

**MEMORANDUM TO:** Board of Directors

**FROM:**

Bret D. Edwards   
Director  
Division of Resolutions and Receiverships

Charles Yi   
General Counsel  
Legal Division

**SUBJECT:**

Notice of Proposed Rulemaking Regarding the Recordkeeping  
Requirements for Qualified Financial Contracts -12 CFR Part 371

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**RECOMMENDATION:** That the Board of Directors (the “Board”) of the Federal Deposit Insurance Corporation (the “FDIC”) approve the publication of the attached Notice of Proposed Rulemaking (the “proposed rule”) titled *Recordkeeping Requirements for Qualified Financial Contracts*. The proposed rule would amend and restate in its entirety 12 CFR Part 371 (“Current Part 371”), which was adopted by the Board in December, 2008. If the proposed rule is approved by the Board, it would be published in the *Federal Register* for a 60-day public comment period.

**INTRODUCTION:** The Board adopted Current Part 371 in order to implement 12 U.S.C. 1821(e)(8)(H), which authorizes the FDIC, in consultation with the other federal banking agencies, to prescribe regulations requiring detailed recordkeeping with respect to qualified financial contracts (“QFCs”) by insured depository institutions (“IDIs”) in a troubled condition. The information is of significant importance to the FDIC in the event that such an IDI subsequently fails, as it enables the FDIC, as receiver, to make informed decisions with respect

to the treatment of QFCs during the one-business-day stay period provided with respect to these contracts under the Federal Deposit Insurance Act.<sup>1</sup>

Current Part 371 sets forth the process by which an IDI becomes subject to its recordkeeping requirements. Current Part 371 also sets forth, in table form, the QFC information that an IDI subject to the rule must maintain.

The modifications to Part 371 set forth in the proposed rule will make certain changes to the recordkeeping requirements to conform recordkeeping requirements for certain IDIs to the comparable requirements of certain financial companies under Part 148, as well as to update the recordkeeping requirements for other IDIs and to make other changes as discussed below. As required by the governing statute (12 U.S.C. 1821(e)(8)(H)), FDIC staff has consulted with staff of the Board of Governors of the Federal Reserve System and the Office of Comptroller of the Currency regarding the proposed rule. The other banking agency staff raised no objection to the proposed modifications to Part 371.

## **DISCUSSION:**

### **I. General Background**

In the almost eight years since Current Part 371 was adopted, the FDIC has obtained QFC information pursuant to Current Part 371 from many IDIs in a troubled condition ranging in size from large, complex institutions to small community banks. This information has proved useful to the FDIC as a receiver in making informed decisions relating to the QFCs of failed IDIs and in planning for the resolution of IDIs in a troubled condition.

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<sup>1</sup> See 12 U.S.C. 1821(e)(10)(B).

On October 31, 2016, the Department of the Treasury published 31 CFR Part 148 (“Part 148”), which was formulated in consultation with FDIC staff and implements Section 210(c)(8)(H) of the Dodd-Frank Wall Street Reform and Customer Protection Act (the “Dodd-Frank Act”).<sup>2</sup> Part 148 sets forth QFC recordkeeping requirements for FSOC-designated systemically important financial companies and their affiliates, other global systemically important bank holding company corporate groups, and other financial company corporate groups of which at least one member has total consolidated assets of \$50 billion or more and, on a consolidated basis, a QFC portfolio that meets certain size thresholds.<sup>3</sup> The recordkeeping requirements of Part 148 are more extensive than those under Current Part 371 and were adopted on the recommendation of FDIC staff based on its experience under Current Part 371 in reviewing records maintained by certain large institutions with complex QFC portfolios. This experience also reinforced staff’s understanding that large IDIs are likely to have complex QFC portfolios. The additional data required by Part 148, which, among other data sets, includes detailed information about collateral, guarantees and credit enhancements, will significantly enhance the ability of the FDIC, as receiver under Title II of the Dodd-Frank Act, to judiciously exercise its rights and responsibilities relating to QFCs within the statutory one-business-day stay.

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<sup>2</sup> 12 U.S.C. 5390(c)(8)(H).

<sup>3</sup> Part 148 subjects to its recordkeeping requirements any financial company (other than an excluded entity as defined in 31 CFR 148.2(f) or one that has no QFCs) that (i) is subject to a determination that the company shall be subject to Federal Reserve supervision and enhanced prudential standards pursuant to 12 U.S.C. 5323; (ii) is subject to a designation as, or as likely to become, systemically important pursuant to 12 U.S.C. 5463; (iii) is identified as a global systemically important bank holding company pursuant to 12 CFR Part 217; or (iv) has total assets on a consolidated basis equal to or greater than \$50 billion, and on a consolidated basis has (1) total gross notional derivatives outstanding equal to or greater than \$250 billion or (2) derivative liabilities equal to or greater than \$3.5 billion. Part 148 also requires that QFC records be maintained for all members of the corporate group (other than any excluded entity or a company with no QFCs) of any such financial company.

Part 148's recordkeeping requirements do not apply to the QFCs of IDIs that are members of these corporate groups since QFC recordkeeping of IDIs is governed by Part 371.<sup>4</sup>

## II. **Proposed Amendments**

### A. **QFC Information for Large IDIs in a Troubled Condition and IDIs in a Troubled Condition that are part of Part 148 Reporting Groups**

The proposed rule would require IDIs in a troubled condition with \$50 billion or more in total consolidated assets and IDIs in a troubled condition that are members of corporate groups that are subject to Part 148 to maintain the same QFC information, in form and substance, as that required by Part 148. Part 148, as compared to Current Part 371, requires the maintenance of more QFC information in a format more aligned with current technology. Such expanded recordkeeping is appropriate for large IDIs because such IDIs are more likely to have complex and extensive QFC portfolios. Staff believes that such expanded recordkeeping also is appropriate for IDIs that are members of a corporate group that is subject to Part 148, regardless of the size of such IDIs, in order to ensure consistency of reporting across the entire corporate group. Consistency of reporting across the corporate group will enable the FDIC to better analyze how an IDI's QFC positions relate to QFC positions of other members of the corporate group and thus will provide useful information in the receivership of the IDI.

The principal new QFC information requirements for these institutions under the proposed rule are (i) new tables that require specific information about the governing agreement for each QFC, including governing law and whether the agreement includes a cross-default to a third party, (ii) tables that require more detailed information about collateral, including the

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<sup>4</sup> The Part 148 recordkeeping requirements also do not apply to subsidiaries of IDIs that are not (i) functionally regulated (as defined in 12 U.S.C. 1844(c)(5)); (ii) security-based-swap dealers as defined in 15 U.S.C. 78c(a)(71)); or (iii) major security-based swap participants (as defined in 15 U.S.C. 78c(a)(67)).

location of the collateral and a breakdown of collateral by item type; (iii) information about guarantees and other credit enhancements and, in the case of QFCs that are themselves guarantees or other credit enhancements, information about the QFCs that are guaranteed or credit-enhanced; (iv) information as to the next margin payment date; (v) identification of the governing master agreement or other netting agreement; (vi) information as to the entity holding the collateral for the QFCs; (vii) information about other positions to which a QFC relates, such as a loan whose interest rate is hedged by the QFC; (viii) a table for each counterparty (the “Counterparty Table”) listing the parent entities of the counterparty, in lieu of the Current Part 371 requirement that the IDI provide a list of affiliates of a counterparty with which it has entered into QFCs; and (ix) a table for the IDI and each of its affiliates (the “Corporate Organizational Table”) listing the parent entities of the IDI and its affiliates, in lieu of the organizational chart required by Current Part 371.

These IDIs would also be required to report QFC information for subsidiaries (“reportable subsidiaries”) that are not functionally regulated subsidiaries, security-based swap dealers or major security-based swap participants. Requiring this information under the proposed rule would enable the FDIC to analyze positions of other members of a corporate group that may affect an IDI in receivership since Part 148 does not require that information be maintained as to reportable subsidiaries.

#### **B. QFC Information for Smaller IDIs**

The proposed rule would make limited changes to the QFC recordkeeping requirements for smaller, “limited scope” IDIs (less than \$50 billion in total assets and not a member of a large corporate group that reports under Part 148), as it is less likely that these IDIs would have QFC positions of a magnitude and complexity that would justify the added burden of subjecting them

to the more extensive recordkeeping requirements for larger IDIs. Accordingly, two new tables that include detailed information as to collateral and provisions of governing agreements and that would be required to be maintained by other IDIs would not be required from smaller IDIs that are not members of corporate groups subject to Part 148. The two data tables that correspond to the tables set forth in Current Part 371 would be applicable to smaller IDIs under the proposed rule with modifications that enhance their usefulness. The changes include several new rows that require additional information. Most of this new information, while not expressly required under Current Part 371, is information that an IDI would maintain in order to provide the data required under Current Part 371. For example, while the proposed rule, unlike Current Part 371, would require that the master agreement or other netting agreement governing a QFC be identified, the exposure resulting from the netting required by such agreements is required by Current Part 371 to be set forth in the data tables. It is possible, however, that in some instances the new data proposed to be maintained may not have been maintained by smaller entities under Current Part 371. For example, the proposed rule would require that the next margin payment date and the amount of such payment be set forth in the data tables. Some smaller IDIs may not themselves track these requirements in advance of a margin call being made, although this information should be readily accessible to them.

The proposed rule also includes revised tables that include rows for information as to QFCs that are themselves guarantees or other types of credit enhancements, including information as to the guarantor and the underlying guaranteed QFCs, and new rows relating to credit enhancements issued in favor of the IDI. This information is not required to be set forth in the data tables of Current Part 371 but is the type of information that would be expected to be maintained in the ordinary course of business and be readily available to an IDI. Likewise, the

proposed rule requires information as to positions of the IDI or an IDI affiliate to which the QFC relates, as well as information as to the trade date of the QFC, all of which is information that would be expected to be maintained by and readily available to the IDI. Similarly, while the Counterparty Table and Corporate Organizational Table (including, in each case, the required identification of immediate and ultimate parent entities) are new, these Tables are required in lieu of affiliation information required, in a different form, by Current Part 371. The proposed rule would also eliminate requirements for information that has proved unclear or not useful under Current Part 371, specifically, the description of the purpose of a position, the documentation status of the position, and the calculation, obtainable from other information included in the tables, of the IDI's collateral excess or deficiency relative to the aggregate market value of all positions.

The proposal also would require that the information be maintained in the same format as the longer tables for larger banks, which is more flexible and makes better use of available technology. For example, the shorter tables for smaller banks would include two "look-up" tables (the longer tables would include four look-up tables), where information common across tables or rows would be entered once in a look-up table to ensure consistency and reduce error and thus allow repetitive data to be updated throughout the tables by simply making a single change in the applicable look-up data table entry. These two proposed look-up tables would provide information that is included in the IDI organization chart and lists of counterparty and IDI affiliates required under Current Part 371 and, accordingly, the proposed rule would eliminate the requirements for delivery of an organization chart and lists with information as to counterparty and IDI affiliates.

Overall, the revisions to the tables will increase the reporting requirements on institutions that have \$50 billion or more in total consolidated assets or are a member of a corporate group required to conform to the Part 148 recordkeeping requirements. For limited scope IDIs, the proposed rule would include significantly fewer revisions to the requirements under Current Part 371 and is not expected to cause significant additional burden to smaller institutions that do not have complex QFC portfolios. The notice of proposed rulemaking includes a question as to any additional burden that may result from the proposed changes to the current tables, as well as a question relating to the burden associated with the increased recordkeeping requirements of the expanded Part 148 tables.

**C. Cease and Desist Orders and Written Agreements to Improve Financial Condition**

As noted above, by law, QFC recordkeeping is required only with respect to IDIs “in a troubled condition.” The proposed rule would not make any change to the definition of “troubled condition.” That definition includes IDIs with composite ratings of 4 or 5 or, for IDIs with \$10 billion or more in total consolidated assets, composite ratings of 3; IDIs subject to proceedings for the suspension or termination of deposit insurance; IDIs subject to cease-and-desist orders or written agreements, or proceedings contemplating the same, requiring action to improve financial condition; IDIs that are informed that they are in troubled condition for purposes of 12 U.S.C. 1831i; and IDIs that have been determined to be experiencing significant deterioration of capital, significant funding difficulties or liquidity stress.<sup>5</sup> Although, in practice QFC recordkeeping requirements have been imposed primarily on the basis of an IDI’s composite rating, one of the five prongs of the definition of troubled condition in Current Part

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<sup>5</sup> This definition was based on the definition of troubled condition under 12 CFR 303.101(c), which requires from institutions in troubled condition and certain other IDIs advance notice of appointment of directors or senior executive officers.

371 is that an IDI is subject to a cease-and-desist order or written agreement issued by its appropriate federal banking agency that requires action to improve its financial condition or is subject to a proceeding initiated by such agency that contemplates the issuance of such an order. The preamble to the proposed rule provides additional background on what constitutes an order or agreement to improve financial condition to make clear that such an order or agreement can include consent agreements and stipulations and to clarify that cease-and-desist orders, written agreements, consent orders, and stipulations can be construed as requiring improvement to the financial condition of an IDI even if they do not specifically refer to the IDI's financial condition or need to raise additional capital.

#### **D. Time for Compliance with Part 371**

Current Part 371 requires IDIs to comply with the recordkeeping requirements of the regulation within 60 days after written notification by the institution's appropriate federal banking agency or the FDIC that it is in troubled condition under Part 371 or to obtain one or more extensions of up to 30 days each. Each extension must be requested no less than 15 days prior to the then-current deadline for compliance. Based on the FDIC's experience, large banks that have become subject to Current Part 371 may require 270 days or more to comply with the recordkeeping requirements. The need for FDIC staff and, in most cases, for the Board, to consider these extension requests each month has proved cumbersome and time-consuming. The proposed rule would retain the current timing requirements for all accelerated records entities, i.e., IDIs with a composite 4 or 5 rating or that are determined by their appropriate federal banking agency or the FDIC to be experiencing significant deterioration of capital or significant funding difficulties or liquidity stress. For these IDIs, for which the risk of near-term failure is greater than for other IDIs in troubled condition, the value of retaining the 60-day

compliance deadline and 30-day extension period outweighs the administrative burden of the process. However, for other entities, the proposed rule would provide for a 270-day compliance period, with extension periods of up to 120 days each. These longer time periods are appropriate for an IDI with a composite rating of “3” or that does not otherwise meet the definition of accelerated records entity. It should be noted that only institutions with \$10 billion or more in total assets may be deemed to be “in a troubled condition” based upon a composite rating of “3.” These institutions are more likely to have larger and more complex QFC portfolios that will require the additional time to satisfy the recordkeeping requirements. Under the proposed rule, all requests for extension must include a description of the progress toward compliance and a plan for completion.

#### **E. Process by which an IDI becomes Subject to Part 371**

Under Current Part 371, an IDI must comply with the recordkeeping requirements of the regulation following written notification by the institution’s appropriate federal banking agency or the FDIC that it is in troubled condition under Part 371. The proposed rule would specify that an IDI does not become subject to the recordkeeping requirements of Part 371 until it receives (i) written notice from the appropriate federal banking agency or the FDIC that the institution is in troubled condition and (ii) written notice from the FDIC that the IDI is subject to Part 371. Requiring that the FDIC notify the IDI that it is subject to the recordkeeping requirements of Part 371 will make it clear to IDIs in a troubled condition when they must begin to comply with Part 371. In addition, it will facilitate efficient administration of Part 371 by the FDIC.

#### **F. Transition Provisions**

The proposed rule would include transition provisions for larger IDIs that are subject to the recordkeeping requirements of Current Part 371 at the time the amendments to Current Part

371 become effective. Smaller, limited scope IDIs that are subject to the recordkeeping requirements of Current Part 371 at the time the amendments become effective would not be affected by the amendments and would continue to comply with Current Part 371 as in effect immediately prior to the amendments becoming effective.

For larger IDIs, the proposed rule would differentiate between those larger IDIs that are and are not maintaining the records required by Current Part 371 at that time. The larger IDIs that are maintaining records as required by Current Part 371 immediately prior to the effective date of the amendments to Current Part 371 will have 270 days (or, if the IDI is an accelerated records entity, 60 days) following the effective date of the amendments to comply with Part 371 as amended. In the interim, such IDIs would be required to continue the recordkeeping required by Current Part 371. Larger IDIs that are not maintaining the records required by Current Part 371 immediately prior to the effective date of the amendments to Current Part 371 will have 270 days (or, for accelerated records entities, 60 days) from the date they first became subject to Current Part 371 to comply with the revised recordkeeping requirements of Part 371, as amended.

#### **G. Other Changes**

The proposed rule would include several other less significant revisions to Part 371. These include (among others) clarification that, for end-of-day values for any day, an IDI must be capable of providing QFC records to the FDIC no later than 7:00 am on the following day, provided that the FDIC gives at least 8 hours advance notice, and a requirement that the IDI maintain each set of daily records for at least five business days. A full description of all changes is in the preamble to the proposed rule, attached.

**CONCLUSION:** Staff recommends that the Board approve the publication of the Notice of Proposed Rulemaking titled “*Recordkeeping Requirements for Qualified Financial Contracts*” in the *Federal Register* with a 60-day public comment period.

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