

FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 370

RIN 3064 - []

Recordkeeping Requirements for Qualified Financial Contracts;

Proposed Rule and Notice

AGENCY: Federal Deposit Insurance Corporation (FDIC).

ACTION: Notice of Proposed Rulemaking.

SUMMARY: The FDIC proposes recordkeeping requirements for qualified financial contracts (QFCs) held by insured depository institutions in a troubled condition as defined in this proposed rule. The appendix to the proposed rule would require an institution in a troubled condition, upon written notification by the FDIC, to produce immediately at the close of processing of the institution's business day, for a period provided in the notification, (1) electronic files for certain position level and counterparty level data; (2) electronic or written lists of (i) QFC counterparty and portfolio location identifiers, (ii) certain affiliates of the institution and the institution's counterparties to QFC transactions, (iii) contact information and organizational charts for key personnel involved in QFC activities, and (iv) contact information for vendors for such activities; and (3) copies of key agreements and related documents for each QFC.

DATES: Comments on this notice of proposed rulemaking must be received by

_____ [INSERT DATE [60] DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER], 2008.

ADDRESSES: You may submit comments by any of the following methods:

- **Federal eRulemaking Portal:** <http://www.regulations.gov>. Follow the instructions for submitting comments.
- **Agency Web site:** <http://www.FDIC.gov/regulations/laws/federal/propose.html>. Follow the instructions for submitting comments.
- **Mail:** Robert E. Feldman, Executive Secretary, Attention: Comments, Federal Deposit Insurance Corporation, 550 17th St., NW, Washington, DC 20429.
- **Hand Delivery/Courier:** Guard station at the rear of the 550 17th Street Building (located on F Street) on business days between 7:00 a.m. and 5:00 p.m. (EST).
- **Email:** Comments@fdic.gov. Include “Recordkeeping Requirements for Qualified Financial Contracts” in the subject line of the message.
- **Public Inspection:** All Comments received will be posted without change to <http://www.fdic.gov/regulations/laws/federal> including any personal information provided. Comments may be inspected and photocopied in the FDIC Public Information Center, 3502 North Fairfax Drive, Room E-1002, Arlington, VA 22226, between 9:00 a.m. and 5:00 p.m. (EST) on business days. Paper copies of public comments may be ordered from the Public Information Center by telephone at (877) 275-3342 or (703) 562-2200.

FOR FURTHER INFORMATION CONTACT: R. Penfield Starke, Counsel, Litigation and Resolutions Branch, Legal Division, (703) 562-2422 or RStarke@FDIC.gov; Michael B. Phillips, Counsel, Supervision and Legislation Branch,

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SUPPLEMENTARY INFORMATION:

I. Background

QFCs are certain financial contracts that have been defined in the Federal Deposit Insurance Act (FDI Act) and that receive special treatment by the FDIC in the event of the failure of an insured depository institution (institution). The special treatment of QFCs after the FDIC's appointment as receiver or conservator for a failed institution initially was codified in the FDI Act as part of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA)⁵ and places certain restrictions on the FDIC as receiver⁶ for a failed institution that held QFCs.

The FDI Act identifies QFCs using the statutory definition of five specific financial contracts. This statutory list of QFCs consists of securities contracts, commodity contracts, forward contracts, repurchase agreements, and swap agreements.⁷ The FDIC

⁵ Pub. L. No. 101-73, 103 Stat. 514 (August 9, 1989).

⁶ Most of the restrictions applicable to the treatment of QFCs by an FDIC receiver also apply to the FDIC in its conservatorship capacity. See U.S.C. 1821(e)(8), (9), (10), and (11). While the treatment of QFCs by an FDIC conservator is not identical to the treatment of QFCs in a receivership, see 12 U.S.C. 1821(e)(8)(E) and (10) (B)(i) and (ii), for purposes of this preamble we intend reference to the FDIC in its receivership capacity to include its role as conservator under this statutory authority.

⁷ 12 U.S.C. 1821(e)(8)(D)(ii) – (vi).

also may define other similar agreements as QFCs by rule or order.⁸ In addition, a master agreement that governs any contracts in these five categories is treated as a QFC⁹ as are security agreements that ensure the performance of a contract from the five enumerated categories.¹⁰

Under the FDI Act and other U.S. insolvency statutes, a party to QFCs with the insolvent entity can exercise its contractual right to terminate QFCs and offset or net out any amounts due between the parties and apply any pledged collateral for payment.¹¹ Under the Bankruptcy Code, this right is immediate upon initiation of bankruptcy proceedings, while under the FDI Act, counterparties cannot exercise this contractual right until after 5:00 p.m. (Eastern Time) on the business day following the appointment of the FDIC as receiver.¹² By contrast, parties to most contracts with insured institutions cannot terminate the contracts based upon the appointment of the FDIC as receiver.¹³ The special rights granted by the FDI Act to QFC counterparties are designed to protect the stability of the financial system and to reduce the potential for cascading interrelated defaults.

If QFC counterparties were unable to terminate and liquidate their positions in a timely manner after the failure of the institution, they would be exposed to market risks and uncertainty regarding the ultimate resolution of QFCs. Absent the ability to terminate a QFC in a timely manner when the counterparty becomes insolvent (which may include exercising rights to offset positions, net payments, and the use of collateral

⁸ 12 U.S.C. 1821(e)(8)(D)(i). The FDIC has provided clarifying definitions for repurchase agreements and swap agreements in 12 C.F.R 360.5.

⁹ 12 U.S.C. 1821(e)(8)(D)(ii)(XI), (iii)(IX), (iv)(IV), (v)(V), and (vi)(V).

¹⁰ 12 U.S.C. 1821(e)(8)(D)(ii)(XII), (iii)(X), (iv)(V), (v)(VI), and (vi)(VI).

¹¹ 12 U.S.C. 1821(e)(8); 11 U.S.C. 555 (securities contracts), 556 (commodities and forward contracts), 559 (repurchase agreements), 560 (swap agreements), and 561 (master netting agreements).

¹² See 12 U.S.C. 1821(e)(10)(B).

¹³ 12 U.S.C. 1821(e)(13).

to cover amounts due), the potential for fluctuation in the value of the QFCs from changes in interest rates and other market factors may create market uncertainty that could lead to broader market disruptions. Consequently, while the Bankruptcy Code and the FDI Act generally do not contain provisions covering creditor or counterparty liquidity concerns arising from insolvency proceedings, those statutes do contain safeguards for counterparties that have entered into certain financial contracts under the Bankruptcy Code and the FDI Act.¹⁴ Both of these statutes treat these types of financial contracts differently from other contracts that an entity may have entered into prior to bankruptcy or failure.¹⁵

Congress, however, recognized the tension between the need of the FDIC as receiver to efficiently resolve a failed institution and the desire to maintain stability in the financial markets. Thus, the treatment of QFCs for failed institutions under the FDI Act provides the FDIC with limited flexibility in crafting a resolution with respect to the institution's QFC portfolio. These provisions allow the FDIC to reduce losses to the deposit insurance fund and retain the value of the failed institution's portfolio, while minimizing the potential for market disruptions that could occur with the liquidation of a large QFC portfolio.

After its appointment as receiver, the FDIC has three options in managing the institution's QFC portfolio: (1) transfer the QFCs to another financial institution, (2) repudiate the QFCs, or (3) retain the QFCs in the receivership. Within certain constraints, the FDIC can apply different options to QFCs with different counterparties.

¹⁴ 11 U.S.C. 555, 556, 559, 560, and 561; 12 U.S.C. 1821(e)(8).

¹⁵ Without such protections for financial contracts and QFCs under the Bankruptcy Code and the FDI Act, respectively, a contract generally will be subject to an automatic stay upon the filing of a bankruptcy petition or the appointment of the FDIC as receiver. See 11 U.S.C. 361; 12 U.S.C. 1821(e)(13).

First, the receiver may transfer a QFC to any other financial institution not currently in default, including but not limited to foreign banks, uninsured banks, and bridge banks or conservatorships operated by the FDIC. If the receiver transfers a QFC to another financial institution, the counterparty cannot exercise its contractual right to terminate the QFC based solely on the transfer, the insolvency, or the appointment of the receiver.

Second, the FDIC as receiver may repudiate a QFC, within a reasonable period of time, if the receiver determines that the contract is burdensome.¹⁶ If the receiver repudiates the QFC, it must pay actual direct compensatory damages, which may include the normal and reasonable costs of cover or other reasonable measure of damages used in the industry for such claims, calculated as of the date of repudiation.¹⁷ If the receiver determines to transfer or repudiate a QFC, all other QFCs entered into between the failed institution and that counterparty, as well as those QFCs entered into with any of that counterparty's affiliates, must be transferred to the same financial institution or repudiated at the same time.

Third, the FDIC as receiver may retain a QFC in the receivership. This option would allow the counterparty to terminate the contract. If a QFC is terminated by the counterparty or repudiated by the receiver, the counterparty may exercise any contractual right to net any payment the counterparty owes to the receiver on a QFC against any payment owed by the receiver to the counterparty on a different QFC.

The FDIC as receiver has very little time to choose among these three options. Under the FDI Act, the FDIC as receiver has until 5:00 p.m. (Eastern Time) on the

¹⁶ 12 U.S.C. 1821(e)(1).

¹⁷ 12 U.S.C. 1821(e)(3)(C).

business day following the date of its appointment as receiver to make its decision to transfer any QFCs. During this period, counterparties are prohibited from terminating or otherwise exercising any contractual rights triggered by the appointment of the receiver under the QFC agreements. In effect, the same time limitation applies to repudiation because, after the expiration of this brief stay, counterparties are free to exercise any contractual right to terminate the QFCs and avoid the FDIC's power to repudiate. If the FDIC as receiver decides to transfer any QFCs, it must take steps reasonably calculated to provide notice of the transfer of the QFCs at the failed institution to the relevant counterparties, who are prohibited from exercising such rights thereafter.¹⁸

To make a well-informed decision on these three options, the FDIC needs access to information such as the types of QFCs, the counterparties and their affiliates, the notional amount and net position on the contracts, the purpose of the contracts, the maturity dates, and the collateral pledged for the contracts. Given the FDI Act's short time frame for such decision by the FDIC, in the case of a QFC portfolio of any significant size or complexity, it may be difficult to obtain and process the large amount of information necessary for an informed decision by the FDIC as receiver unless that information is readily available to the FDIC in a format that permits the FDIC to quickly and efficiently carry out an appropriate financial and legal analysis.

In light of the large volume of information concerning QFCs that a receiver must process in the limited time frame set forth in the FDI Act, the FDIC is proposing QFC recordkeeping requirements for institutions in a troubled condition, as described below.

¹⁸ See 12 U.S.C. 1821(e)(10)(B). This limited time frame in which QFC counterparties are stayed from acting is in contrast to parties to other contracts with a failed institution which may be required to continue to perform by a receiver, and the receiver may stay a party from terminating such other contracts subject to monetary damages or default for up to 90 days.

The absence of adequate information for decision-making by the FDIC as receiver increases the likelihood that, in a failed bank situation, QFCs will be left in the receivership or repudiated, instead of transferred to open institutions or a bridge bank. The FDIC does not believe that the proposed QFC recordkeeping requirements are overly burdensome, but encompass information that should be maintained by institutions as part of their risk management of capital market activities. Given the business and related counterparty risks and supervisory considerations, the FDIC believes that the proposed recordkeeping requirements are consistent with safe and sound banking practices by institutions holding QFCs.

II. The Proposed Rule

In 2005, the Bankruptcy Abuse Prevention and Consumer Protection Act¹⁹ was enacted, with section 908 of the Act authorizing the FDIC, in consultation with the other Federal banking agencies, to set recordkeeping requirements for QFCs held in institutions determined to be in a “troubled condition.”²⁰ Consistent with this statutory authority, the proposed rule applies to all institutions that are FDIC-insured and have been deemed to be in a troubled condition.

For purposes of this proposed rule, “troubled condition” means any insured depository institution that (1) has a composite supervisory rating, as determined by its appropriate Federal banking agency in its most recent examination, of 3 (only if the insured depository institution has total consolidated assets of ten billion dollars or greater), 4 or 5 under the Uniform Financial Institution Rating System, or in the case of an insured branch of a foreign bank, an equivalent rating; (2) is subject to a proceeding

¹⁹ Pub. L. No. 109-8, 119 Stat. 23 (April 20, 2005); H.R. Rep. No. 106-834, section 9, at 35 (2000).

²⁰ 12 U.S.C 1821(e)(8)(H).

initiated by the FDIC for termination or suspension of deposit insurance; (3) is subject to a cease-and-desist order or written agreement issued by the appropriate Federal banking agency, as defined in 12 U.S.C. 1813(q), that requires action to improve the financial condition of the insured depository institution or is subject to a proceeding initiated by the appropriate Federal banking agency which contemplates the issuance of an order that requires action to improve the financial condition of the insured depository institution, unless otherwise informed in writing by the appropriate Federal banking agency; (4) is informed in writing by the insured depository institution's appropriate Federal banking agency that it is in troubled condition for purposes of 12 U.S.C. 1831i on the basis of the institution's most recent report of condition or report of examination, or other information available to the institution's appropriate Federal banking agency; or (5) is determined by the appropriate Federal banking agency or the FDIC in consultation with the appropriate Federal banking agency to be experiencing a significant deterioration of capital or significant funding difficulties or liquidity stress, notwithstanding the composite rating of the institution by its appropriate Federal banking agency in its most recent report of examination.

The third and fourth criteria of the term "troubled condition" as defined in this proposed rule are similar to criteria for the definition of that term in other FDIC rules and the rules of the other Federal banking agencies (which generally implement 12 U.S.C. 1831i, regarding the Federal banking agencies' approval of appointment of directors and senior executive officers of institutions).²¹ However, the first, second, and fifth criteria

²¹ See 12 CFR 303.101(c) (FDIC), 12 CFR. 5.51(c)(6) (OCC), 12 CFR 225.71(d) (FRB); and 12 CFR 563.555 (OTS).

for the definition of “troubled condition” in the proposed rule differ from the other agencies’ rules that implement 12 U.S.C. 1831i.

Consistent with the FDIC’s and the other Federal banking agencies’ definition of “troubled condition” for purposes of 12 U.S.C. 1831i, the first criterion of the definition of “troubled condition” in this proposed rule includes institutions with a composite rating, as determined by its appropriate Federal banking agency in its most recent examination, of 4 or 5 under the Uniform Financial Institution Rating System, or in the case of an insured branch of a foreign bank, an equivalent rating. However, for purposes of this first criterion for “troubled condition” in this proposed rule, the FDIC has included any insured depository institution with total consolidated assets of ten billion dollars or greater and a composite rating, as determined by its appropriate Federal banking agency in its most recent examination, of 3 under the Uniform Financial Institution Rating System. The inclusion of institutions of such asset size with a composite rating of 3 reflects the risks to the deposit insurance fund arising from large institutions with QFC portfolios for which the appropriate Federal banking agency has assigned a composite rating of 3.

The second criterion of the definition of “troubled condition” in this proposed rule reflects the FDIC’s responsibility to terminate the deposit insurance of institutions that pose unreasonable risk to the deposit insurance fund. Similarly, the fifth criterion of this definition is based on circumstances that create a significant risk that an institution may require the appointment of the FDIC as receiver.

In accordance with section 11(e)(8)(H) of the FDI Act, we have consulted with the other Federal banking agencies regarding the proposed part 370 and Appendix A.

This Notice of Proposed Rulemaking (NPR) reflects various comments from the other Federal banking agencies.

III. Appendix A: QFC Recordkeeping Requirements

Appendix A to proposed Part 370 sets forth the specific QFC recordkeeping requirements proposed in this NPR. These QFC recordkeeping requirements are organized under three categories as provided in Appendix A: (1) position level data (Table A1), (2) counterparty level data (Table A2), and (3) certain contracts and lists of counterparty affiliates and identifiers, affiliates of the institution that are counterparties to QFC transactions, organizational charts involving the institution and its affiliates, and supporting vendors (Section B). An institution in a troubled condition would be required to maintain the position level data and counterparty data listed under Tables A1 and A2 in electronic files in a format acceptable to the FDIC, and such institutions would be required to demonstrate the ability to produce this information immediately at the close of processing of the institution's business day, for a period provided in a written notification by the FDIC. The files required under Section B are less quantitative and could be maintained in electronic format, in written format, or in a combination of those two formats. Nonetheless, the nature of this information would require that it be updated and available upon request on a daily basis.

The proposed rule and Appendix A are intended to facilitate the ability of the receiver to gather relevant information on QFCs in order to make business decisions within the short time frame between when a failure occurs and when the FDIC as receiver must act under 12 U.S.C. 1821(e)(9) and (10). Also, the data fields and related information required in Appendix A are important for the due diligence by institutions of their QFC agreements in conjunction with their risk management policies and procedures.

For purposes of the proposed rule and Appendix A, “position” is defined in the proposed rule to mean the rights and obligations of a person or entity as party to an individual transaction. For example, “position” would include the rights and obligations of an institution under a “Transaction” (as such term is defined in the 2002 Master Agreement of the International Swaps and Derivatives Association (ISDA)), such as an interest rate swap.

Table A1. Table A1 requires data that must be maintained regarding open QFC positions entered into by that institution.²² For such data, the institution must demonstrate the ability to produce immediately at the close of processing of the institution’s business day, for a period provided in a written notification by the FDIC, a report that aggregates the current market value and the amount of QFCs by each of the delineated fields. In addition, the FDIC also may require a certain combination of recordkeeping fields from Table A1 where significant for purposes of its evaluation of risks associated with the institution’s positions.

The following data fields are required in Table A1:

1. *Unique position identifier.* This information would include CUSIP identifiers or unique trade confirmation numbers, if available. This information is needed in order to readily track and distinguish positions.
2. *Portfolio location identifier.* This information would be used to provide the location in which the position is booked by the institution (e.g., the New York or London branch of the institution).

²² These positions include QFCs entered into by affiliates of the insured institution that are covered by the master agreements to which the institution is a party.

3. *Type of position.* This information describes the products used, sold or traded by an institution. It would include position types such as interest rate swaps, credit default swaps, equity swaps, and foreign exchange forwards, and securities or loan repurchase agreements.
4. *Purpose of the position.* This information identifies the role of the QFC in the institution's business strategy. For example, it would identify whether the purpose of a position is for trading, or for hedging other exposures such as mortgage loan servicing or certificates of deposit.
5. *Termination date.* This date indicates when the institution's rights and obligations regarding the position are expected to end.
6. *Next call, put, or cancellation date.* This information indicates the next date when a call, put, or cancellation may occur with respect to the position.
7. *Next payment date.* This information would include payment dates for potential upcoming obligations.
8. *Current market value of the position.* This information would cover position values as of the date of the file. It would be used to determine if the institution is in- or out-of-the-money with the counterparty.
9. *Unique counterparty identifier.* This information would be used to aggregate positions by counterparty.
10. *Notional or principal amount of the position.* This information is needed to assist in the FDIC's evaluation of the position. It would include the notional amount where applicable.

11. *Documentation status of the position.* This information would document whether the position was affirmed, confirmed, or neither affirmed nor confirmed. It is needed to determine the reliability of booked positions and their legal status.

Table A2. Table A2 requires data that must be maintained at the counterparty²³ level for all QFCs entered into by an institution. For such data, the institution must demonstrate the ability to produce immediately at the close of processing of the institution's business day, for a period provided in a written notification by the FDIC, a report that (i) itemizes, by each counterparty and its affiliates with QFCs with the institution, the data required in each field delineated in Table A2; and (ii) aggregates by field, for each counterparty and its affiliates, the data required in each field. The following data fields are required in Table A2:

1. *Unique counterparty identifier.* This information would be used by the FDIC to aggregate positions by counterparty.
2. *Current market value of all positions.* This data must be aggregated and to the extent permitted under all applicable agreements, netted as of the date of the file. If one or more positions cannot be netted against others, they would be maintained as separate entries.
3. *Current market value of all collateral posted by the institution.* This information would include the current market value of all collateral and the

²³ The use of the term "counterparty" in Appendix A generally includes all entities (including all affiliates) that are effectively treated as a single counterparty under a master agreement.

types of collateral, if any, that the institution has posted against all positions with each counterparty.

4. *Current market value of all collateral posted by counterparties.* This information would include the current market value of all collateral and the types of collateral, if any, that the counterparty has posted against all positions.
5. *Institution's collateral excess or deficiency.* This information would be provided with respect to all the positions as determined under each applicable agreement, such as master netting agreements and security agreements. If all positions are not secured by the same collateral, then separate entries should be maintained for each collateral excess and/or deficiency. This information would include thresholds and haircuts where applicable.
6. *Counterparty's collateral excess or deficiency.* This information would be provided with respect to all the positions as determined under each applicable agreement. If all positions are not secured by the same collateral, then separate entries should be maintained for each collateral excess and/or deficiency. This information would include thresholds and haircuts where applicable.
7. *Institution's collateral excess or deficiency for all positions.* This information would be based on the aggregate market value of the positions (after netting to the extent permitted under all applicable agreements) and the aggregate market value of all collateral posted by the institution against the positions, in whole or in part.

B. Data files and contract information required under Section B: Section B of Appendix A requires that other data files be maintained in either written or electronic format for QFCs and upon a written request by the FDIC, be produced immediately at the close of processing of the institution's business day, for the period provided in that written request. Each institution must maintain lists of: counterparty identifiers with the associated counterparty and contact information; affiliates of the counterparties that are also counterparties to QFC transactions; affiliates of the institution that are counterparties to QFC transactions, specifically indicating which affiliates are direct or indirect subsidiaries of the institution; and portfolio location identifiers with the associated booking locations.

For each QFC, the institution must maintain copies in a central location or data base in the United States of certain agreements, including active master netting agreements, and other QFC agreements between the institution and its counterparties that govern the QFC; active or "open" confirmations, if the position has been confirmed; credit support documents; and assignment documents, if applicable. The institution also must maintain a legal entity organizational chart; an organizational chart of all personnel involved in QFC-related activities at the institution, parent and affiliates; and a list of vendors supporting the QFC-related activities.

IV. Requests for Comment:

The FDIC recognizes that the proposed QFC recordkeeping requirements for institutions could not be implemented without some regulatory and financial burden on the industry. The FDIC is seeking to minimize the burden while at the same time ensuring it can quickly and cost effectively resolve an institution in a troubled condition

upon its failure. The FDIC seeks comment on the potential industry costs and feasibility of implementing the requirements of the proposed rule. The FDIC is also interested in comments on whether there are other ways to accomplish its goal of meeting the QFC recordkeeping-related requirements which might be more effective or less costly or burdensome.

For purposes of the final rule, the FDIC seeks comments on all aspects of the proposed rule. In particular, the FDIC seeks comments on these specific issues:

1. Whether the definition of “troubled condition” in the proposed rule should be modified in the final rule to include any insured depository institution that has received a composite rating as determined by its appropriate Federal banking agency in its most recent examination, of a 3 under the Uniform Financial Institution Rating System?

2. Whether the QFC recordkeeping requirements in this proposed rule should be applied in the final rule to cover all institutions, regardless of whether they are in a troubled condition? Alternatively, should the proposed rule be applied to cover all institutions, regardless of whether they are in a troubled condition, if they meet certain quantitative thresholds? Possible thresholds are outlined in the following question. Such an expansion of the scope of the proposed rule would be consistent with the important role that the availability of this information will have in the case of the appointment of a receiver or conservator in facilitating an orderly resolution of a failed institution and the reduction of the losses of the deposit insurance fund. Delaying the obligation for such recordkeeping until an institution is in a troubled condition increases the risks of disruption and the potential for losses to the deposit insurance fund. In addition, the requirements imposed by this proposed rule are consistent with the data and records

necessary for the safe and sound management of the risks arising from QFC activities. The absence of such prudent management practices increases the risks to the deposit insurance fund. The FDIC's general authority to promulgate rules to protect the deposit insurance fund would provide additional support for this expanded coverage.²⁴

3. Whether the QFC recordkeeping requirements in this proposed rule should be applied in the final rule only to institutions that meet certain quantitative thresholds, for example, including (i) the total consolidated assets of the institution exceed a certain threshold (e.g., a minimum total asset size of the institution of \$2 billion or more); (ii) the institution's holding of QFCs exceeds a certain total notional or principal amount; (iii) the institution is a party to no fewer than 10 open positions, or (iv) the total notional or principal amount of QFCs held by the institution constitute more than a certain percentage of tier 1 and tier 2 capital under the risk-based capital guidelines of the appropriate Federal banking agency, based on the institution's most recent consolidated Report of Condition and Income (e.g., greater than 20 percent of the institution's tier 1 and tier 2 risk-based capital)? In addition, should the FDIC consider other relevant factors such as the total number of QFC transactions by the institution, the types of QFCs executed by the institution, and the complexity of the QFC positions executed by the institution? Alternatively, should institutions below thresholds of the types described in this question be required to comply with the substantive requirements in proposed part 370 and section B of proposed Appendix A, but be excused from the requirements in Tables A1 and A2 of proposed Appendix A that records be maintained in electronic form?

²⁴ See 12 U.S.C. 1819(a)(Tenth); 12 U.S.C. 1821(a)(4)(A).

4. Should the QFC position level data fields in Table A1 of proposed Appendix A be required of affiliates of institutions subject to the proposed rule? Alternatively, should the QFC position level data fields in Table A1 of proposed Appendix A be required for affiliates of the institution that are counterparties to QFC transactions where such transactions are subject to a master agreement that also governs QFC transactions entered into by the institution?

5. Are there additional recordkeeping requirements or modifications to the proposed QFC recordkeeping requirements that would better reflect current internal risk management concerns of institutions?

6. Should the data requirements in proposed Appendix A be tailored to fit specific QFC categories (e.g., repurchase agreements and swap contracts)?

7. Should the FDIC revise its current definition of “troubled condition” in 12 CFR 303.102(c) to include the definition of “troubled condition” in this proposed rule?

8. The FDIC requests comment concerning (i) the extent to which contracts of institutions and their affiliates are subject to master netting agreements, cross-collateralization agreements, or other master agreements that affect the institutions’ net positions or collateral sufficiency with respect to a counterparty;²⁵ (ii) the extent to which contracts of counterparties and their affiliates are subject to master netting agreements, cross-collateralization agreements, or other master agreements that affect the counterparties’ net positions or collateral sufficiency; and (iii) the processes by which such impacts are monitored by institutions, counterparties, and their affiliates, respectively. Please note that such cross-affiliate netting across the insured institution in

²⁵ This situation might occur, for example, if an institution and its affiliates were treated as a single party under a master netting agreement, whereby their respective positions would be netted against one another and that net position, in turn, would be netted against the counterparty’s position.

receivership and its affiliates may be contrary to the provisions of the FDI Act governing the liabilities of the receivership and the distribution of the proceeds of the sale or liquidation of the insured institution's assets if such netting would disadvantage the insured institution and impose losses on the institution in receivership otherwise attributable to contracts by the institution's affiliates.

9. Do any of the data fields required in Tables A1 and A2 of proposed Appendix A call for information that is not relevant to the institutions' and counterparties' legal and economic positions regarding their QFC portfolios? Also, please provide any modifications of the data fields in Tables A1 and A2, in addition to the information required in section B of proposed Appendix A that would be appropriate for the appropriate Federal banking agency and the FDIC to better monitor QFCs entered into by institutions, counterparties, and affiliates of institutions and counterparties that are covered by section B.1 of proposed Appendix A.

10. Under section 370.1(c) of the proposed rule, an insured institution must comply with this rule and Appendix A within 30 days after written notification by the institution's appropriate Federal banking agency or the FDIC that it is in a "troubled condition" as defined in the proposed rule. Should the FDIC include in the final rule an approval procedure for requests for an extension of the 30 day deadline from institutions with an aggregate amount of QFCs beyond a certain threshold and based on specific dates for compliance?

11. Should Appendix A be amended to include requirements for a listing of the institution's QFC-related portfolios, those portfolios' risk information, and the specific counterparties associated with those portfolios?

V. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA)²⁶ requires an agency publishing a notice of proposed rulemaking to prepare and make available for public comment an initial regulatory flexibility analysis that describes the impact of the final rule on small entities. Under regulations issued by the Small Business Administration,²⁷ a “small entity” includes a bank holding company, commercial bank, or savings association with assets of \$165 million or less (collectively, small banking organizations). The RFA provides that an agency is not required to prepare and publish a regulatory flexibility analysis if the agency certifies that the proposed rule would not have a significant economic impact on a substantial number of small entities.

Under section 605(b) of the RFA,²⁸ the FDIC certifies that this proposed rule would not have a significant economic impact on a substantial number of small entities. The proposed rule consists of requirements for institutions that have been determined to be in a troubled condition, as defined in the proposed rule. These requirements include the maintenance of certain information regarding the institution’s QFCs that it would be able to produce on short notice by the appropriate Federal banking agency or the FDIC. This proposed rule would not have a significant economic impact on a substantial number of small entities for three reasons. First, QFCs are generally sophisticated financial instruments that are usually used by larger financial institutions to hedge assets, provide funding, or increase income. Because of the nature of the capital markets in which QFCs are used, smaller entities generally do not participate in such markets. Second, the number of small entities affected is further limited due to the proposed rule only being

²⁶ 5 U.S.C. 603(a).

²⁷ 13 CFR 121.201.

²⁸ 5 U.S.C. 605(b).

applicable to institutions that are determined to be in a troubled condition under the definition in the rule. Third, the impact on small entities that do use QFCs and are in a troubled condition further is limited by the fact that the information requested by the FDIC involves information that the institution already should have accessible if it is operated in a safe and sound manner.

VI. Paperwork Reduction Act

A. Request for Comment on Proposed Information Collection. In accordance with the requirements of the Paperwork Reduction Act of 1995 (PRA), 44 U.S.C. 3501 – 3521, the FDIC may not conduct or sponsor, and the respondent is not required to respond to, an information collection unless it displays a currently valid Office of Management and Budget (OMB) control number. The FDIC is requesting comment on the proposed information collection requirements contained in this rule. The FDIC also is giving notice that the proposed collection of information has been submitted to OMB for review and approval under section 3506 of the PRA and section 1320.11 of OMB's implementing regulations (5 CFR Part 1320).

Comments: In addition to the questions raised elsewhere in this preamble, comment is solicited on: (1) whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; (2) the accuracy of the agency's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used; (3) the quality, utility, and clarity of the information to be collected; (4) ways to minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or

other technological collection techniques or other forms of information technology; e.g., permitting electronic submission of responses; and (5) estimates of capital or start-up costs and costs of operation, maintenance, and purchases of services to provide information.

Commenters may submit comments on aspects of the proposed rule that may affect recordkeeping requirements at the addresses listed in the **ADDRESSES section of this NPR**. In addition, you should send a copy of your comments to the OMB Desk Officer for the FDIC, by mail to the Office of Information and Regulatory Affairs, U.S. Office of Management, New Executive Office Building, Room 10235, 725 17th Street, NW, Washington, DC 20503, or by fax to (202) 395-6974.

B. Proposed Information Collection.

Title of Information Collection: Recordkeeping Requirements for Qualified Financial Contracts: Proposed Rule and Notice.

OMB Number: 3064 – [NEW]

Frequency of Response: Where applicable under this proposed rule, upon written request of the institution’s appropriate Federal banking agency or the FDIC immediately at the close of processing of the institution’s business day for a period provided in a written notification by the FDIC.

Affected Public: Insured depository institutions determined to be in a “troubled condition” as defined in the rule.

Abstract: The combined annual burden of complying with this proposed rule is estimated to be 9,600 hours. This estimate assumes that 150 institutions will be subject to the requirements of the proposed rule and that such institution will spend, on average, 24

hours annually complying with the proposed reporting requirements and 40 hours annually complying with the proposed records maintenance requirements. Factors considered in developing the burden estimate include the existing and historical average number of insured institutions with supervisory ratings of 3 (for institutions with total consolidated assets of ten billion dollars or greater), 4, or 5; the volume of QFC activity in institutions that presently have supervisory ratings of 3 (where the asset threshold for an institution is met or exceeded), 4, or 5; the time necessary to complete other types of regulatory reports; the frequency with which the FDIC may require institutions to produce QFC information under this proposed rule; and the time necessary to update and maintain QFC and related information as required in the proposed rule.

Estimated Burden: The combined annual burden is estimated to be 9,600 hours. This estimate is derived from the product of the estimated number of institutions that would be subject to the proposed rule and the estimated hours per respondent necessary to meet the proposed rule's reporting and records maintenance requirements. There are an estimated 150 institutions that currently would be subject to the requirements of the proposed rule. Approximately 110 institutions would have been subject to the proposed rule on average over the past 10 years.

The combined reporting and record maintenance burdens related to the proposed rule are estimated at 64 hours per respondent annually. This estimate consists of two components: a reporting component and a records maintenance component. It is estimated that reports as described in Tables A and B of proposed Appendix A will require 2 hours on average to complete. This estimate is based on a number of considerations including the relatively small number of items requested, the time

necessary to complete other regulatory reports, and the reported volume of QFC activity evident within the existing population of institutions that would be subject to the proposed rule. The time necessary to produce such reports could be substantially more than 2 hours for larger institutions with greater QFC volumes.

The FDIC may request the information required in Tables A1 and A2, and section B of Appendix A of the proposed rule relatively frequently or infrequently depending on such factors as the reported volume of an institution's QFC exposures, the number of QFC positions held by an institution (if known), and the near term failure prospects of an institution. For example, the FDIC would be more likely to request the information required to be maintained under this proposed rule and Appendix if the institution has a sizeable volume of reported QFC exposures (measured in carrying values or notational amounts as applicable) relative to that institution's assets or regulatory capital than an institution with a nominal volume of reported QFC exposures. Similarly, the FDIC likely would require more frequent reporting for institutions with low supervisory ratings. Based on the assumption that 12 reports would be required within a given year for such institutions, the total reporting component of the estimate would be 24 hours per respondent.

It is further estimated that institutions subject to these requirements will spend, on average, an estimated 10 hours per quarter, or 40 hours annually updating and maintaining the records and information required by section B of proposed Appendix A. Again, larger institutions with greater QFC volumes would likely spend considerably more time updating and maintaining records pertaining to QFC activities. Combining the

records maintenance and reporting component estimates results in an estimated annual burden of 64 hours per respondent.

Estimated Number of Respondents: 150.

Estimated Time per Response: 64 hours annually per respondent (24 hours -- reporting; 40 hours – recordkeeping).

Estimated Total Annual Burden: 9,600 hours.

VII. Solicitation of Comments on the Use of Plain Language

Section 722 of the Gramm-Leach-Bliley Act required the Federal banking agencies to use plain language in all proposed and final rules published after January 1, 2000. The Federal banking agencies invite comment on how to make this proposed rule easier to understand. For example:

- Have we organized the material to suit your needs? If not, how could the rule be more clearly stated?
- Are the requirements in the rule clearly stated? If not, how could the rule be more clearly stated?
- Do the regulations contain technical language or jargon that is not clear? If so, which language requires clarification?
- Would a different format (grouping and order of sections, use of headings, paragraphing) make the regulation easier to understand? If so, what changes would make the regulation easier to understand?
- Would more, but shorter sections be better? If so, which sections should be changed?
- What else could we do to make the regulation easier to understand?

List of Subjects

12 CFR Part 370

Administrative practice and procedure, Bank deposit insurance, Banking, Banks, Reporting and recordkeeping requirements, Savings associations, Securities, State non-member banks.

The Board of Directors of the Federal Deposit Insurance Corporation proposes to add a new part 370 to title 12 of the Code of Federal Regulations as follows:

PART 370 ----- RECORDKEEPING REQUIREMENTS FOR QUALIFIED FINANCIAL CONTRACTS

1. The authority citation for part 370 shall read as follows:

Authority: 12 U.S.C. 1819(a)(Tenth); 1820(g); 1821(e)(8)(D) and (H); 1831g; 1831i, and 1831s.

2. Add new part 370 to read as follows:

Sec.

370.1 Scope and purpose.

370.2 Definitions.

370.3 Form, availability and retention of records.

370.4 Content of records.

Appendix A to Part 370 – File Structure for Qualified Financial Contract Records

§ 370.1 Scope, purpose, and applicability.

(a) Scope. This part applies to insured depository institutions that are in a troubled condition as defined in section 370.2(f).

(b) Purpose. This part establishes recordkeeping requirements with respect to qualified financial contracts for insured depository institutions that are in a troubled condition.

(c) Applicability. An insured depository institution shall comply with this part within 30 days after written notification by the institution's appropriate Federal banking agency or the FDIC that it is in a troubled condition under section 370.2(f).

§ 370.2 Definitions.

For purposes of this part:

(a) Affiliate means any company that controls, is controlled by, or is under common control with another company.

(b) Appropriate Federal banking agency means the agency or agencies designated under 12 U.S.C. 1813(q).

(c) Insured depository institution means any bank or savings association, as defined in 12 U.S.C. 1813, the deposits of which are insured by the FDIC.

(d) Position means the rights and obligations of a person or entity as a party to an individual transaction under a QFC.

(e) Qualified financial contracts (QFCs) mean those qualified financial contracts that are defined in 12 U.S.C. 1821(e)(8)(D) to include securities contracts, commodity contracts, forward contracts, repurchase agreements, and swap agreements and any other contract determined by the FDIC to be a QFC as defined in that section.

(f) Troubled condition means for purposes of this part, any insured depository institution that (1) has a composite rating, as determined by its appropriate Federal banking agency in its most recent report of examination, of 3 (only for insured depository

institutions with total consolidated assets of ten billion dollars or greater), 4, or 5 under the Uniform Financial Institution Rating System, or in the case of an insured branch of a foreign bank, an equivalent rating; (2) is subject to a proceeding initiated by the FDIC for termination or suspension of deposit insurance; (3) is subject to a cease-and-desist order or written agreement issued by the appropriate Federal banking agency, as defined in 12 U.S.C. 1813(q), that requires action to improve the financial condition of the insured depository institution or is subject to a proceeding initiated by the appropriate Federal banking agency which contemplates the issuance of an order that requires action to improve the financial condition of the insured depository institution, unless otherwise informed in writing by the appropriate Federal banking agency; (4) is informed in writing by the insured depository institution's appropriate Federal banking agency that it is in troubled condition for purposes of 12 U.S.C. 1831i on the basis of the institution's most recent report of condition or report of examination, or other information available to the institution's appropriate Federal banking agency; or (5) is determined by the appropriate Federal banking agency or the FDIC in consultation with the appropriate Federal banking agency to be experiencing a significant deterioration of capital or significant funding difficulties or liquidity stress, notwithstanding the composite rating of the institution by its appropriate Federal banking agency in its most recent report of examination.

§ 370.3 Form, availability and maintenance of records.

(a) Form and availability. The records required to be maintained by an insured depository institution for QFCs under this part—

(1) Except for records that must be maintained through electronic files under Appendix A of this part, may be maintained in any form, including in an electronic file, provided that the records are updated at least daily;

(2) If the records are not maintained in written form, will be capable of being reproduced or printed in written form; and

(3) Will be made available upon written request by the institution's appropriate Federal banking agency or the FDIC immediately at the close of processing of the institution's business day, for a period provided in that written request.

(b) Maintenance of records after the institution is no longer in a troubled condition. Insured depository institutions that are in a troubled condition as defined in section 370.2(f) shall continue to maintain records required under this part for a period of one year after the date that the appropriate Federal banking agency notifies the institution that it is no longer in a troubled condition as defined in section 370.2(f).

(c) Maintenance of records after an acquisition of an institution that is in a troubled condition. If an insured depository institution that has been determined by the appropriate Federal banking agency to be in a troubled condition ceases to exist as an insured depository institution as a result of a merger or a similar transaction into an insured depository institution that is not in a troubled condition immediately following the acquisition, the obligation to maintain records under this part will terminate when the institution in a troubled condition ceases to exist as a separately insured depository institution.

§ 370.4 Content of records.

For each QFC for which an insured depository institution is a party or is subject to a master netting agreement involving the QFC, that institution must maintain records as listed under Appendix A of this part.

Appendix A to Part 370 – File Structure for Qualified Financial Contract (QFC)

Records

QFC Recordkeeping Requirements

A. Electronic Files to Be Maintained for QFCs

1. Any insured depository institution that is subject to this part (“institution”) must maintain, in an electronic file in a format acceptable to the FDIC, the position level data found in Table A1 for all open positions in QFCs entered into by that institution or for which the institution is subject. In addition, for such data, the institution must, at the FDIC’s written request, produce immediately at the close of processing of the institution’s business day, for a period provided in that written request, a report in a format acceptable to the FDIC that aggregates the current market value and the amount of QFCs by each of the fields in Table A1. The FDIC also may require in its written requests a certain combination of recordkeeping fields from Table A1 where significant for purposes of its evaluation of risks associated with the institution’s positions.

Table A1. Position Level Data		
Field	Example	Data Application
Unique position identifier and CUSIP, if available	999999999AU	Information needed to readily track and distinguish positions; unique trade confirmation number if available

Portfolio location identifier (to identify the headquarters or branch where the position is booked)	XY12Z	Information needed to determine the headquarters or branch where the position is booked (see section B.1 of this Appendix)
Type of position (including the general nature of the reference asset or interest rate)	Interest rate swap, credit default swap, equity swap, foreign exchange forward, securities repurchase agreement, loan repurchase agreement	Information needed to determine the extent to which the institution is involved in any particular QFC market
Purpose of the position (if the purpose consists of hedging strategies, include the general category of the item(s) hedged)	Trading, hedging mortgage servicing, hedging certificates of deposit	Information needed to determine the role of the QFC in the institution's business strategy
Termination date (date the position terminates or is expected to terminate, expire, mature, or when final performance is required)	3/31/2010	Information needed to determine when the institution's rights and obligations regarding the position are expected to end
Next call, put, or cancellation date	9/30/08	Information needed to determine when a call, put, or cancellation may occur with respect to a position
Next payment date	9/30/08	Information needed to anticipate potential upcoming obligations
Current market value of the position (as of the date of the file)	\$995,000	Information needed to determine if the institution is in- or out-of-the money with the counterparty
Unique counterparty identifier	AB999C	Information needed to aggregate positions by counterparty
Notional or principal amount of the position (this is the notional amount, where applicable)	\$1,000,000	Information needed to help evaluate the position
Documentation status of position	Affirmed, confirmed, or neither affirmed nor confirmed	Information needed to determine reliability of a booked position and its legal status

2. Also, the institution must maintain, in an electronic file in a format acceptable to the FDIC, the counterparty-level data found in Table A2 for all open positions in QFCs entered into by that institution. In addition, the institution must, at the FDIC's written request, produce immediately at the close of processing of the institution's business day, for a period provided in that written request, a report in a format acceptable to the FDIC that (i) itemizes, by each counterparty and by each of its affiliates, the data required in each field in Table A2, and (ii) aggregates by field, for each counterparty and its affiliates, the data required in each field in Table A2.

Table A2. Counterparty-Level Data		
Field	Example	Data Application
Unique counterparty identifier	AB999C	Information needed to aggregate positions by counterparty
Current market value of all positions, as aggregated and, to the extent permitted under each applicable agreement, netted ²⁹ (as of the date of the file)	(\$1,000,000)	Information needed to help evaluate the positions
Current market value of all collateral and the type of collateral, if any, that the institution has posted against all positions with each counterparty	\$950,000; U.S. treasuries	Information needed to determine the extent to which the institution has provided collateral
Current market value of all collateral and the type of collateral, if any, that the counterparty has posted against all positions	\$50,000; U.S. treasuries	Information needed to determine the extent to which the counterparty has provided collateral

²⁹ If one or more positions cannot be netted against others, they should be maintained as separate entries.

Institution's collateral excess or deficiency with respect to all the positions, as determined under each applicable agreement including thresholds and haircuts where applicable ³⁰	(\$25,000)	Information needed to determine the extent to which the institution has satisfied collateral requirements under each applicable agreement
Counterparty's collateral excess or deficiency with respect to all the positions with each counterparty, as determined under each applicable agreement including thresholds and haircuts where applicable.	\$50,000	Information needed to determine the extent to which the counterparty has satisfied collateral requirements under each applicable agreement
The institution's collateral excess or deficiency with respect to all the positions, based on the aggregate market value of the positions (after netting to the extent permitted under each applicable agreement) and the aggregate market value of all collateral posted by the institution against the positions, in whole or in part	(\$50,000)	Information needed to determine the extent to which the institution's obligations regarding the positions may be unsecured

B. Other Files (In Written or Electronic Form) to Be Maintained for QFCs

The institution must, at the FDIC's written request, produce the following files immediately at the close of processing of the institution's business day, for a period provided in that written request.

1. Each institution must maintain the following files in written or electronic form:
 - A list of counterparty identifiers, with the associated counterparties and contact information;
 - A list of the affiliates of the counterparties that are also counterparties to QFC transactions with the institution or its affiliates, and the specific master netting agreements under which they are counterparties;

³⁰ If all positions are not secured by the same collateral, then separate entries should be maintained for each position or set of positions secured by the same collateral.

- A list of affiliates of the institution that are counterparties to QFC transactions where such transactions are subject to a master agreement that also governs QFC transactions entered into by the institution. Such list must specify (i) which affiliates are direct or indirect subsidiaries of the institution and (ii) the specific master agreements under which those affiliates are counterparties to QFC transactions; and
 - A list of portfolio identifiers (see Table A1), with the associated booking locations.
2. For each QFC, the institution must maintain all of the following documents:
- Agreements (including master agreements and annexes, supplements or other modifications with respect to the agreements) between the institution and its counterparties that govern the QFC transactions
 - Documents related to and affirming the position;
 - Active or “open” confirmations, if the position has been confirmed;
 - Credit support documents; and
 - Assignment documents, if applicable, including documents that confirm that all required consents, approvals, or other conditions precedent for such assignment(s) have been obtained or satisfied..
3. The institution must maintain:
- a legal-entity organizational chart, showing the institution, its corporate parent and all other affiliates, if any; and

- an organizational chart, including names and position titles, of all personnel significantly involved in QFC-related activities at the institution, its parent and its affiliates.
 - Contact information for the primary contact person for purposes of compliance with this part by the institution.
4. The institution must maintain a list of vendors supporting the QFC-related activities and their contact information.

Dated at Washington, DC, this 15th day of July, 2008.

By order of the Board of Directors.
Federal Deposit Insurance Corporation.

Robert E. Feldman,
Executive Secretary