by a city, local or state government and have long been identified as among the safest investment options in the country. The financial crisis, however, has triggered a drop in revenue and fewer bond payments for some local governments than expected.

Consulting firms and others have also weighed in on what they view is an impending issue. Consulting firm Roubini Global Economics expects nearly $100 billion in municipal bond defaults in the next five years, due to state and local government debt issues from the recent recession.[3] Martin Hutchinson, contributing editor to *Money Morning*, indicates that the problem facing the municipal bond market is the emergence of the "deadbeat state," citing the beating that state and local government finances have taken during this economic downturn in particular. Making matters worse, Hutchinson cites larger debt loads in states, which cannot be covered due to the reduced property tax stream resulting from record housing defaults.[4]

[1] "Bond Basics," June 2004, www.publicbonds.org/bond_basics/bond_basics.htm.

[2] Toscano, Paul, "Municipal Bonds at Greatest Risk of Default," www.cnbc.com/id/35818485/Municipal_Bonds_at_Greatest_Risk_of_Default?slide=1.

[3] Corkery, Michael, "Muni Default Estimate: $100 Billion," *Wall Street Journal*, March 2, 2011, online.wsj.com/article/SB10001424052748703409904576174933066991472.html.

[4] Hutchinson, Martin, "Municipal Bond Forecast: Deadbeat States Emerge as Biggest Threat to Muni-Bond Investors," *Money Morning, January 26,*

While some predictions suggest that states will have budget deficits nearing $127 billion through 2012, the Center on Budget and Policy Priorities proposes that the numbers could actually be much worse. At mid-year 2010, 48 states faced fiscal-year shortfalls of 30% of their budgets, totaling $200 billion. This is the largest gap in recorded history, and the problems are likely to continue into—and, perhaps, beyond—the next fiscal year. In the end, such state budget shortfalls for 2011 and 2012 may reach $260 billion.

Many feel that the political climate and larger budget issues facing the nation will impact any assistance for fiscally-troubled states. According to Erskine Bowles, co-chairman of the National Commission on Fiscal Responsibility and Reform, "States expecting Congress to authorize more assistance are going to be left with a very large hole to fill."[5]

> ***Fact Check:*** *Municipal bonds default less than company debt; Moody's stated that "the average failure rate for investment-grade municipal debt from 1970 through 2009 was 0.03%, compared with 0.97% for similar corporate bonds."*[5]

The Significance of Rating Agencies and Bond Insurers

Both the rating of a municipal bond and underlying insurance coverage can make purchasing a bond more appealing to an investor. Even so, given the credit crisis, relying solely on the rating and/or insurance is not without question. Both rating agencies and bond insurers have come under additional scrutiny as a result of the huge losses that followed the subprime mortgage crisis in recent years.

One of the most important steps is to identify the credit risk. Investorwords.com defines credit risk as "the possibility that a bond issuer will default by failing to repay principal and interest in a timely manner. Bonds issued by corporations are more likely to be defaulted on, since companies often go bankrupt. Municipalities occasionally default as well, although it is much less common."[6]

Credit risk can occur when a government entity issues a bond and then experiences economic or political difficulties that prevent it from paying interest or returning the principal. To protect oneself against such credit risk, a bondholder can review the credit rating of a bond issue and/or only purchase insured bonds. These are important steps to help ensure a successful return.

In determining credit risk, most investors rely heavily on the credit rating issued by the rating agencies Fitch, Moody's, and Standard & Poor's. When assigning a rating for general obligation bonds, these agencies assess a government entity's economic/financial condition, debt structure, demography, and management practices. Such criteria are also used in analyzing revenue bonds and lease obligations, in addition to considering other credit factors and the bond document's covenants and protections.[7]

WM Financial Strategies provides the table on the next page, which compares the investment-grade ratings of the three major ratings agencies.

All bonds rated BBB-/Baa3 and above are considered investment grade, meaning they are expected to meet their debt service obligations in full and on time. Average ratings for state and local governments, respectively, are in the AA/Aa and A categories.

In his article, "Can You Trust the Rating Agencies," Municipal Credit Analyst Jay Abrams indicates that the spotlight is now on the rating agencies themselves, as a result of Senate hearings on their role in rating debt backed by subprime real estate.[8] This leads investors to question whether municipal bond ratings should also be called into question. Not long ago, Moody's and Fitch announced "recalibrations" of their municipal ratings to bring them in line with their corporate counterparts.

2011, moneymorning.com/2011/01/06/municipal-bond-forecast-dead-beat-states-emerge-as-biggest-threat-to-muni-bond-investors/.

[5] Miller, Don, "State Budget Crises Threaten U.S. Economic Recovery," *Money Morning, July 16, 2011,* moneymorning.com/2010/07/16/state-budget-crises/.

[6] www.investorwords.com/1210/credit_risk.html.

[7] "Municipal Bond Ratings," WM Financial Strategies, www.munibondadvisor.com/rating.htm.

[8] Abrams, Jay H, "Can You Trust the Rating Agencies?," May 17, 2010, www.fmsbonds.com/News/bond_article.asp?id=353.

	Moody's	Standard & Poor's	Fitch
Best Quality	Aaa	AAA	AAA
High Quality	Aa1 Aa2 Aa3	AA+ AA AA-	AA+ AA AA-
Upper Medium Grade	A1 A2 A3	A+ A A-	A+ A A-
Medium Grade	Baa1 Baa2 Baa3	BBB+ BBB BBB-	BBB+ BBB BBB-

This action was widely seen as recognition that municipal bonds, with their extremely low default rates, were rated too low in comparison with much riskier—but higher-rated—corporate bonds.

The role of the bond insurer is equally important, as it promises to repay bondholders or investors in the event of a default. Bond insurers utilize their AAA credit ratings to guarantee lower-rated debt issued by public municipalities. However, the bond insurer must maintain sufficient capital to cover any potential defaults; as increased defaults are predicted, this becomes much more important. Credit rating agencies have downgraded the bond insurer ratings when the insurer's risk exceeds its capital levels.

Marketwire issued a press release in February 2011 outlining the results of the Bedford Report.[9] Highlights from this release mark critical factors for today's municipal bond market.

- Because insurers hold up to two-thirds of their assets in bonds, they are extremely sensitive to credit market conditions.
- Analysts predict downside pressure on these companies due to weak underwriting, weak investment portfolios, and reduced income from the variable annuities.
- Standard and Poor's announced nine new categories. Companies must now raise additional capital and lower their risk to earn high investment grades. (Note: This change is a response to many companies whose AAA investment grades were reduced during the recent crisis. One large bond insurer even had to restructure due to the extent of the crisis.)
- After giving high ratings to financial instruments whose value plummeted during the credit crisis, S&P also changed the criteria for mortgage-backed bonds and other securities.

Despite concerns surrounding bond insurers, municipalities recognize the importance of maintaining insurance for increased investor appeal. State and municipal governments often face tight budgets. Many are even having difficulty paying for their police, fire, schools, and other basic services. One place where municipalities cannot cut back, however, is insurance. "Budget deficits have been a big issue but I think people need to be careful and make sure they are covered and can pay losses if they occur. There is a possibility of a claim that could be a lot bigger than the cost of insurance," notes Susan Kostro, an insurance executive.[10]

Board and Senior Management Responsibilities

Most institutions maintain policies that restrict and limit the amount or types of investments. The heightened level of concern about municipal bonds underscores the importance of board and senior management responsibilities specific to investment portfolio management. Ultimately, the board of directors is responsible for approving the institution's risk tolerances.

In light of the recent headlines and attention given to municipal bonds, the rating agencies, and insurers, board and senior management should be prepared to

[9] "Ambac & Assured Guaranty Continue to Face Analyst Scrutiny: The Bedford Report Provides Analyst Research on Ambac Financial & Assured Guaranty," Marketwire, press release, February 4, 2011, www.marketwatch.com/story/ambac-assured-guaranty-continue-to-face-analyst-scrutiny-2011-02-04.

[10] O'Connor, Amy, "Public Entities and Their Insurance Providers Adjust Sails in Fiscal Storm," February 10, 2011, www.mynewmarkets.com/articles/180376/public-entities-and-their-insurance-providers-adjust-sails-in-fiscal-storm.

take inventory of their institution's municipal exposure. A review of municipal exposures should begin with the balance sheet and include investments, loans, and deposits. A granular approach would capture the level of exposure to municipals based on factors, such as rating, geography, and maturity. Reports to senior management should provide enough information for management to understand how sensitive its securities and derivatives holdings are to credit quality shifts, market prices, and rates, in addition to liquidity and other risk factors. The board of directors should review reports and presentations on both the institution's exposures to securities and derivative instruments and its total credit risk exposures. Specific attention should be given to those issuers that are located in states or municipalities experiencing the most stress. Attention should also be given to revenue bonds or those that have had their ratings downgraded or pulled completely. These securities seem to be under additional stress that may impact both credit and liquidity concerns at financial institutions.

A periodic review of information that is sufficient in detail and timely will allow the board of directors to understand and assess credit, market, and liquidity risks associated with securities and derivative positions. Understanding the level of exposure to municipals and associated risk will better enable board and senior management to make sound decisions. The board's fulfillment of these responsibilities should be supported and clearly demonstrated through board or committee meeting minutes accompanied by reports and presentation packages on the credit, market, and liquidity risks associated with the securities and derivatives portfolios. Minutes should also reflect discussions of issues relating to governance between board members and senior management regarding the institution's risk management process, risk exposures, and perceived emerging risk.

Despite the fact that, historically, municipal bond defaults have remained relatively low, the impact of the economic crisis has many strategists and analysts sounding the alarm. With this alarm ringing, municipal exposure at financial institutions warrants additional scrutiny from both a credit and liquidity risk perspective. Taking additional measures to aggregate and understand these exposures may only be part of the drill at this juncture, but a drill well worth the effort, given the overall economic climate of problem assets on financial institutions' balance sheets. ■

Board of Governors of the Federal Reserve System

Got Questions? Need Answers? Check Out the Board's New FAQs Section!

The Federal Reserve Board has redesigned and expanded the *Current FAQs* (frequently asked questions) section of its website. New questions and answers address the Federal Reserve's roles and actions, currency and coin, consumer issues, the banking and financial system, and the economy.

Many answers link to related information and resources, and videos accompany some answers. Users can navigate the FAQs by topic. Questions and answers will be updated regularly, and new entries will be added as needed. Users may submit ideas for new questions using an online form.

To access the Current FAQs, visit: **www.federalreserve.gov/faqs/faq.htm.**

Innovation and Insight: Lessons from *SRC Insights'* Founder

by Katrina Johnston, SRC Project Manager

Next quarter's issue of *SRC Insights* will mark its 16th year of publication. As SRC staff embark on another year of providing articles and insights to benefit Third District bankers, the founder of *SRC Insights*, Cindi Course, is embarking on a new endeavor: working in the 12th District. Cindi accepted a role with the Federal Reserve Bank of San Francisco beginning May 23. In her 17 years with the Federal Reserve Bank of Philadelphia, she has been a steadfast resource in the department due to her extensive contributions and vision. In this feature, Cindi provides her insight on the innovations she has seen—and helped to create—over the course of her career in SRC, how SRC will continue to collaborate with bankers, and why the department is positioned to overcome future challenges.

Reaching Out from the Start

Before joining the Fed, Cindi worked for a community bank in New Jersey. One of the reasons she was hired in SRC was to bring additional industry perspective into the department—joining other industry hires to balance the department's view and show the other side of the coin. Outreach activities were a top priority, including Bankers' Forums (then in their infancy), CPA/CFO Roundtables, and this brand-new publication.

"Shortly after I started, I was looking at publications that other Districts had done, to get ideas and best practices, and I found that many were not sustainable for a variety of reasons," Cindi explains. SRC's leaders, led by Mike Collins, saw the great value in outreach activities. So the first issue of *SRC Insights* was launched with strong support. Cindi even remembers much of the content: Mike's first column of many and "When We Disagree," an article about the appeals program. The publication has run uninterrupted for four issues each year since its inception.

Evolving Outreach

Although the early issues may look different from today's, the mission is much the same: reaching out to bankers. "*SRC Insights* was another way of reaching a broader base of individuals than we could reach through our face-to-face outreach," Cindi says. In the beginning, she would perform most of the editorial work, acquiring and editing articles from SRC staff, in addition to formatting and laying out the issues. Now, more staff throughout the Reserve Bank are involved in various stages of publication. And there have been two major redesigns of the style to reflect newer designs and advanced technology, with another redesign planned for next quarter.

SRC Insights' changes reflect the evolution of the industry. *Compliance Corner*, the central section that was once part of *Insights*, has now evolved into a standalone Systemwide publication, *Consumer Compliance Outlook*. Though *Insights* may not look the same now as it first did, its core content is very similar to the early issues. It still leads off with an article from SRC's senior officer (next quarter's issue will also mark Bill Lang's first article), and it still covers emerging issues that examiners think the bankers might be interested in.

SRC's other outreach activities maintain their core purpose as well. "The Bankers' Forums actually are very similar now to the way they were when we first started," Cindi says. "Because it's a model that works. We share some of our thoughts. We always have one of our senior officers give a perspective on what's going on broadly, we have an economic update, and then we may have one or two specialized presentations. But mostly we're there to listen. And we do take the information that we learn from the bankers back and help to inform our policy with that feedback. When I was involved directly with the Bankers' Forums, I would prepare notes and send them to the

Board of Governors, saying 'This is what our bankers are talking about.' That really hasn't changed. As a model, it really does work."

The CPA/CFO Roundtable has evolved to include internal auditors in addition to CFOs from Third District institutions and CPAs from the firms that audit them. These events provide a forum for more dynamic discussions. And one of the more recent, reinvigorated methods for outreach is directors' outreach. "Directors realize that the pace of change in the industry is phenomenal," Cindi remarks. "And, particularly, in this current economic downturn, they are hungry for any information they can get. While the directors' outreach went on hiatus in the earlier part of the 2000s, the interest is picking up again."

It is this collaborative relationship that helps outreach activities succeed, and Cindi has played a large role in shaping it. SRC will continue to collaborate well with bankers to ensure the safety and soundness of Third District institutions. "Bankers are real people with real concerns and real lives," Cindi notes, "And they really want to do what's best for their organizations."

Outreach Moving Forward

With technology developing so many fascinating tools and outlets, it might be easy to adopt new methods to reach institutions using the latest Twitter update or webinar format. But Cindi warns against relying too heavily on advanced technology when collaborating with institutions. SRC should "be careful with how we define the purpose of our outreach," she says. "If the purpose of our outreach is one-way communication, to convey information, then webinars will be fantastic tools, particularly for the directors, many of whom have outside jobs and have very limited time to dedicate to their director role. When they are dedicating that time, it really is about the institution. So the webinars would be great for one-way communication."

But much of SRC's outreach is valued as two-way communication. Even with *SRC Insights*, many articles are developed based on discussions with bank management or other feedback. And bankers are always encouraged to contact the editors with any ideas for articles they'd like to read. Other forums are very important for face-to-face discussions, where SRC staff can really hear from the bankers. "Technology is wonderful," Cindi says, "It can help us move *Insights* faster, it can help us deliver online training faster, it can help us get technical bytes out quickly. But there's still no substitute for person-to-person contact. "

For the future of the publication she began 16 years ago, Cindi sees relevance as a critical factor for success. SRC's supervisory responsibilities are increasing to include savings and loan holding companies, in addition to its current state member banks and bank holding companies. Content must be relevant to and connect with both audiences.

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Another challenge will be timeliness. "It's good that *SRC Insights* is published quarterly, and we get the web version published out in advance of the hard copy," Cindi says. "Because so many things are changing now, particularly with Dodd-Frank, the Basel capital accord, etc., keeping things timely is also going to be a challenge."

Innovation

With all of her efforts toward SRC outreach, it's hard to believe Cindi ever had time to focus on anything else during her career at the Philadelphia Fed. But focus she did. In addition to her outreach with bankers and other regulators, Cindi has also championed many efforts to benefit SRC staff. Much of her work embodies the concept of innovation. For example, she worked to craft the first CPE program, which helped CPA-licensed staff earn National Association of State Boards of Accountancy (NASBA) credits through Federal Reserve System training in order to maintain their licenses. This has had a great impact on many staff members, who previously had to attend outside training for their licenses. This has also benefitted the many CPA-licensed bankers who attend SRC's outreach events.

And in the mid-1990s, Cindi was part of the first group in the Bank to draft a telecommuting policy. Working from home presented a great opportunity, but it lacked a formal procedure. Cindi saw the need and decided to help fill it. "If staff could work effectively in the field, why couldn't they work effectively from their homes?" she questioned. Now, many staff are able to telecommute very effectively on a regular basis.

Innovation is a big buzz word these days, but Cindi has always looked at things in what could be considered an innovative way. She likens her outlook to the Barbara Mandrell song, "I Was Country When Country Wasn't Cool," saying "I was innovative before innovative was cool." In order to be innovative, she recognizes that a supportive management team is a necessity. Knowing that SRC management encouraged new ways of thinking about things, Cindi adopted an interesting method: approach management not with a problem, but with a solution. If she saw that SRC wasn't getting through to its bankers as well as it could, she would suggest ways to get around it and get through to them. Such insight is part of the reason *SRC Insights* has flourished so consistently for so long.

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Cindi's personal work ethic is a great model for thinkers and strategists who want to make a difference in their institution. "With our heavy workloads, you sometimes have to think innovatively on your own time and let ideas percolate," she admits. "But the personal and professional rewards can be immense."

The Bar Is Set

The San Francisco Fed staff are certainly lucky to have such a strong employee and role model joining them. As Cindi moves forward, she looks back on the experiences and mentors who have helped shape her decision-making. In her new role, she will be involved with risk and policy issues, so her past banking experience will continue to be relevant. She also credits Mike Collins for being a fantastic mentor.

"I've often found myself over my career, when I'm in a place where I'm not sure what to do, thinking, 'How would Mike handle this?' And that helps to inform my decision-making. And then I think broadly about how other folks I've worked with in the System who I regard as strong role models would handle it. And that, too, will inform a decision. So I'll be bringing a lot of history, a lot of depth from the Federal Reserve System to San Francisco. I think I can make a huge difference, not just for San Francisco, but for the Federal Reserve System." She also adds that she'll still be visible. "I'm not going away, I'm just doing something different."

It's not just Third District employees she is saying goodbye to, but Third District bankers. She values the relationships she has formed with bankers through outreach events and her recent role in the Community Regional Supervision Unit. The impression she would like to leave behind is that anything is possible. As many who have worked with her have noticed, Cindi views what some might see as failures instead as opportunities to do something new. Her work ethic has made her a department and District go-to for any range of questions or requests.

As she moves forward and Mike retires, Cindi is assured that SRC is poised to face future challenges. "Neither Mike, nor I, nor anyone else who's left recently would be doing our jobs if we didn't help to prepare the officers and staff to assume broader or different responsibilities. We've got a fantastic team in the department, a rapidly expanding team, and they'll be able to carry the organization forward. It's going to be different. And it's for the folks who are here to define what the organization is going to be in the future."

Whether it's the legacy of *SRC Insights* or other innovative projects in the department, Cindi leaves behind a strong influence on that future. ■

Financial Institution Accounting: Changes for 2011

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measurement of loans, deciding that assets managed by financial institutions for the collection of contractual cash flows for a lending or financing activity should generally qualify for measurement at amortized cost on the balance sheet, rather the originally proposed fair value cost. Additionally, the FASB-proposed framework for accounting for financial instruments differs significantly from the IASB's. There appears to be an ultimate goal of revisiting these statements and issuing a joint final standard.

At present, regulatory agencies are uncertain what the potential accounting implication of the financial instruments proposal will be for financial institutions. In May 2010, regulatory comments regarding the exposure draft were provided to the FASB. While no effective date for a final standard has been determined, a new standard is not likely to become effective before 2013.

Accounting Treatment of Leases

Currently, the FASB is reviewing comments received on its leasing proposal, issued in August 2010. Under the proposal, a new lease accounting model eliminates the off-balance sheet approach of operating leases. For financial institutions serving as lessees, the proposal requires right-to-use asset entry and a corresponding liability equal to the present value of lease payment obligations. In addition, initial direct costs are included with the balance sheet recording of the right-to-use asset. Interest expense is recognized, and an ongoing assessment of facts and circumstances is required.

For financial institutions serving as lessors, a dual accounting approach is required. If there is significant risk or benefit exposure to the underlying leased asset, the lessor would apply the "performance obligation approach," whereby the leased asset is recorded on the balance sheet as a receivable for the expected lease payments. A deferred revenue entry is recorded for the corresponding performance obligation liability. However, if there is no risk or benefit exposure to the underlying asset, the lessor would apply the "derecognition approach," whereby a portion of the leased asset is removed from the books. A receivable for expected payments and the residual asset that represents the right to the underlying asset at the end of the lease's term are recorded. In addition, an expense entry related to the removed portion of the leased asset is recognized.

The proposal could have a significant impact on financial institutions that engage heavily in leasing activity, as the interest expense on the outstanding obligation must be recognized, and the right-of-use asset must be amortized over either the expected lease term or the asset's useful life, whichever is shorter. Other potential implications arising from this proposal include:

- Impact on lending decisions: leasing rather than buying
- Changes to income statement metrics and capital ratios: the result of increased lease-related assets
- Increases in operational monitoring: accounting systems enhancements
- Additional book/tax differences: the result of possible increases in deferred tax assets and adjustments in regulatory capital
- Extensive data gathering for existing transactions due to the lack of grandfathering

For financial institutions with a significant presence in the leasing business, management should consider the ramifications of this proposal relative to balance sheet, income and capital management, strategic planning, and information systems.

Accounting Treatment of Troubled Debt Restructuring (TDRs)

Banks should be able to get a clearer picture on troubled debt restructurings (TDRs). FASB defines a TDR as a loan concession granted by the lender based on legal or economic reasons related to the debtor's financial difficulties that it would not otherwise permit. The increase is because FASB issued Accounting Standards Update (ASU) 2011-02 "Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring is Troubled Debt Restructuring."[3] The update issued did not change the requirements of more granular credit quality and allowance for loan and lease losses (ALLL) disclosures for loans, including quantitative and qualitative disclosure information about TDRs. Rather, the guidance provides clarifying information for creditors when determining whether a loan restructuring is a TDR. Specifically, the guidance provides clarification on concessions and financial difficulties, in addition to disclosures related to TDRs.

This new guidance could result in an increase in loans being reported as TDRs.

This new guidance could result in an increase in loans being reported as TDRs. In addition, since TDRs must be evaluated under Accounting Standard Codification (ASC) 310-10 (formerly FAS 114) impairment rules, the ALLL and corresponding credit quality indicators and ratios could change. As such, bank management should review the guidance, with a focus on the nature and extent of TDRs that have occurred, and their effect on the ALLL during a reporting period.

Disclosures Regarding the Credit Quality of Financial Receivables and the Allowance for Credit Losses

In July 2010, the FASB issued an Accounting Standards Update (ASU) to provide transparency regarding a financial institution's ALLL and credit quality of financing receivables. In general, the amended disclosures contained in the update apply to all loans carried at amortized cost and include guidance on:

- Roll-forward of the ALLL by portfolio segment
- Nonaccrual status of financing receivables
- Impairment status of financing receivables
- Internal credit risk ratings and aging of past due financing receivables at the end of a reporting period
- Purchase and sale of financing receivables disaggregated by portfolio

In conjunction with this guidance, financial institutions will be required to provide more transparency in their loan disclosure and ALLL documentation. As such, examiners should consider discussing the impact of these disclosures with bank management, particularly if a system change to collect the appropriate data to meet this accounting standard is necessary. In addition, since the guidance is not prescriptive in nature, examiners should inform financial institutions not to disclose their regulatory credit classification treatment if deemed confidential.

Other Accounting Issues

Proposed Guidance—Loan Impairment

On January 31, 2011, the FASB and the IASB issued for comment a joint loan impairment proposal that proposes to change U.S. generally accepted accounting principles (GAAP) and international financial reporting standards (IFRS). This proposal change aims to evolve from an incurred loss to an expected loss model that would utilize more forward-looking data to estimate credit losses. The impact of the proposed standard may require financial institutions to recognize loan losses earlier than under the current model, based on management's estimate of expected future credit losses, and require revisions to the ALLL estimation process, potentially increasing ALLL levels. The comment period for this proposal ended April 1, 2011.

Revisions to Goodwill Impairment Test

ASU No. 2010-28, "Intangibles - Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts" became effective in the first quarter of 2011. This update modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. This revision to the current GAAP process will eliminate the ability to assert that a reporting unit is not required to perform Step 2 because the carrying amount of the reporting unit is zero or negative, despite qualitative factors indicating that goodwill is more likely than not impaired. Goodwill impairments, then, may be reported sooner than under current practice.

Amendments to Service Organization Standards

Recently, the American Institute of Certified Public Accountants (AICPA) revised its Service Organizations guide (commonly known as the "SAS 70 guide") to reflect

[3] www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175822278141&blobheader=application%2Fpdf.

requirements and guidance in Statement on Standards for Attestation Engagements No. 16 (SSAE 16).[4] This revision will be effective in June 2011. Two major changes to the guide require that:

- The service organization provides a written assertion to the service auditor about the fairness of the presentation of the description of its system and the suitability of the design
- Regarding the effectiveness of operating controls, the service auditor's opinion of the description of the service organization's system reviews the same period covered by the auditor's test of the operating effectiveness of controls[5]

Proposed ASU—"Reconsideration of Effective Control for Repurchase Agreements"

Another proposed ASU involves repurchase agreements. In November 2010, the FASB issued a proposed ASU Topic 860, "Transfers and Servicing (ASC Topic 860) – Reconsideration of Effective Control for Repurchase Agreements." One main point of the proposal is that the exchange of collateral is not a determining factor for effective control. Instead, effective control should be based on the transferor's contractual rights and obligations. It is hoped that the proposed ASU would improve accounting for repurchase agreements where the transferor is entitled and obligated to repurchase and redeem financial assets before maturity. The comment period ended January 15, 2011, for this proposal.

Conclusion

These are only a few of the updates and proposals issued in the accounting world. Bank management should review the accounting announcements as they become available and assess how they might be relevant to an individual institution. Increased awareness of coming changes can help institutions stay ahead of the curve. ■

[4] www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/AudAttest/AudAttestGuidance/DownloadableDocuments/Final%20Service%20Orgs%20FAQ.pdf.

[5] Sherinsky, Judith M., "Replacing SAS 70: New Standards for Engagements Involving Outsourcing," Journal of Accountancy, August 2010, www.thefreelibrary.com/Replacing+SAS+70%3A+new+standards+for+engagements+involving+outsourcing.-a0233606990.

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Note: The Bank Resources pages offer a variety of information, guidance and tools for financial institutions related to regulatory reporting, financial services, and bank supervision and regulation.

WHO TO CALL: 2011 UPDATES

As evident throughout this issue of *SRC Insights*, there have been some significant staffing changes in the Supervision, Regulation and Credit (SRC) Department in recent weeks. Those who typically contact Mike Collins directly should contact Bill Lang (william.lang@phil.frb.org) at (215) 574-7225. Those who typically contact Cindi Course directly should contact Bill Wisser (william.t.wisser@phil.frb.org) at (215) 574-7267.

The following list should help you find the correct contact person to call in different areas of SRC. Financial institutions that have an appointed central point of contact should generally contact that individual directly.

Contact names appearing in **bold** are the primary contacts for their areas.

Community Regional Supervision

William W. Lang, SVP	215-574-7225
Constance H. Wallgren, VP	215-574-6217
Elisabeth V. Levins, AVP	215-574-3438
Eric A. Sonnheim, AVP	215-574-4116
William T. Wisser, AVP	215-574-7267
Stephen J. Harter, Manager	**215-574-4385**
Adina A. Himes, Manager	**215-574-6443**
Jacqueline Fenton, Manager	**215-574-6234**
Lorraine Lopez, Manager	**215-574-6596**

Consumer Compliance & CRA Examinations

William W. Lang, SVP	215-574-7225
Robin P. Myers, AVP	215-574-4182
Robert Snarr, Manager	**215-574-3918**

Consumer Complaints

Federal Reserve Consumer Help Center	**888-851-1920**

Regulations Assistance

Regulations Assistance Line	**215-574-6568**

Enforcement

A. Reed Raymond, VP	215-574-6483
Joseph J. Willcox, Manager	**215-574-4327**

Regulatory Applications

A. Reed Raymond, VP	215-574-6483
H. Robert Tillman, AVP	215-574-4155
James D. DePowell, Manager	**215-574-4153**

Retail Risk Analysis

Christopher C. Henderson, Retail Risk Officer	**215-574-4139**

Discount Window and Reserve Analysis

Vish P. Viswanathan, VP	215-574-6403
Gail L. Todd, Credit Officer	**215-574-3886**

DFA Today: A Dodd-Frank Act Implementation Update

Considerable progress is being made on the implementation and rulemaking process associated with the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act or the act), but much work still remains. Certain aspects of the Dodd-Frank Act continue to stir spirited debate among legislators, regulators, bankers, and the public. It is important to remain up-to-date on the latest developments and to convey opinions and feedback through the proper venues.

The first quarter 2011 issue of *SRC Insights* contained a special feature titled "Navigating Dodd-Frank: An Implementation Update and Resource Guide." Subsequent issues of *SRC Insights* will contain a periodic summary of new Dodd-Frank-related events that have occurred since the previous issue. This ongoing feature is devoted to enhancing awareness of the activities associated with the implementation of the act, highlighting notable proposals, legislative actions, agency updates, speeches and testimony, and financial industry studies that have been released. Reference links to more detailed information on the subject matter are also provided.

If you have any questions regarding this recurring feature, please contact Senior Specialist Bob Rell (bob.rell@phil.frb.org) at (215) 574-4382.

RULE PROPOSALS AND REQUESTS FOR COMMENT

April 21, 2011
Studies Regarding the Resolution of Financial Companies Under the Bankruptcy Code
This is a Federal Reserve request for public information and comment to conduct two studies regarding the resolution of financial companies under Chapter 7 or Chapter 11 of the U.S. Bankruptcy Code and to conduct one study regarding international coordination relating to the resolution of systemic financial companies under the Bankruptcy Code and applicable foreign law.
http://www.federalreserve.gov/newsevents/press/bcreg/20110421a.htm

April 19, 2011
Federal Reserve Proposes Rule Under Regulation Z Pertaining to a Consumer's Ability to Repay a Mortgage and Minimum Mortgage Underwriting Standards
This proposal under Regulation Z would require creditors to determine a consumer's ability to repay a mortgage before making the loan and would establish minimum mortgage underwriting standards. The proposal also implements the act's limits on prepayment penalties.
http://www.federalreserve.gov/newsevents/press/bcreg/20110419a.htm

April 15, 2011
Notice of Intent to Apply Certain Supervisory Guidance to Savings and Loan Holding Companies
This is a request for comment on a notice that outlines how the Federal Reserve intends to apply certain parts of its current consolidated supervisory program for bank holding companies to savings and loan holding companies (SLHCs) after assuming supervisory responsibility for SLHCs in July 2011. The Dodd-Frank Act transfers supervisory functions related to SLHCs and their nondepository subsidiaries to the Board on July 21, 2011.
http://www.federalreserve.gov/newsevents/press/bcreg/20110415a.htm

April 12, 2011
Margin and Capital Requirements for Covered Swap Entities
Agencies are requesting comment on a proposed rule to establish minimum margin and capital requirements for registered swap dealers, major swap participants, security-based swap dealers, and major security-based swap participants as required by the act.
http://www.federalreserve.gov/newsevents/press/bcreg/20110412a.htm

April 12, 2011
Agencies Seek Comment on Resolution Plan Reporting
Large, systemically-significant bank holding companies and nonbank financial companies would be required to submit annual resolution plans and quarterly credit exposure reports under a rule proposed by the Federal Reserve Board and the Federal Deposit Insurance Corporation (FDIC).
http://www.federalreserve.gov/newsevents/press/bcreg/20110412b.htm

April 6, 2011
Regulation D, Q, and DD: Prohibition Against Payment of Interest on Demand Deposits
These proposed amendments would repeal Regulation Q, Prohibition Against Payment of Interest on Demand Deposits, effective July 21, 2011. The proposed amendments would also repeal the Board's published interpretation of Regulation Q and remove references to Regulation Q found in the Board's other regulations, including section 204.10 of Regulation D (Reserve Requirements of Depository Institutions) and paragraph (n) of Supplement I to Regulation DD (Truth in Savings).
http://www.federalreserve.gov/newsevents/press/bcreg/20110406a.htm

March 30, 2011
Incentive-Based Compensation Arrangements
This proposal would require a covered financial institution to report incentive-based compensation arrangements and would prohibit incentive-based compensation arrangements at a covered financial institution when such compensation is excessive, could expose the institution to inappropriate risks, or could lead to material financial loss.
http://www.federalreserve.gov/newsevents/press/bcreg/20110330a.htm

March 30, 2011
Regulation HH: Risk Management Standards Regarding Certain Financial Market Utilities
This is a proposal to promulgate risk management standards governing the operations related to the payment, clearing, and settlement activities of certain financial market utilities that are designated as systemically important by the Financial Stability Oversight Council (FSOC).
http://www.federalreserve.gov/newsevents/press/other/20110330a.htm

March 29, 2011
Credit Risk Retention
This interagency proposed rule would require sponsors of asset-backed securities (ABS) to retain at least 5 percent of the credit risk of the assets underlying the securities.
http://www.federalreserve.gov/newsevents/press/bcreg/20110329a.htm

March 9, 2011
Consumer Financial Protection Bureau (CFPB) Consumer Response Intake Fields
The CFPB published a request for comment on forms that will be used for questions, complaints, and other information about consumer financial products.
http://edocket.access.gpo.gov/2011/pdf/2011-5349.pdf

March 1, 2011
Regulation B: Equal Credit Opportunity and Regulation V: Fair Credit Reporting Risk-Based Pricing Regulations
This is a proposal to amend certain model notices in Regulation B to include the disclosure of credit scores and information relating to credit scores if a credit score is used in taking adverse action. The joint proposal would revise the content requirements for risk-based pricing notices and add related model forms to reflect the new credit score disclosure requirements.
http://www.federalreserve.gov/newsevents/press/bcreg/20110301a.htm

March 1, 2011
Core and Brokered Deposit Study as Mandated by Section 1506 of the Dodd-Frank Act.
The FDIC is conducting a study to evaluate the definition of core deposits for the purpose of calculating insurance premiums. Differences between core deposits and brokered deposits and their role in the economy and U.S. banking sector will also be considered.
http://www.fdic.gov/regulations/reform/coredeposits.html

February 23, 2011
Federal Reserve Seeks Comment on Proposed Revisions to Escrow Account Requirements for Home Mortgage Loans
This is a proposal to implement statutory changes made by the Dodd-Frank Act that lengthen the time for which a mandatory escrow account established for a higher-priced mortgage loan must be maintained. In addition, the proposal would implement the act's disclosure requirements regarding escrow accounts. The proposal also would exempt certain loans from the statute's escrow requirement. The primary exemption would apply to mortgage loans extended by creditors that operate predominantly in rural or underserved areas, originate a limited number of mortgage loans, and do not maintain escrow accounts for any mortgage loans they service.
http://www.federalreserve.gov/newsevents/press/bcreg/20110223b.htm

February 8, 2011
Regulation Y: Definitions of Predominantly Engaged in Financial Activities and Significant Nonbank Financial Company and Bank Holding Company
This is a notice of proposed rulemaking and request for comment regarding proposed amendments to Regulation Y that (1) establish the criteria for determining whether a company is "predominantly engaged in financial activities" and (2) define the terms "significant nonbank financial company" and "significant bank holding company" for purposes of Title I of the act.
http://www.federalreserve.gov/newsevents/press/bcreg/20110208a.htm

February 3, 2011
Agency Information Collection
This is a notice of intention to require savings and loan holding companies (SLHCs) to submit the same reports as bank holding companies (BHCs), beginning with the March 31, 2012, reporting period.
http://www.federalreserve.gov/newsevents/press/bcreg/20110203a.html

FINAL RULES ADOPTED

March 25, 2011
Truth-in-Lending Act (TILA) Exemption Threshold Increase
The Board issued a final rule to raise the exemption threshold from $25,000 to $50,000 for: 1) non-home secured credit (under Regulation Z) and 2) consumer leases (under Regulation M). The final rule will be effective July 21, 2011.
http://www.federalreserve.gov/newsevents/press/bcreg/20110325a.htm

February 23, 2011
Truth-in-Lending Act Escrow Requirements
The Board issued a final rule to increase the annual percentage rate (APR) threshold used to determine whether a mortgage lender is required to establish an escrow account for property taxes and insurance for first-lien "jumbo" residential mortgage loans, effective April 1, 2011.
http://www.federalreserve.gov/newsevents/press/bcreg/20110223b.htm

February 9, 2011
Volcker Rule Conformance Period
The Board announced its approval of a final rule to implement the provisions of the act that give banking firms a period of time to conform their activities and investments to the prohibitions and restrictions of the Volcker Rule [DFA Section 619(c)(6)].
http://www.federalreserve.gov/newsevents/press/bcreg/20110209a.htm

LEGISLATIVE ACTIONS

April 15, 2011
H.R. 1573: To Facilitate Implementation of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Promote Regulatory Coordination, and Avoid Market Disruption
Reps. Lucas (R-Okla), Bachus (R-Ala), Conaway (R-Texas), and Garrett (R-N.J.) introduced H.R. 1573, which would extend the deadline for implementing Title VII of the act by 18 months.
http://www.govtrack.us/congress/billtext.xpd?bill=h112-1573

March 31, 2011
S. 712: Financial Takeover Repeal Act of 2011
Senator Jim DeMint (R-SC) introduced a bill, The Financial Takeover Repeal Act of 2011 (S. 712), which would repeal the act. The legislation currently has 18 Republican co-sponsors.
http://www.govtrack.us/congress/bill.xpd?bill=s112-712

REPORT RELEASES, SPEECHES, AND EVENTS OF INTEREST

April 22, 2011
Study and Recommendations on Section 404(b) of the Sarbanes-Oxley Act of 2002 for Issuers With Public Float Between $75 and $250 Million
The staff of the office of the chief accountant of the Securities and Exchange Commission (SEC) published its study examining Section 404(b) of the Sarbanes-Oxley Act, which requires public companies' auditors to report on, and attest to, management's assessment of its internal controls.
http://www.sec.gov/news/studies/2011/404bfloat-study.pdf

April 18, 2011
The Orderly Liquidation of Lehman Brothers Holdings under the Dodd-Frank Act
The FDIC report examines how it could have structured

an orderly resolution of Lehman Brothers Holdings, Inc. under the orderly liquidation authority of Title II of the act, had that law been in effect in advance of Lehman's failure.
http://www.fdic.gov/regulations/reform/lehman.html

April 13, 2011
Wall Street and the Financial Crisis: Anatomy of a Financial Collapse
The United States Senate Permanent Subcommittee on Investigations Committee on Homeland Security and Governmental Affairs issued its report, "Wall Street and the Financial Crisis: Anatomy of a Financial Collapse," on the causes of the recent global financial collapse.
http://levin.senate.gov/newsroom/supporting/2011/PSI_WallStreetCrisis_041311.pdf

April 7, 2011
Community Bankers and Supervisors: Seeking Balance
Governor Sarah Bloom Raskin spoke at the Federal Reserve Bank of New York Community Bankers Conference, New York, New York.
http://www.federalreserve.gov/newsevents/speech/raskin20110407a.htm

March 31, 2011
Regulating Systemic Risk
Governor Daniel K. Tarullo spoke during the 2011 Credit Markets Symposium, Charlotte, North Carolina.
http://www.federalreserve.gov/newsevents/speech/tarullo20110331a.htm

March 30, 2011
Review of Congressional Budget Office's (CBO's) Cost Estimate for the Dodd-Frank Wall Street Reform and Consumer Protection At: Testimony of Douglas W. Elmendorf, Director
The CBO estimated that, over the 2010–2020 period, the Dodd-Frank Act would increase both revenue and direct (or mandatory) spending by $13.4 billion and $10.2 billion, respectively. On net, those effects were projected to reduce deficits by $3.2 billion. The revenue would stem primarily from fees assessed on various financial institutions and market participants.
http://www.cbo.gov/ftpdocs/121xx/doc12120/03-29-Dodd-Frank.pdf

February 17, 2011
Oversight of Dodd-Frank Implementation: A Progress Report by the Regulators at the Half-Year Mark
This is testimony on implementation of the Dodd-Frank Act before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, Washington, D.C.
http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Hearing&Hearing_ID=c43953db-0fd7-43c3-b6b8-97e2d0da3ef7

February 17, 2011
Interchange Fees
Governor Sarah Bloom Raskin testified before the Subcommittee on Financial Institutions and Consumer Credit, Committee on Financial Services, U.S. House of Representatives, Washington, D.C.
http://www.federalreserve.gov/newsevents/testimony/raskin20110217a.htm

UPDATES ON NEW AGENCIES

Consumer Financial Protection Bureau

April 11, 2011
Consumer Financial Protection Bureau and National Association of Attorneys General Presidential Initiative Working Group Release Joint Statement of Principles
The CFPB and the Presidential Initiative Working Group of the National Association of Attorneys General (NAAG) announced agreement on a Joint Statement of Principles, the first step in forging a new partnership between federal and state officials to protect consumers of financial products and services.
http://www.consumerfinance.gov/pressrelease/consumer-financial-protection-bureau-and-national-association-of-attorneys-general-presidential-initiative-working-group-release-joint-statement-of-principles/

April 1, 2011
CFPB Spending Update: CFO Update for the First Quarter of Fiscal Year 2011
The CFPB issued its first spending update. The goal of these updates is to provide a snapshot of how the CFPB is spending and add perspective on how it employs resources to fulfill its mission.
http://www.consumerfinance.gov/budget/cfo-q1-2011/

March 31, 2011
Treasury Department Announces Senior Hires for Consumer Financial Protection Bureau
The U.S. Department of the Treasury announced the hiring of senior leadership for the CFPB, selecting Catherine West to serve as Chief Operating Officer, Gail Hillebrand to serve as Associate Director of Consumer Education and Engagement, Dennis Slagter to serve as Chief Human Capital Officer, and David Gragan to serve as Assistant Director of Procurement.
http://www.treasury.gov/press-center/press-releases/Pages/tg1123.aspx

March 16, 2011
Testimony of Elizabeth Warren Before the House Financial Services Committee
Elizabeth Warren, Special Advisor to the Secretary of the Treasury for the Consumer Financial Protection Bureau, testified before the Subcommittee on Financial Institutions and Consumer Credit Committee on Financial Services, United States House of Representatives.
http://www.consumerfinance.gov/speech/testimony-of-elizabeth-warren-before-the-house-financial-services-committee/

Federal Insurance Office

March 17, 2011
Director of Federal Insurance Office (FIO) Named
Secretary of the Treasury Timothy Geithner announced that the first director of the new FIO will be Michael McRaith, currently insurance director of Illinois and formerly the secretary/treasurer of the National Association of Insurance Commissioners (NAIC).

Financial Stability Oversight Council

April 14, 2011
Financial Stability Oversight Council (FSOC)
J. Nellie Liang, Director, Office of Financial Stability Policy and Research, testified before the Subcommittee on Oversight and Investigations, Committee on Financial Services, U.S. House of Representatives, Washington, D.C.
http://www.federalreserve.gov/newsevents/testimony/liang20110414a.htm

March 17, 2011
FSOC Meeting
The FSOC convened its fourth meeting on March 17, 2011, at the U.S. Department of the Treasury and approved each of the documents and resolutions put forward during the session. These included: a Notice of Proposed Rulemaking (NPR) regarding designations of financial market utilities for heightened supervision; an NPR on the FSOC's FOIA Regulations; and the minutes of the FSOC's previous meeting, held on January 18, 2011.
http://www.treasury.gov/initiatives/Pages/FSOC-index.aspx

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