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Washington Update

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**Presented By:
Patton Boggs LLP**

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Legislative Update: Financial Regulatory Reform

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Financial Regulatory Reform

- I. Consolidation and Reorganization of Regulators**
- II. Oversight, Systemic Risk, and the Role of the Federal Reserve**
- III. Consumer Protection Initiatives**
- IV. Hedge Funds and Other Unregulated Entities**
- V. Credit Rating Agencies**
- VI. Derivatives**
- VII. The Insurance Industry**
- VIII. Executive Compensation Restrictions**
- IX. The House & Senate Fall 2009**

I. Consolidation and Reorganization of Regulators

- The Administration's Proposal Would:
 - Eliminate the OCC and the OTS.
 - Create a National Bank Supervisor.
 - Force SEC and the CFTC to harmonize their statutory and regulatory frameworks in lieu of merging the agencies.
 - Create a new entity, the Consumer Financial Protection Agency (CFPA).
 - Create a Financial Oversight Council (Council) to support the Fed in their monitoring of systemic risk.

II. Oversight and Regulation of Systemic Risk and the Role of the Federal Reserve

- The Administration's Proposal:
 - The Fed would have the authority to monitor systemic risk and exercise resolution authority.
 - In consultation with the Treasury, the Fed would promulgate rules to guide the identification of Tier 1 Financial Holding Companies (FHCs).
 - And in consultation with the Council, the Fed would set prudential standards for Tier 1 FHCs to maximize financial stability.
- Opposition to the Fed: The SEC and FDIC, as well as some members of Congress, are skeptical of the Fed taking on this role and would prefer that the Council be given greater power as it is comprised of agency heads that would be better equipped to understand systemic risk. Additionally, the Fed has previously failed in this role.

III. Consumer Protection Initiatives

- **Administration's Proposal:**
 - The CFPA would have broad authority to enact consumer protection regulations that impact a broad range of financial products and services.
 - Among other things, lenders would be required to offer “Plain Vanilla” loans before other products could be offered and consumers would need to be adequately warned of the risks of other products.
 - The CFPA rules would constitute a floor, not a ceiling for states.
- **Congress:**
 - In December, Financial Services Committee Chairman Barney Frank (D-MA) shepherded the Wall Street Reform and Consumer Protection Act to passage in the House despite strong opposition from industry and Republicans. The legislation does not, however, mirror the Administration's proposal. For example, there is no “plain vanilla” requirement and the CFPA is headed by a board and not a single director.
 - Senate Banking Committee Chairman Chris Dodd (D-CT) has circulated a draft proposal and hopes to have a bill for consideration by end of January
 - In May 2009, Congress passed the CARD Act, which protects consumers from certain practices employed by credit card companies.

IV. Regulation of Hedge Funds and Other Unregulated Entities

- **Administration's Proposal:**
 - **All advisers to hedge funds and other private pools of capital that have more than \$30 million of assets under management, would be required to register with the SEC under the Investment Advisers Act.**
 - **The investment adviser would have to file public reports and keep, records, and other documents that the SEC deems necessary to protect investors and the public interest.**
 - **The SEC would conduct regular examinations of these funds and share the information with the Fed and Council in order to determine if they should have Tier 1 FHC status.**
- **IRS Action: In June 2009, the IRS announced that all hedge funds and private equity investors must disclose their off-shore investments.**

V. Regulation of Credit Rating Agencies

- **SEC Action:** In April 2009, a new rule went into effect that requires nationally recognized statistical rating organizations (NRSROs) to provide enhanced disclosures on the manner in which they measure performance, and the procedures and methods they use to determine ratings. This is an effort to strengthen previously enacted legislation.
- **Administration's Proposal:** In July 2009, the Administration sent a proposal to Congress that would not only provide for increased transparency and oversight of NRSROs, but would reduce market reliance on these organizations, reduce conflicts of interest at these organizations, and require them to register with the SEC.

VI. Regulation of Derivatives

- **Administration's Proposal:**
 - Regulators would be required to impose capital, reporting, and margin requirements on all derivative dealers.
 - All standardized OTC derivatives would be cleared through a regulated central clearing house and traded on either an SEC or CFTC regulated exchange or a regulated transparent electronic trading system. (The House bill includes an exemption for most end users that can demonstrate a legitimate business use).
 - Tailored swap transactions would be regulated to ensure that such transactions are not used solely as a means to avoid clearing requirements.
- **Market Reforms:** In April 2009, the International Swaps and Derivatives Association agreed to abide by certain market reforms, with the goal of facilitating centralized clearing of swaps.

VII. Regulation of the Insurance Industry

- Administration's Proposal:
 - Office of National Insurance (ONI) would be created within Treasury.
 - ONI would monitor insurance industry for any financial troubles and recommend insurance companies for supervision as Tier 1 FHCs.
- Congress:
 - Administration's proposal is consistent with Rep. Bean's (D-IL) proposed bill, "National Insurance Consumer Protection Act" (H.R. 1880).
 - Rep. Kanjorski's (D-PA) bill, the "Insurance Information Act," (H.R. 2609) mirrors Administration's proposal and was passed out of committee in December.

VIII. Executive Compensation Restrictions

- Executive compensation restrictions for those who received or will receive TARP funds under the Emergency Economic Stabilization Act (EESA) (as amended by the American Recovery and Reinvestment Act).
- Treasury Interim Final Rule places restrictions on compensation structures for Senior Executive Officers, created pursuant to the EESA.
- Compensation Czar oversees compensation structures of 7 largest companies receiving TARP funds and advises others who received federal assistance.
- Both Senate and House have introduced measures to prohibit or limit various forms of bonuses.
- Recent events demonstrate compensation practices will remain on Congress' agenda.

IX. The House & Senate in 2010

- **House:**
 - **Chairman Frank's agenda in Financial Services Committee will certainly include a push to pass financial regulatory reform legislation and will likely include GSE reform, Internet gambling, and market structure issues.**
 - **The committee will also continue to focus on housing issues as more American families lose their homes in foreclosure.**
- **Senate:**
 - **Chairman Dodd's decision not to run for reelection in 2010 alters political landscape but full impact not yet clear. He may be more willing to push Administration's agenda and risk a partisan outcome or he may act to preserve his legacy and continue to work with Republicans to reach some level of consensus.**
 - **Sen. Dodd has formed working groups among committee members to iron out differences on major issues such as the CFPA, Fed authority and regulation of derivatives.**
 - **The Senate may have a bill to consider during the first quarter of 2010 but Republican opposition will likely delay passage and the eventual conference to reconcile the House and Senate bills.**

Regulatory Issues

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Update on other issues

- **Federal Deposit Insurance developments**
- **Credit CARD Act implementation**
- **OFAC Penalties**
- **FinCEN initiatives**
- **Other AML developments**
- **Other issues**

Federal Deposit Insurance

- **Failed Banks**
 - **2009's final tally**
 - **2010 predictions**
- **Resolution strategies continue to evolve**
 - **Role of private equity**
- **Temporary Liquidity Guarantee Plan extended to 6/30/10**
 - **Planned phase-out for Debt Guarantee Program**
- **Extended \$250,000 coverage to 12/31/13**
 - **Twist for insured foreign branches**
- **Deposit insurance premiums – the stick**
 - **Executive compensation**
 - **Activities**

Credit CARD Act Implementation

- **Timetable**
- **Status of Reg Z changes**
- **Stored value/prepaid care rulemaking**
- **FinCEN rulemaking directive for stored value**
- **Other required actions/studies**
- **Latest developments**

OFAC

- **Credit Suisse - \$526 million for Iranian Transactions**
- **Lloyds TSB Bank - \$217 million (plus \$350 million?)**
- **More to come?**
- **Iran-Venezuela**
- **DHL - \$9.44 million (Iranian and Sudan)**
- **Australia and New Zealand Bank Group, Ltd. - \$5.75 million (Sudan)**
- **Global terrorism sanctions: financial, material, or technological support" - any property, tangible or intangible**
- **Economic Sanctions Enforcement Guidelines**
- **Cuban Assets Control Regulations amendments**
- **Financial Sector Symposium**
- **MOUs with other regulators to leverage resources**

FinCEN's Initiatives

- **Mortgage lenders and originators**
- **And .. other finance companies (?)**
- **CTRs for mutual funds?**
- **Section 314(a) for state, local and foreign governments**
- **Section 314(b) safe harbor for (mortgage) fraud**
- **Money services businesses (inc. stored value)**
- **Stored value as required by Credit CARD Act**
- **Revised Bank BSA/AML Examination Manual?**

FinCEN MSB/Stored Value Proposal

- **Require foreign MSBs to register even if no physical presence?**
- **Better stored value definition ?**
 - Technologically neutral and consistent with actual use of store value within the economy
 - Neutral in regards to the type of entity that provides/issues the stored value.
- **Alternative - electronic monetary value generally accepted as medium of exchange, whether or not redeemable for currency or funds.**
- **Treat stored value as a form of money transmission? Impact on industry, law enforcement and regulators?**

FinCEN MSB/Stored Value Proposal

- **Are distinctions between open and closed loop systems still meaningful?**
- **Should open loop and closed loop stored value be regulated differently and if so, how?**
- **Should only certain uses or types of value transfers involving stored value be considered money transmission?**
- **Which stored value participants - issuers, sellers, redeemers - should be regulated and why?**
- **Retain thresholds?**

FinCEN MSB/Stored Value Proposal

- **Differing regulatory requirements if stored value product in bearer form or anonymous versus tied to an identifiable account holder?**
- **Regulate memory chip products differently from magnetic strip products?**
- **Comment period closed September 9, 2009.**
 - **Major trade associations and a few entities commented**
 - **Various areas of law enforcement encouraged to participate in rule-making**

Mortgage and Other Finance Companies

- **2003 Advanced notice of proposed rulemaking**
 - **Persons involved in real estate closings and settlements**
- **Significant research and reports on mortgage fraud**
 - **Interagency effort on foreclosure rescue scams and loan modification**
 - **Mortgage fraud SAR analysis**
- **35 + ongoing investigations**
- **Nonbank residential mortgage lenders and originators**
 - **AML program and SAR requirement proposed**
 - **Others?**
- **Incremental approach to other loan and finance companies?**

Other AML/CFT and Related Developments

- **Tax evasion, tax evasion, tax evasion**
 - **IRS v. Switzerland**
 - UBS Agreement
 - DOJ/IRS-Swiss Agreement
 - Swiss government's rejection
 - **Asia – the next frontier?**
 - **SARs?**
- **SWIFT, IAT, regulatory policy and more**
- **Political corruption**
- **Moving beyond AML**
 - **Foreign Corrupt Practices Act**
 - **Financial Fraud Task Force - mortgage fraud, securities, economic stimulus programs, and predatory lending**
- **Online gambling – regulatory delay and indictment**
- **FTC MoneyGram Order - \$18 million**

Data Security/Privacy/ Identity Theft

- **Heartland Payments Settlement**
- **FTC Actions**
- **Federal legislation**
 - **H.R. 2221/S.1490 (Leahy)/S.139 (Feinstein)**
 - **Boucher draft**
- **Cell phones**
- **Identity Theft red flags**
 - **Extension**
 - **Exemptions - lawyers/small businesses – accountants next?**

Issues to Watch

- **Financial Fraud Task Force**
- **Foreign AML enforcement actions against US organizations**
- **GAO report on regulators' rulemaking failures**
- **Basel II dead? On to Basel III?**
- **TARP in a new decade**
- **Privacy – Patriot Act 215, NSLs**
- **Prepaid Phone Cards – Escheatment and Beyond**
- **FTC as de facto regulator**
- **Data Security/Privacy legislation**
- **IRS proposal for reporting credit/debit/prepaid card transactions**

Regulatory Reform: Conclusion

- **Plan for the future**
- **Analyze your business model**
- **Consider how legislation should be amended**
- **Construct legislative history**
- **Assess the impact**
- **Comment on regulations**
- **Be prepared!**

Questions?

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