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MARKET SOLUTIONS

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MARKET SOLUTIONS

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Market Solutions is a quarterly newsletter about the activities of the Financial Markets Association as well as legislative/regulatory developments of interest to FMA members. The opinions expressed in this publication are those of the authors, not necessarily those of the Association and are not meant to constitute legal advice. *Market Solutions* is provided as a membership service of the **Financial Markets Association**, 333 2nd Street, NE - #104, Washington, DC 20002, *dp-fma@starpower.net*, 202/544-6327, *www.fmaweb.org*. Please let us have your suggestions on topics you would like to see addressed in future issues.

FMA FINANCIAL MARKETS ASSOCIATION

FINRA's New Consolidated Supervision Rules

By Hank Sanchez
Oyster Consulting, LLC

Overview

On December 23, 2013, the SEC approved changes to the FINRA supervisory and supervision rules, and consolidated certain NYSE rules into these new rules (the "Approval Release")[1]. The effective date for the new Rules was December 1, 2014.

As many in the industry know, the finalization of the rule changes was not that simple. The initial volley discussing the proposed rules was launched in May 2008 with Regulatory Notice 08-24. The proposal languished until, in September 2011, FINRA, without explanation, withdrew the initial proposal[2]. The proposal was resurrected on June 21, 2013, when FINRA filed with the SEC an updated version of the proposal[3]. There were over 570 total comments sent in to the SEC. On October 2, 2013, FINRA responded to the comments and filed an amendment to the proposed rule change[4]. While several comments supported the proposal, other comments discussed concerns related to such things as the definition of "covered accounts" (discussed below) and the single supervisor requirement, as well as the documentation requirements relating to customer complaints, and the additional testing required.

FINRA Regulatory Notice 14-10, released in March 2014, discusses the rule changes and should be reviewed by firms' legal and compliance teams, as well as with the business and supervisory teams. Below is a summary of the key provisions of the new rules and a discussion of the effect of the rules on FINRA member firms. While most of the changes truly are a consolidation of existing rules, there are some things that firms should be aware of both in updating their current procedures and how they test those procedures.

As noted in the Approval Release, FINRA made the changes as part of the process of consolidating its rulebook. In sum, the changes are shown in the table on page 3.

The new rules retain some of the prior requirements of NASD Rules 3010 and 3012

- Branch inspection cycles: (3110 (c)(1)(A) through (C));
- Requiring that the person conducting branch inspections is sufficiently independent from the branch and persons in the branch: (3110 (c)(3)(B)); and
- Procedures for the monitoring of registered representatives' activities (3110).

Interestingly, none of the commentators to the proposed rules, and none of the FINRA discussions about the rules discuss what firms should do vis-à-vis their next 3120 Report (formerly

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Legislative/Regulatory Actions

This column was written by lawyers from Morrison & Foerster LLP to update selected key legislative and regulatory developments affecting financial services and capital markets activities. Because of the generality of this column, the information provided herein may not be applicable in all situations, and should not be acted upon without specific legal advice based on particular situations.

In this issue, we address various selected developments with regard to the **Volcker Rule**, **Derivatives** in connection with the Dodd-Frank Act's Title VII and general updates from the Commodity Futures Trading Commission (CFTC), and the **Consumer Financial Protection Bureau (CFPB)**.

VOLCKER RULE

Federal Reserve Board Extends the Volcker Rule Conformance Period for Legacy Funds

On December 18, 2014, the Board of Governors of the Federal Reserve System issued an order extending for an additional year—i.e., until July 21, 2016—the Volcker Rule conformance period for banking entities to conform their investment in and relationships with covered funds and with foreign funds that may be subject to the Volcker Rule, and that were in place prior to December 31, 2013 ("legacy funds"). The order also announces the Board's intention to grant the final one-year extension of the conformance period pursuant to its authority until July 21, 2017. No extension was granted for the conformance period for proprietary trading, which still will expire on July 21, 2015.

In the Board's view, the extensions allow for the divestiture of fund investments in an orderly manner consistent with protecting the safety and soundness of banking entities, reduce potential disruptive effects that significant divestitures of covered funds could have on markets, allow banking entities additional time to conform their relationships with covered funds, and are consistent with the legislative history of Section 619 of the Dodd-Frank Act.

It is hoped that during the extensions of the conformance period, the regulatory agencies will address certain interpretive issues under the Volcker Rule not discussed in the order that have made it difficult for banking entities to make definitive choices in order to be in compliance.

For more information, please read our client alert at ***http://www.mofo.com/~/media/Files/ClientAlert/2014/12/141224FRBExtendsVolcker.pdf.***

House Passes Bill to Ease Volcker Rule and Other Regulatory Requirements

On January 14, 2015, the U.S. House of Representatives voted (271-154) to pass H.R. 37, the "Promoting Job Creation and Reducing Small Business Burdens Act." If enacted, the bill, among other things, would extend the Volcker Rule conformance date for collateralized loan obligations and ease requirements for investment advisers of small business investment companies and venture capital firms. The bill also includes a number of measures that correct issues arising in the JOBS Act, or that otherwise are intended to promote capital formation, to reduce regulatory burdens, and for other purposes.

For more information, please read our client alert at ***http://www.mofo.com/~/media/Files/ClientAlert/2015/01/150116VolckerRule.pdf.***

DERIVATIVES UPDATE

The phase-in of Title VII of the Dodd-Frank Act and the regulations thereunder continues. It appears that many cross-border issues remain unresolved.

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FMA Welcomes New Members!

Lilanthi Alahendra	Navigant
Mauricio Angee	Mercantil Commercebank, N.A.
Neil Baritz	Baritz & Colman LLP
Rostin Behnam	Senate Agriculture Committee
Bradley Berman	Morrison & Foerster LLP
Karina Bjelland	Navigant
Michael Blayney	WilmerHale
Joe Borg	Alabama Securities Commission
Annmarie Boyd	FDIC

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However, progress has continued. ISDA in November published an important protocol under which, among other things, certain swaps market participants have agreed to give cross-border effect to certain special resolution regimes. In addition, the CFTC and the prudential banking regulators have reproposed margin requirements for uncleared swaps.

Federal Reserve Board and OCC Issue Interim Final Rule Amending U.S. Bank Capital and Other Rules to Account for Global Implementation of Bank Special Resolution Regimes

The EU regulators' determination late last year not to recognize U.S. central counterparties (CCPs) under European legislation, while at the same recognizing CCPs located in Australia, Hong Kong, Japan, and Singapore, illustrates the ongoing difficulties with the cross-border application of swaps regulations. The European authorities did not recognize U.S. CCPs because they determined that the U.S. regulatory framework might not be "equivalent" to the EU framework. The EU extended its deadline for recognition of non-EU CCPs by six months, to June 15, 2015. A refusal by the EU to timely recognize U.S. CCPs would put those CCPs in a difficult position, as they would not constitute "Qualifying CCPs" for purposes of Basel III risk-weighting, and European banks would incur prohibitive costs to clear transactions through such CCPs.

The EU's refusal to recognize U.S. CCPs may be understood as part of an ongoing tug of war with the U.S. regulators over whose regulatory requirements will apply to which market participants and which transactions. In the European Commission press release announcing the recognition of Australia, Hong Kong, Japan, and Singapore CCPs, Michel Barnier, the European Commissioner for Internal Markets and Services, was quoted as stating that such recognition demonstrated that "EU is willing to defer to the regulatory frameworks of third countries, if they meet the same objectives as EU rules," and that EU regulators are in close dialogue with the CFTC and SEC "as we develop our assessments of their respective regimes and discuss their approaches to deference." In a somewhat analogous (but reversed) situation last year, the CFTC, as a condition to no-action relief for certain EU-regulated multilateral trading facilities (MTFs), required such MTFs to demonstrate, on a requirement-by-requirement basis, that many of the regulatory requirements established by governmental authorities in their home countries were in accordance with the CFTC's own regulatory requirements for swap execution facilities. The CFTC's requirement-by-requirement approach to cross-border recognition appeared to set a higher bar than does the EU's "same objectives" approach, and to signal that the CFTC will give little deference to non-U.S. regulators.

Recent developments also include ISDA's launch, in November of last year, of the ISDA 2014 Resolution Stay Protocol. The protocol is intended to address the possibility that the failure of a large bank could destabilize markets in the event of a close-out of such bank's derivatives book. Many jurisdictions have addressed this issue, or may soon address it, by means of legislation such as the orderly liquidation authority provisions of Title II of Dodd-Frank. The protocol clarifies the cross-border application of such special resolution regimes by providing that, when a party adheres to the protocol, such party opts into the provisions of certain special resolution regimes to which its counterparties may be subject. Adhering parties also agree to give up certain cross-default rights. In a conforming rulemaking, U.S. regulators have issued an interim final rule amending the definition of "qualifying master netting agreement" under regulatory capital, liquidity coverage ratio, and lending limits rules to ensure that the treatment of certain financial contracts will not be affected by the protocol or by the implementation of special resolutions regimes in foreign jurisdictions. For

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2015 Examination Priorities

SEC

http://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2015.pdf

FINRA

http://www.finra.org/Newsroom/NewsReleases/2015/P602237

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further information, see our Client Alert, available here: ***http://www.mofo.com/~/media/Files/ClientAlert/2015/01/150112FRBOCCInterimFinalRule.pdf.***

Prudential Regulators and CFTC Repropose Margin Requirement Rules for Uncleared Swaps

Further, last fall both the CFTC and the prudential banking regulators reproposed margin rules for uncleared swaps; they originally proposed such rules in 2011. With certain significant exceptions, the new proposals are intended to conform to the international framework for margin for uncleared swaps stated by the Basel Committee on Banking Supervision (BCBS) and the International Organization of Securities Commissions (IOSCO). One significant area where the U.S. regulators have not followed the BCBS/IOSCO framework relates to the definition of "material swaps exposure," a calculation of the aggregate notional amount of swaps that may require a financial end user to provide initial margin. The U.S. proposals define "material swaps exposure" as a much lower aggregate notional amount than that required by the BCBS/IOSCO framework. The U.S. proposals, if adopted in final regulations, would thus require many more financial end users to provide initial margin than would be the case under the BCBS/IOSCO framework. For further information regarding the CFTC's and prudential regulators' proposed margin rules, see our Client Alert, available here: ***http://www.mofo.com/~/media/Files/ClientAlert/2014/11/141113RulesforUnclearedSwaps.pdf.***

CFTC Excludes Certain Swaps with Utility Special Entities from the Special Entity *de Minimis* Calculation for Purposes of Swap Dealer Registration

On September 26, 2014, the CFTC published a final rule in the *Federal Register* permitting a person to exclude "utility operations-related swaps" entered into with "utility special entities" in calculating the aggregate gross notional amount of the person's swaps positions for purposes of the *de minimis* exception from swap dealer registration applicable to swaps with special entities. The final rule means that such swaps are now subject to the general $8 billion notional *de minimis* exception threshold from swap dealer registration (which is set to fall to $3 billion), rather than the much lower threshold of $25 million for other special entities. The final rule became effective on October 27, 2014. For more information, please see our client alert at ***http://www.mofo.com/~/media/Files/ClientAlert/2014/10/141009CFTCExcludesCertainSwaps.pdf.***

Congress Limits Swaps Pushout Requirement to Certain ABS Swaps

On December 16, 2014, President Barack Obama limited the scope of swaps and security-based swaps subject to the Dodd-Frank Act's pushout requirement to certain asset-backed security swaps when he signed into law the Consolidated and Further Continuing Appropriations Act, 2015. This Act contains an amendment to Section 716 of the Dodd-Frank Act, commonly known as the Lincoln Amendment, or the Swaps Pushout Rule. The new amendment also codifies the Federal Reserve's rule that uninsured branches and agencies of foreign

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FMA Welcomes *More* New Members!

David Fredrickson	SEC
Melissa Gohs	Raymond James Financial Services
David Harris	Senior Risk & Compliance Counsel
Anthony Hays	CFTC
Daniel Hugunine	Balch & Bingham LLP
Ronald Long	Wells Fargo Advisors
Suzanne McDougall	Renaissance Regulatory Services, Inc.
William Mack	Greenberg Traurig, P.A.
Jonathan Marcus	CFTC
Marshall Martin	City National Bank of Florida
Jason Maxwell	Regions Bank

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banks may receive the same exceptions as insured depository institutions (IDIs) from the pushout requirement. As amended, IDIs and uninsured branches and agencies of foreign banks that are swap dealers or security-based swap dealers will only be required to push out swaps based on an asset-backed security or a group or index primarily comprised of asset-backed securities, defined in the amendment as "structured finance swaps." Such institutions may nonetheless enter into structured finance swaps if (i) they are undertaken for hedging or risk management purposes or (ii) each asset-backed security underlying such structured finance swaps is of a credit quality and of a type or category with respect to which the Prudential Regulators have jointly adopted rules authorizing such swap activity. For more information, please see our client alert on this topic at: ***http://www.mofo.com/~/media/Files/ClientAlert/2014/12/141222SwapsPushoutRequirements.pdf.***

CFTC and SEC Propose Interpretation Concerning Forward Contracts with Embedded Volumetric Optionality

On November 13, 2014, the CFTC and the SEC federal approved for publication in the *Federal Register* a proposed interpretation clarifying the CFTC's interpretation regarding forwards with embedded volumetric optionality contained in the Product Definitions Release. Forwards with embedded volumetric optionality are contracts for the forward delivery of a nonfinancial commodity, but contain optionality as to the quantity of commodity to be delivered. The proposed interpretation would modify the seventh element of the original interpretation to read that "[t]he embedded volumetric optionality is primarily intended, at the time that the parties enter into the agreement, contract, or transaction, to address physical factors or regulatory requirements that reasonably influence demand for, or supply of, the underlying commodity." The modification is intended to reduce uncertainty as to the reason for exercise of the embedded optionality by making the inquiry about the intent of the parties at contract initiation (as opposed to the time of exercise under the original interpretation). For this purpose, the interpretation states that parties may reasonably rely on counterparty representations regarding the intended purpose of the embedded optionality. In addition, the modification is designed to recognize that contracting parties may have some degree of influence or control over physical or regulatory factors affecting supply and demand, as opposed to being "outside their control" as required in the original interpretation. The proposed interpretation also states that physical factors would be construed broadly to include any fact or circumstance that would reasonably influence the parties' supply of or demand for the nonfinancial commodity. The comment period for the proposed interpretation closed on December 22, 2014. For more information, please see our client alert available at ***http://www.mofo.com/~/media/Files/ClientAlert/2014/12/141212CFTCSECVolumetric.pdf.***

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FMA Welcomes *More* New Members!

James Montfort	Goodwin Procter LLP
Scott Nance	Wiley Rein LLP
Bao Nguyen	Kaufman, Rossin & Co.
Scott Norton	BankUnited
Elizabeth Osterman	SEC
Robert Pargac	Navigant
Brian Quinn	SEC
William Reilly, Jr.	Oyster Consulting, LLC
Susana Rodriguez	Navigant
Elad Roisman	Senate Banking Committee
Evan Rosser	Oyster Consulting, LLC
Alfred Saikali	Shook, Hardy & Bacon LLP
Hank Sanchez	Oyster Consulting, LLC
Anne Small	SEC
Sandra Sojka	FinCEN
Daniel Stipano	OCC

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CFPB UPDATE

CFPB Weighs in on Lending to Servicemembers

On December 29, 2014, the CFPB released a report, entitled "The Extension of High-Cost Credit to Servicemembers and Their Families." According to the CFPB, the Report provides a "snapshot" of the market for "high-cost credit products" that are not currently covered by the Military Lending Act and Department of Defense (DoD) rules that implement that Act. The CFPB released the Report together with its comment letter to the DoD on its recent proposal to amend the regulation that implements the MLA. The DoD proposal would significantly expand the scope of the DoD's current regulation by applying the MLA to new types of creditors and credit products, including open-end credit, with special rules for credit cards. In its comment letter, the CFPB expressed support for the DoD's proposed expansion of the regulation. Comments on the DoD proposal to amend its MLA regulation were due on December 26, 2014. For our client alert on these developments, please visit ***http://www.mofo.com/~/media/Files/ClientAlert/2014/12/141231CFPB.pdf.***

CFPB Issues Long-Awaited Proposed Rule on Prepaid Cards

In November 2014, the CFPB issued a long-awaited proposed rule on the regulation of prepaid card products, which appeared in the *Federal Register* on December 23, 2014. The proposal, which would amend Regulation E and Regulation Z, is broader in scope than anticipated, going beyond conventional network-branded general-purpose prepaid cards to include payroll cards; some federal, state, and local government benefit cards; student financial aid disbursement cards; tax refund cards; and peer-to-peer payment products. The proposed rule would regulate every aspect of covered products, including disclosures, error resolution, and what the CFPB refers to as "credit features." Of particular note, the provisions regarding credit features, which include proposed amendments to Regulation Z, represent a significant departure from the prior regulatory treatment of overdraft services for other accounts subject to Regulation E. Comments on the proposed rule are due by early March 2015. For our client alert on this topic, please visit ***http://www.mofo.com/~/media/Files/ClientAlert/2014/11/141113CFPB.pdf.***

CFPB Finalizes Privacy Rule

On October 20, 2014, the CFPB announced that it had finalized its proposed rule addressing the annual privacy notice requirement under the Gramm-Leach-Bliley Act and Regulation P. The final rule was published in the *Federal Register* on October 28, 2014, and is effective as of that date. Under the final rule, which does not differ materially from the CFPB's proposed rule, financial institutions are still required to deliver an initial privacy notice to consumers in writing; however, institutions are permitted to post their annual privacy notice online, rather than mailing it to each customer, if certain conditions are met. Nevertheless, the new privacy disclosure rule is unlikely to ease the regulatory burden on many financial institutions. For our client alert on this topic, please visit ***http://www.mofo.com/~/media/Files/ClientAlert/2014/10/141021CFPBFinalRule.pdf.***

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JOB BANK

Results-driven and dynamic senior-level industry professional with a proven record of accomplishment in Basel implementation and regulatory, compliance, and legal risk management. Develops and implements comprehensive, integrated compliance and business infrastructures to fulfill regulatory mandates and support new strategic ventures, products, and transactions, including M&A and business model transformation. Manages sensitive regulatory relationships, examinations, and audits. A forward-thinking and innovative leader, with an in-depth understanding of evolving frameworks for international and domestic banking, securities, and derivatives activities. Contact David Harris at 980/254-2318 or ***wilson.david.harris@gmail.com.***

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CFPB Proposes Issuing No-Action Letters

On October 10, 2014, the CFPB issued notice of a proposed policy allowing staff to issue no-action letters for "innovative financial products or services that promise substantial consumer benefit." The proposal is specifically designed for new financial products or services for which the application of statutory or regulatory provisions is uncertain. The CFPB stated that such uncertainty may discourage market innovations by preventing development of or investment in consumer-friendly products because of the potential risk of enforcement or supervisory actions. To reduce the regulatory uncertainty for such emerging financial products or services, the CFPB is proposing a process by which an entity may submit a request for a no-action letter. For our client alert on this topic, please visit ***http://www.mofo.com/~/media/Files/ClientAlert/2014/10/141016CFPBNoActionLetter.pdf.***

FMA Welcomes *More* New Members!

Bill Strome	
Daniel Suarez	Kaufman, Rossin & Co.
Vaughn Swartz	TD Securities (USA) LLC
Naoto Takemoto	The Bank of Japan
Catherine Topping	FDIC
Danforth Townley	SEC
Elisha Tuku	Senate Banking Committee
Grace Vogel	PricewaterhouseCoopers LLP
David Weinberger	International Assets Advisory, LLC
John White	WeiserMazars
George Wilder	CFTC
James Wrona	FINRA

CFPB Enforcement Action Related to Deposit Account Advertising

On October 9, 2014, the CFPB announced a consent order with M&T Bank relating to the bank's advertising, marketing and promotion of checking accounts with an "inactivity conversion feature." The consent order alleged that the bank had deceptively advertised checking accounts as "free" or "no strings attached" without disclosing in its ads that if customers failed to maintain minimum account activity, they would be switched to fee-bearing accounts. The consent order does not challenge the dormant account fees themselves or the automatic conversion feature; instead, it targets the way the bank advertised its free checking accounts. The CFPB alleged that from 2009 to 2012, M&T assessed approximately $2.9 million in monthly maintenance fees, collecting approximately $2 million of these fees from about 59,000 consumers. M&T agreed to refund the fees collected, reduce charged-off balances by the amount of the remaining fees assessed, and pay a $200,000 civil monetary penalty. ■

**Leonard N. Chanin, Julian E. Hammar, Ryan H. Rogers, James Schwartz, and Diana E. Whitaker contributed to this column.*

We hope to see you in sunny Fort Lauderdale in April.