



## In This Issue

### Bank & Thrift Regulatory Update

Basel Committee Finalizes Approach for Measuring Counterparty Credit Risk for the Capital Framework .....	1
OCC Bulletins Alert Institutions to FFIEC Statements on Cyber Threats .....	1
OCC Issues New Comptroller’s Handbook Booklet on Garnishment of Accounts Containing Federal Benefit Payments.....	2

### Enterprise & Consumer Compliance

CFPB Office of Consumer Response Issues Report on Complaints Handling in 2013 .....	2
CFPB Director Outlines Rulemaking Process to ABA.....	3
FTC Reaches Settlement with Debt Collectors .....	3

### Capital Markets & Investment Management

SEC Seeks Comment on Target Date Funds Disclosure .....	4
SEC Announces Additional \$150,000 Payment to First Whistleblower Award Recipient .....	4
CFTC, OFR Sign Memorandum of Understanding to Improve Data Quality .....	5
OTC Derivatives Regulators Issue Report to the G20.....	5
Enforcement Actions .....	6

Recent Supervisory Actions .....	8
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# Bank & Thrift

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## Basel Committee Finalizes Approach for Measuring Counterparty Credit Risk for the Capital Framework

The Bank for International Settlements' Basel Committee on Banking Supervision (Basel Committee) published, on March 31, 2014, a final standard on the treatment of derivatives-related transactions in its capital adequacy framework. The final standard, *The standardized approach for measuring counterparty credit risk exposures*, will replace both the Current Exposure Method and the Standardized Method in the Basel capital framework. It will also simplify the framework by narrowing the range of methodologies available to banks in measuring their counterparty credit risk exposures.

The Basel Committee states "the new approach reduces the need for discretion by national authorities, limits the use of banks' internal estimates, and avoids undue complexity by drawing upon prudential approaches already available in the capital framework. It is calibrated to reflect the volatilities observed over the recent stress period, while also taking account of incentives for centralised clearing of derivative transactions."

The new approach will take effect on January 1, 2017. The Basel Committee indicates that at that time it will eliminate the use of the "IMM shortcut method" for measuring counterparty exposures.

## OCC Bulletins Alert Institutions to FFIEC Statements on Cyber Threats

On April 2, 2014, the Office of the Comptroller of the Currency (OCC) released Bulletin 2014-13 to announce the release of a joint statement by members of the Federal Financial Institutions Examination Council (FFIEC) that notifies institutions of a large-dollar-value automated teller machine (ATM) cash-out fraud characterized as Unlimited Operations by the U.S. Secret Service. The members indicate there has been a recent increase in cyber-attacks on financial institutions launched in connection with this fraud for the purpose of gaining access to, and altering the settings on, ATM Web-based control panels used by small-to-medium-sized financial institutions. Institutions are expected to take steps to mitigate this threat by ensuring that:

- Each institution's and service provider's management of enterprise risk addresses this type of threat in its risk assessment process; and
- Controls associated with institution's information technology networks, card issuer authorization systems, systems that manage ATM parameters, and fraud detection and response processes are reviewed for adequacy against this threat.

On April 3, 2014, the OCC released Bulletin 2014-14 to announce the release of a second FFIEC joint statement. This statement highlights the risks associated with the continued distributed-denial-of-service (DDoS) attacks and the steps that institutions are expected to take to mitigate the risks they pose. In particular, institutions are expected to:

- Monitor incoming traffic to its public Web site;
- Activate incident response plans if it suspects that a DDoS attack is occurring; and

- Ensure sufficient staffing for the duration of the attack, including the use of previously contracted third-party services, if appropriate.

The members of the FFIEC include the OCC, the Federal Reserve Board, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the State Liaison Committee, and the Consumer Financial Protection Bureau.

## OCC Issues New Comptroller's Handbook Booklet on Garnishment of Accounts Containing Federal Benefit Payments

The Office of the Comptroller of the Currency (OCC) issued the booklet "*Garnishment of Accounts Containing Federal Benefit Payments*" on April 1, 2014. The booklet, which is new to the *Comptroller's Handbook*, contains interagency guidance and examination procedures for the interagency final rule governing the garnishment of certain federal benefit payments that are directly deposited to accounts at financial institutions. In general, the booklet:

- Establishes procedures that financial institutions must follow when they receive a garnishment order against an account holder who receives certain types of federal benefit payments by direct deposit.
- Requires financial institutions that receive such a garnishment order to determine the sum of such federal benefit payments deposited to the account during a two-month period and ensure that the account holder has access to an amount equal to that sum or to the current balance of the account, whichever is lower.

# Enterprise & Consumer Compliance

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## CFPB Office of Consumer Response Issues Report on Complaints Handling in 2013

The Consumer Financial Protection Bureau (CFPB or Bureau) released its *Consumer Response Annual Report* on March 31, 2014. The report summarizes the efforts of the CFPB's Office of Consumer Response, which handles consumer complaints received by the CFPB, during calendar year 2013. The report notes that, between 2012 and 2013, complaint volume rose 80 percent, from 91,000 complaints in 2012 to 163,700 in 2013. The Bureau currently accepts consumer complaints related to mortgages, bank accounts and services, private student loans, vehicle and other consumer loans, credit reporting, money transfers, debt collection, and payday loans. Most complaints were related to mortgages (37 percent), debt collection (19 percent), and credit reporting (15 percent). Interestingly, the Bureau only began accepting complaints related to debt collection in July 2013.

The CFPB notes that complaints inform the Bureau's work and help to identify problems, which then feed into the Bureau's supervision and enforcement prioritization process.

## CFPB Director Outlines Rulemaking Process to ABA

Richard Cordray, Director of the Consumer Financial Protection Bureau (CFPB or Bureau), spoke before the American Bar Association (ABA) on April 3, 2014. Director Cordray's remarks centered on the rulemaking process and a new CFPB project referred to as "regulatory implementation."

Throughout his remarks, Director Cordray highlighted ways the CFPB was "doing some things differently" with regard to the rulemaking process, including:

- Conducting field hearings on a regular basis to solicit input from a broader group of constituents than is generally reachable through a *Federal Register* notice (i.e., average consumers);
- Experimenting with online pilot projects like Cornell University's e-Rulemaking Initiative to facilitate public participation in consumer financial protection rulemakings;
- "Placing the voice of the consumer at the center of [the CFPB's] consciousness" to help prioritize new issues to be addressed by new regulation (i.e., identifying the need for regulation based on consumer complaints); and
- Introducing "regulatory implementation" to support strong implementation of new rules. From the perspective of the industry this includes:
  - Taking affirmative steps to help the industry understand the rules, including publishing plain-language guides and releasing explanatory videos;
  - Coordinating, as appropriate, with other regulators on examination procedures and releasing the procedures months in advance of the effective date of the rules;
  - Publishing readiness guides and checklists;
  - Launching eRegulations (a CFPB Web-based tool); and
  - Attending industry conferences and participating in webinars.

For consumers this effort includes:

- Conducting broad outreach to community organizations;
- Publishing explanatory materials in multiple languages;
- Drafting sample materials that consumers may customize for their needs (e.g., letters to credit reporting agencies to dispute information); and
- Posting answers to frequently asked questions on "Ask CFPB."

Director Cordray concluded with the thought "Consumers and industry both win – as does the agency – when our rules can be understood consistently and applied effectively."

## FTC Reaches Settlement with Debt Collectors

The Federal Trade Commission (FTC) announced that it had reached a settlement with two defendants alleged to have violated debt collection practices under the *Federal Trade Commission Act* and the *Fair Debt Collection Practices Act*. The settlement imposed a \$23 million judgment against the defendants that was suspended due to their inability to pay, except for \$3 million in frozen funds and personal assets the defendants agreed to surrender. The defendants also agreed to permanent bans from the debt collection business.

# Capital Markets & Investment Management

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## SEC Seeks Comment on Target Date Funds Disclosure

The Securities and Exchange Commission (SEC) announced on April 3, 2014 that it is seeking comment on a recommendation by its Investor Advisory Committee (IAC) regarding disclosure by target date mutual funds. The *Dodd-Frank Wall Street Reform and Consumer Protection Act* (The Dodd-Frank Act) established the IAC to advise the SEC on regulatory priorities, the regulation of securities products, trading strategies, fee structures, the effectiveness of disclosure, and on initiatives to protect investor interests and to promote investor confidence and the integrity of the securities marketplace. The Dodd-Frank Act authorizes the IAC to submit findings and recommendations for review and consideration by the SEC.

Target date funds are designed to make investing for retirement more convenient by automatically making changes over time to the fund's allocation among different asset classes, such as stocks, bonds, and cash. In 2010, the SEC proposed a rule that would require marketing materials for target date funds to include a graphical or tabular depiction of changes in the fund's asset allocation over time, known as a fund's "glide path." The SEC is reopening the comment period on its 2010 proposal to request comment on the IAC's recommendation that the SEC develop a glide path illustration based on a standardized measure of fund risk, which would replace or supplement what it previously proposed.

Members of the public will have 60 days to comment on the IAC's recommendation after the release is published in the *Federal Register*.

## SEC Announces Additional \$150,000 Payment to First Whistleblower Award Recipient

On April 4, 2014, the Securities and Exchange Commission (SEC) announced that the whistleblower who received the first award under its new whistleblower program will receive an additional \$150,000 payout now that the SEC has collected additional funds in the case. The whistleblower has now been awarded a total of nearly \$200,000 since the award was announced on August 21, 2012. The award recipient helped the SEC stop a multi-million dollar fraud by providing documents and other significant information that allowed its investigation to move at an accelerated pace and prevent the fraud from harming additional victims. The award represents 30 percent of the amount collected in the SEC enforcement action against the perpetrators of the scheme, the maximum percentage payout allowed under the law.

"This latest payment shows that the SEC's aggressive collection efforts pay dividends not only for harmed investors but also for whistleblowers," said Sean McKessy, Chief of the

SEC's Whistleblower Office. "As we collect additional funds from securities law violators, we can increase the payouts to whistleblowers."

The *Dodd-Frank Wall Street Reform and Consumer Protection Act* (The Dodd-Frank Act) authorized the whistleblower program to reward individuals who offer high-quality original information that leads to an SEC enforcement action in which more than \$1 million in sanctions is ordered. Awards can range from 10 percent to 30 percent of the money collected. The Dodd-Frank Act included enhanced anti-retaliation employment protections for whistleblowers and provisions to protect their identity. The law specifies that the SEC cannot disclose any information, including information the whistleblower provided to the SEC, which could reasonably be expected to directly or indirectly reveal a whistleblower's identity.

## CFTC, OFR Sign Memorandum of Understanding to Improve Data Quality

On March 31, 2014, the Commodity Futures Trading Commission (CFTC) and Office of Financial Research (OFR) announced a Memorandum of Understanding (MOU) on the terms and conditions for the CFTC and OFR to begin a joint project to enhance the quality, types, and formats of data collected from registered swap data repositories (SDRs). The joint project will build on the CFTC's work with the SDRs to harmonize data reporting and improve data quality, data standards, and over-the-counter (OTC) derivative product taxonomies. The CFTC and the OFR also announced the creation of a staff-level Interagency Data Quality and Analytics Working Group to coordinate the structuring of this cooperative project focusing on data quality and the use of analytical tools for regulatory purposes.

The MOU establishes a process for assessing the quality of the data. The assessment will form the basis for the subsequent development of a project plan for understanding swaps and other OTC derivative transactions and their impact on financial stability. The project plan will define the scope, content, and intended outcomes of further collaboration between OFR and the CFTC, to advance their common goal of improving the quality and utility of data collected under the authority of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (Dodd-Frank Act).

"One of the signature achievements of Dodd-Frank is that regulators now have a picture of the size and the scope of the derivatives market for systemic risk purposes," said CFTC Acting Chairman Mark Wetjen. "Today's agreement with OFR will enhance the CFTC's ability to see and analyze the data reported to SDRs and continue a critical dialogue on how the agency, given resource constraints, can leverage OFR's expertise and resources to protect the American public."

OFR Director Richard Berner noted that the project relates to the OFR's mission of promoting financial stability. "At the OFR, we believe that fulfilling the promise of transparency in derivatives markets is vital," Berner said. "I applaud the CFTC for its leadership and pledge the commitment of the OFR to help make the data in swap data repositories as useful as possible to regulators and market participants for monitoring financial stability and regulating the industry."

## OTC Derivatives Regulators Issue Report to the G20

On March 31, 2014, the Over-the-Counter (OTC) Derivatives Regulators Group (ODRG), which is made up of authorities with responsibility for the regulation of OTC derivatives markets in

Australia, Brazil, the European Union, Hong Kong, Japan, Ontario, Quebec, Singapore, Switzerland, and the United States, issued a report that identifies the current list of remaining cross-border implementation issues related to global reform of the OTC derivatives markets. The report also includes a summary of the status of such issues and a timetable for addressing them through a series of reports to the G20 Finance Ministers and Central Bank Governors over the course of 2014.

## Enforcement Actions

The Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC) recently announced the following enforcement actions:

- The SEC announced two separate cases against individuals who profited by insider trading on confidential information they learned from their spouses about Silicon Valley-based tech companies. Without admitting or denying the allegations, one individual agreed to pay more than \$300,000 to settle the SEC's charges and the other individual agreed to pay approximately \$280,000.
- The SEC announced charges against a Florida-based financial services firm for improperly calculating advisory fees and overcharging clients. The firm agreed to settle the SEC's charges and has reviewed client records and reimbursed 2,304 current and former client accounts with refunds and credits totaling \$553,624, including interest. In the settlement, the firm agreed to pay an additional \$553,624 penalty.
- The SEC charged two friends with insider trading on confidential information from an investment banker about an impending transaction between engineering and construction companies. The SEC's complaint charges the individuals with violations of Section 10(b) of the *Securities Exchange Act of 1934* and Rule 10b-5. In addition to a financial sanction of \$528,175 in disgorgement and prejudgment interest, one individual has consented to the entry of a judgment permanently enjoining him from violations of Section 10(b) of the Exchange Act and Rule 10b-5.
- The SEC charged the owner of a New Jersey-based brokerage firm with manipulative trading of publicly traded stocks through an illegal practice known as "layering" or "spoofing," whereby a trader places orders with no intention of having them executed but rather to trick others into buying or selling a stock at an artificial price driven by the orders that the trader later cancels. The SEC also charged the owner and other firms with registration violations. Two firms and five individuals agreed to pay a combined total of nearly \$3 million to settle the case.
- The CFTC obtained a federal court supplemental consent Order requiring two Florida-based defendants and their North Carolina-based company to jointly pay a total of \$5.76 million in civil monetary penalties for defrauding customers through a retail foreign currency trading scheme.
- The CFTC announced that a U.S. District Court entered a final judgment Order imposing a civil monetary penalty of almost \$6 million against a Florida-based defendant and his Pennsylvania-based company in a CFTC enforcement action. The court's Order followed an earlier default judgment Order finding that the defendants had committed fraud and imposing registration and trading bans.
- The CFTC announced that a U.S. District Court entered permanent injunction Orders against two Florida-based residents and their companies that were sued by the CFTC for their role in a multi-million dollar precious metals scheme. The Orders require one defendant and his company to jointly pay \$750,515 in restitution to their customers and a \$1.5 million civil monetary penalty, and the other individual and his company to jointly pay \$380,664 in restitution and a \$750,000 civil monetary penalty. The Orders also impose

permanent solicitation, trading and registration bans against the defendants, and prohibit them from further violations of the *Commodity Exchange Act* (CEA) and CFTC regulations.

- The CFTC announced that a U.S. District Court entered a consent Order requiring a collapsed global financial derivatives brokerage firm to begin making final restitution payments to its customers to satisfy its obligation of full restitution for \$1.212 billion in losses sustained by the firm's customers when it failed in 2011. In addition to full restitution, the consent Order imposed a \$100 million civil monetary penalty on the firm to be paid after it has fully paid customers and certain other creditors entitled to priority under bankruptcy law.



## Recent Supervisory Actions against Financial Institutions

Last Updated: April 4, 2014

Agency	Institution Type	Action	Date	Synopsis of Action
CFPB	Mortgage lender	Notice of Charges	1/29	The Bureau of Consumer Financial Protection initiated an administrative proceeding against a New Jersey-based mortgage lender and its affiliates for a mortgage insurance kickback scheme. The Bureau is seeking a civil fine, a permanent injunction to prevent future violations, and restitution.
CFPB	Mortgage lender	Consent Order	1/16	The Bureau of Consumer Financial Protection ordered a Missouri-based mortgage lender and its former owner and current president to pay \$81,076 for funneling illegal kickbacks to a bank in exchange for real estate referrals.
OCC	Large financial institution	Order for Civil Money Penalty	1/7	The Office of the Comptroller of the Currency announced a \$350 million civil money penalty against three affiliated banks for Bank Secrecy Act (BSA) violations. The penalty follows a January 2013 cease and desist order in which the three banks were directed to correct deficiencies in their compliance programs.
Federal Reserve Board	State member bank	Civil Money Penalty	01/09	The Federal Reserve Board entered into an Order of Assessment of Civil Money Penalty with a Texas-based state member bank to address violations of the National Flood Insurance Act.
Federal Reserve Board	State member bank	Civil Money Penalty	01/09	The Federal Reserve Board entered into an Order of Assessment of Civil Money Penalty with a New York-based state member bank to address violations of the National Flood Insurance Act.
CFPB	Large financial institution	Consent Order	12/23	The Bureau of Consumer Financial Protection entered into a Consent Order with a large financial institution to resolve the CFPB's claims that the institution engaged in a pattern or practice of discrimination on the basis of race and national origin in residential mortgage lending in violation of the Equal Credit Opportunity Act. The Consent Order requires the institution to pay \$35 million in restitution.
CFPB, OCC, FDIC	Various	Consent Order, Order for Restitution, Order for Civil Money Penalty	12/23	The Bureau of Consumer Financial Protection, Office of the Comptroller of the Currency, and Federal Deposit Insurance Corporation each participated in actions against a financial institution and certain of its subsidiaries to address unfair and deceptive marketing practices related to credit card "add on" products. Collectively, the orders require \$59.5 million in restitution and civil money penalties of \$16.2 million.
CFPB	Large financial institution	Consent Order, Civil Money Penalty	12/20	The Bureau of Consumer Financial Protection entered into a Consent Order to with a resolve the CFPB's claim that the financial institution, an indirect auto lender, violated the anti-discrimination provisions of the Equal Credit Opportunity Act. The institution was required to pay \$80 million in damages to affected borrowers and an additional \$18 million civil money penalty.

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