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FINANCIAL SERVICES ALERT

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DEVELOPMENTS OF NOTE

Dodd-Frank Act Conference Report Finalized by Financial Regulatory Reform Conference Committee

The Congressional conference committee on financial regulatory reform released its 2,319 page conference report reconciling the Wall Street Reform and Consumer Protection Act of 2009 that was passed by the U.S. House of Representatives on December 11, 2009 (the “House Bill”) with the Restoring American Financial Stability Act of 2010 that was passed by the U.S. Senate on May 20, 2010 (the “Senate Bill”). The final legislation, which was renamed by the conference committee the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Act”), would comprehensively reform the regulation of financial products and services by providing for, among other things, the establishment of a Financial Stability Oversight Council (the “Council”) to monitor systemic risk, the creation of a new resolution process for systemically important financial institutions, the establishment of a Consumer Financial Protection Bureau (the “CFPB”), the registration of private fund advisers and the regulation of derivatives.

After releasing its conference report, the conference committee reconvened to revise the funding provisions of the Act to address concerns regarding a proposed assessment on large financial institutions. The conference committee agreed to replace the proposed assessment with provisions that would authorize (i) the early termination of the Troubled Asset Relief

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Program and (ii) require the FDIC to take steps to increase the reserve ratio of the Deposit Insurance Fund from 1.15 percent to 1.35 percent of estimated insured deposits by September 30, 2020, provided that any increased assessment must not be applied to institutions with less than $10 billion in assets.

The Act still must be passed by both chambers of Congress and signed by the President to become effective. In light of the death of Senator Robert C. Byrd, the Senate has postponed its legislative schedule for the first two days of July, which means that the Act will not be put to a vote in that chamber before the July 4th congressional recess. Upon passage, the Act requires numerous studies and rulemaking by Federal banking and securities regulators, a process that can be expected to last for several years. The following are some of the highlights of the Act:

- Proprietary trading and the sponsorship of hedge funds and private equity funds by banking entities would be restricted under provisions known as the "Volcker Rule." Subject to certain limitations, banking entities would be permitted to organize and offer a hedge fund or private equity fund for the provision of "bona fide trust, fiduciary, or investment advisory services" and make and retain an investment in a hedge fund or private equity fund that the banking entity organizes and offers, provided that such investments (i) are reduced to not more than 3% of the total ownership of a fund within one year after the fund's establishment (with the possibility of a two year extension) and (ii) that such investments do not exceed 3% of the banking entity's Tier 1 capital.

- The OTS would be eliminated but the thrift charter would be preserved. Thrifts would be supervised by the OCC and savings and loan holding companies would be supervised by the FRB.

- New capital standards would eliminate trust preferred securities as Tier 1 capital. Existing trust preferred securities would be grandfathered for banking entities with less than $15 billion of assets. Larger banking entities would be subject to a three-year phase-in period beginning on January 1, 2013.

- New authority would be established for the orderly resolution of large financial companies. No standing resolution fund for large financial companies would be established under the Act; however, following the resolution of a large financial company, the FDIC would be authorized to recover the costs of such resolution through a special assessment levied on financial firms with more than $50 billion in assets.

- Deposit insurance coverage levels would be permanently increased to $250,000, retroactive to January 1, 2008. The Transaction Account Guarantee Program would be extended for two years and would become mandatory for all insured depository institutions.

- Interest would be permitted on business demand deposit accounts.

- The CFPB would be established as an independent bureau within the FRB. The CFPB would prescribe rules applicable to most providers of consumer financial products and services and would have examination powers over depository institutions with total assets of more than $10 billion and certain nondepository providers of consumer financial products and services, such as mortgage brokers and money services

businesses. Auto dealers were granted a controversial exemption from the CFPB's jurisdiction.

- On the petition of a member agency of the Council, the Council would be authorized to set aside a final regulation prescribed by the CFPB, or a provision of such a regulation, if the Council decides that the regulation or provision would put the safety and soundness of the United States banking system or the stability of the financial system of the United States at risk.

- The OCC would only be allowed to preempt, on a case-by-case basis, a state law that "prevents or significantly interferes" with the business of banking and only after notice and an opportunity to comment.

- The FRB would be authorized to regulate interchange fees for debit card transactions by adopting rules to require that such fees be "reasonable and proportional" to the incremental cost incurred in processing such transactions. Network fees charged by payments networks and certain prepaid cards, including government-issued cards used to provide health and welfare benefits, would be generally exempt from the rules. Issuers and payments networks would also be subject to additional restrictions on exclusivity and routing arrangements and merchant practices.

- New minimum mortgage underwriting standards would be required for residential mortgages. Lenders would be required to obtain "verified and documented information" that the consumer has a "reasonable ability to repay." Compensation paid to mortgage loan originators that varies based on the terms of loans (other than the amount of principal of the loan) would be prohibited. Regulators would establish a class of qualified loans that would be protected from legal liability, such as the borrower's right to rescind the loan and seek damages. Certain loan features such as negative amortization, prepayment penalties and balloon payments, would exclude loans from the safe harbor. Qualified mortgages would still have to have a net tangible benefit to borrowers. Lenders packaging qualified mortgages into securities would be exempted from a 5% risk retention provision.

- Banks would be permitted to trade certain derivatives, such as interest rate and foreign exchange swaps, and use derivatives for hedging directly related to that depository institution's activities. Insured depository institutions would, however, be required to spin off to separately capitalized affiliates other derivatives trading practices, including commodities and energy, equity derivatives and uncleared credit default swaps, as well as to comply with prohibitions (under the Volcker Rule) on proprietary trading in derivatives.

- The Act would create parallel regimes under the CFTC and the SEC for regulating swaps, resulting in dual registration and other compliance requirements for swap dealers and major swap participants. Joint rule-making by the two Commissions, however, would be required with respect to mixed swaps and books and records requirements for swap dealers, major swap participants, and swap clearing organizations and agencies. The Act would establish a formal process for determining jurisdiction, status and rule-making authority for new products that includes resolution of disputes between the CFTC and SEC by the Court of Appeals.

- The Act would impose mandatory clearing of swaps at registered clearing organizations or agencies and exchange trading on registered exchanges for standardized products and transactions with limited exceptions, including for certain end-users that are hedging or mitigating commercial risk.

- The Act would impose new, heightened duties on swap dealers and major swap participants when acting as advisors or counterparties in transactions with certain "special entities," including municipalities and other political subdivisions, as well as pension, endowment and retirement plans.

- With respect to asset-backed securities, the Federal banking and securities regulators would be required to adopt rules providing that an issuer or other entity creating an asset-backed security must retain an economic interest in the credit risk of the security's underlying assets, including not less than 5% of any particular asset, unless the securitizer meets certain underwriting standards or the underlying assets are "qualified residential mortgages" in accordance with the new rules. The SEC also would be directed to prescribe regulations requiring an issuer to perform due diligence on an asset-backed security's underlying assets and disclose its findings.

- Advisers to private funds (including hedge funds and private equity funds) with greater than $150 million in assets would be required to register under the Investment Advisers Act of 1940 (the "Advisers Act") within one year of the enactment of the Act. Advisers to venture capital funds (to be defined by the SEC), although not subject to registration, would be subject to certain reporting requirements.

- Family offices would be exempt from registration under the Advisers Act pursuant to rules to be enacted by the SEC consistent with previous exemptions.

- The SEC would be required to adjust the "accredited investor" standard under Regulation D to exclude a primary residence from net worth and adjust the standard pursuant to periodic reviews. The "qualified client" standard under the Advisers Act would also be subject to periodic review and adjustment.

- The SEC would be required to provide a report to Congress within 6 months of enactment that addresses specified issues regarding the provision of personalized advice to retail customers by investment advisers and broker-dealers. The SEC would be authorized, but not required, to engage in rulemaking establishing a fiduciary duty for broker-dealers with respect to retail and other customers. The Act also expressly provides for SEC authority to set the standard of conduct for broker-dealers and investment advisers with respect to retail customers.

- Under the Act, each nationally recognized securities rating organizations ("NRSRO") would be subject to annual examination by the SEC which would make its inspection reports publicly available. The SEC would be required to adopt rules mandating that an NRSRO make public disclosures of (a) quantitative and qualitative information underlying each credit rating and (b) the performance of ratings over time. The Act would enable private actions against an NRSRO over credit ratings and provide that the enforcement and penalty provisions of the Securities Exchange Act of 1934 would apply to statements made by a credit rating agency in the same manner and to the same extent as to statements made by a registered public accounting firm or a securities analyst under the securities laws.

- The SEC would have rulemaking power to prohibit or limit the use by broker-dealers and investment advisers of mandatory arbitration of disputes involving the securities laws and rules of self-regulatory organizations. The Act would increase protections and incentives for whistleblowers and expand the scope of collateral bars that the SEC could impose as sanctions. The Act would create express additional aiding and abetting causes of action under the Securities Act of 1933, the Investment Company Act of 1940 and the Advisers Act.

- The SEC would have rulemaking authority with respect to securities lending and be required to adopt rules designed to increase the transparency of information regarding securities lending available to broker-dealers and investors.

- The SEC would receive express authority to adopt rules granting proxy access for shareholder nominees, and would be required to adopt rules under which an annual proxy statement would have to explain why an issuer had chosen to have the same person serve as chief executive officer and chairman of the board, or chosen not to do so.

- Shareholders would be granted a non-binding vote on executive compensation and "golden parachute" payments.

- Stock exchanges would be required to change their listing rules to require that each member of a listed company's compensation committee be independent and be granted the authority and funding to retain advisors (compensation consultant and legal counsel) who are independent based on specific enumerated factors.

- Changes in proxy rules would require the disclosure of the relationship between executive pay and financial performance of the issuer, the ratio of the median pay of all employees to the pay of the chief executive officer, and employee and director hedging activities.

- Stock exchanges would be required to prohibit the listing of any security of an issuer that does not adopt policies governing the claw back of excess executive compensation based on inaccurate financial statements.

- The Federal financial regulators would be required to impose enhanced disclosure and reporting of compensation arrangements at regulated financial institutions.

- The Act would create within the Treasury the Federal Office of Insurance, which would monitor the insurance industry and be required to complete a study within 18 months on how to modernize and improve the system of insurance regulation in the United States.

Future editions of the *Alert* will provide in-depth discussion and analysis of the provisions of the Act and the *Alert* will continue its coverage of financial regulatory reform throughout the rulemaking process.

FinCEN Issues Proposed Regulations Expanding Anti-Money Laundering Obligations of Providers and Sellers of Prepaid Access

The U.S. Treasury Department's Financial Crimes Enforcement Network ("FinCEN") published proposed regulations (the "Proposed Regulations") that would expand the anti-money laundering ("AML") obligations under the Bank Secrecy Act (the "BSA") for providers and sellers of "prepaid access." In issuing the proposal, FinCEN explained that the Proposed Regulations, which are mandated under the Credit Card Accountability, Responsibility and Disclosure Act of 2009, are intended to address regulatory gaps that have resulted from the proliferation of, and innovations in, prepaid access devices over the last ten years and their increasing use as accepted payment methods. Subject to certain exceptions, the Proposed Regulations would apply to providers and sellers of a wide range of prepaid access devices, including gift cards, mobile phones, electronic serial numbers, key fobs and other mechanisms that provide a portal to funds that have been paid for in advance and are retrievable and transferable.

Under FinCEN's current regulations, certain "issuers, "sellers," and "redeemers" of "stored value" are considered to be "money services businesses" ("MSBs") for purposes of FinCEN's BSA regulations. Such issuers, sellers and redeemers of stored value must establish written anti-money laundering ("AML") programs and comply with currency transaction report ("CTR") filing obligations, but are not required to register as MSBs with FinCEN or file suspicious activity reports ("SARs"). FinCEN explained that when initially adopting its MSB regulations in 1999 it deferred the application of these requirements to the stored value industry to avoid any unintended consequences that might result from applying the rules to an industry that was then in its infancy.

The Proposed Regulations would impose additional obligations on "providers" and "sellers" of "prepaid access." As explained below, certain types of prepaid access would be excluded from coverage by the Proposed Regulations because they do not fit within the rule's definition of "prepaid program." In addition, as with other categories of MSBs, the Proposed Regulations would not apply to prepaid access providers or sellers that are banks or are registered with, or regulated or examined by, the SEC or CFTC.

Definition of "Prepaid Access"

The Proposed Regulations would replace the term "stored value" with "prepaid access," which would be defined as an "[e]lectronic device or vehicle, such as a card, plate, code, number, electronic serial number, mobile identification number, personal identification number, or other instrument that provides a portal to funds or the value of funds that have been paid in advance and can be retrievable and transferrable at some point in the future." The change in terminology from "stored value" to "prepaid access" reflects FinCEN's understanding that prepaid value is not "stored" on a card, but instead stored in a location or a medium that can be accessed electronically through the card or an alternative device.

"Providers" and "Sellers" of Prepaid Access

A "provider" of prepaid access would be "the person with principal oversight and control over one or more prepaid programs," as determined based on the facts and circumstances of each prepaid program's transaction chain. As described in the Proposed Regulations, activities that include "principal oversight and control" of a prepaid program include (a) organizing the prepaid program, (b) setting the terms and conditions and determining

that the terms have not been exceeded, (c) determining the other businesses that will participate in the transaction chain underlying the prepaid access (which may include the issuing bank, the payment processor or the distributor), (d) controlling or directing the appropriate party to initiate, freeze or terminate prepaid access, and (e) engaging in activity that demonstrates oversight and control of transactions.

A "seller" of prepaid access would be defined as "any person that receives funds or the value of funds in exchange for providing prepaid access as part of a prepaid program directly to the person that provided the funds or value, or to a third party as directed by the person." The "seller" of prepaid access would generally be the party with the most face-to-face contact with the purchaser and would typically be a general purpose retailer, such as a pharmacy, convenience store, supermarket or discount store.

PREPAID PROGRAMS

The Proposed Regulations would apply to entities that are providers or sellers with respect to "prepaid programs." A "prepaid program" would generally be "an arrangement under which one or more persons acting together provide(s) a particular form of prepaid access."

Recognizing that certain prepaid products and services are not conducive to money laundering, FinCEN would specify in the Proposed Regulations that certain types of arrangements would not be considered prepaid programs, including, subject in each case to the requirements described below, (1) programs that use prepaid access to pay employee benefits and compensation, to pay government benefits, such as unemployment, child support, or disaster assistance, or to disburse reimbursement funds from pre-tax flexible spending accounts for health care and dependent care expenses; (2) prepaid products with a limited maximum value of $1,000, provided, among other things, that the maximum value is clearly visible on the prepaid access product; and (3) closed-loop prepaid access products (such as a specific retailer's gift card).

To qualify for these exclusions from the definition of "prepaid program," the prepaid product must not permit funds or value to be transmitted internationally or permit transfers between or among users of prepaid access, such as person-to-person transfers. In addition, unless it qualifies as closed loop prepaid access, the prepaid product cannot provide the ability to load monetary value from other non-depository sources.

REQUIREMENTS UNDER THE PROPOSED REGULATIONS

As described above, issuers, sellers and redeemers of stored value are currently required to establish AML programs and comply with CTR filing obligations; under the Proposed Regulations, providers and sellers of prepaid access would need to comply with these requirements. As part of their AML programs, providers and sellers of prepaid access would be required to have policies and procedures to verify the identity of customers who obtain prepaid access through a prepaid program and would have to retain customer identifying information, including name, date of birth, address and identification number, for five years.

Providers and sellers of prepaid access also would become subject to the same SAR filing obligations as other types of MSBs. In addition, providers of prepaid access (but not sellers) would need to retain for five years transactional records generated in the ordinary course of business by the payment processor or other party that facilitates prepaid access

activation, loads, reloads, purchases, withdrawals, transfers, or other prepaid-related transactions.

Finally, providers of prepaid access would be required to register with FinCEN as MSBs. In registering with FinCEN, the provider of prepaid access would need to identify each prepaid program for which it is the provider of prepaid access. Sellers of prepaid access would not be required to register with FinCEN.

COMMENT PERIOD

Comments on the Proposed Regulations must be submitted on or before July 28, 2010.

SEC Proposes Advertising Rule Amendments for Target Date Funds

The SEC issued proposed amendments to Rule 482 under the Securities Act of 1933, as amended (the "Securities Act"), and Rule 34b-1 under the Investment Company Act of 1940, as amended, that are designed primarily to provide additional information about target date funds to potential investors. Because of the impact of market events in 2008 on target date funds and their increased importance as retirement savings investment vehicles, the SEC has devoted particular attention to issues raised by target date funds. In 2009, target date funds were the subject of a joint hearing by the SEC and DOL and congressional testimony by SEC Chairman Mary L. Schapiro and Andrew J. Donohue, Director of the SEC's Division of Investment Management (as discussed in the May 26, 2009 *Alert*). In 2010, the SEC and DOL subsequently issued a joint bulletin designed to provide basic information to Directors on target date funds (as discussed in the May 18, 2010 *Alert*). The major elements of the proposed amendments (the "Amendments") are described below.

DEFINITION OF TARGET DATE FUND AND SCOPE OF THE AMENDMENTS

The Amendments define a target date fund as an investment company that has an investment objective or strategy of providing varying degrees of long-term appreciation and capital preservation through a mix of equity and fixed income exposures that changes over time based on an investor's age, target retirement date, or life expectancy ("Target Date Funds"). For purposes of the Amendments, the "Target Date" of a Target Date Fund is deemed to be either: (i) the date, including a year, included in the name of the Target Date Fund, or (ii) if no date is used in the name of the Fund, the date described in the fund's prospectus as the approximate date that an investor is expected to retire or cease purchasing fund shares.

The Amendments would, in general terms, apply to advertisements and supplemental sales literature (collectively, "Marketing Materials") that place more than an insubstantial focus on one or more Target Date Funds. Whether Marketing Materials place a more than insubstantial focus on one or more Target Date Funds will be based on the facts and circumstances surrounding the Marketing Materials. Materials that may not be primarily focused on marketing Target Date Funds (*e.g.,* a complete list of each fund within a fund complex, together with their performance), but that are nonetheless considered Marketing Materials under Rules 482 and 34b-1 would not be deemed to place a more than insubstantial focus on Target Date Funds; however, materials related to a specific Target Date Fund or to multiple Target Date Funds that are designed to

market the Target Date Fund or Target Date Funds to investors will be deemed to place a more than insubstantial focus on Target Date Funds.

USE OF TARGET DATES IN FUND NAMES

Under the Amendments, Marketing Materials placing more than an insubstantial focus on one or more Target Date Funds, and that include the name of a Target Date Fund that includes a Target Date (*e.g.,* XYZ 2030 Fund), would be required to disclose the percentage allocations among types of investments (each an "Asset Class"), such as equity securities, fixed income securities, and cash and cash equivalents, for the Target Date Fund. The Amendments do not specify the Asset Classes to be used or the methodology for calculating allocations; however, the Asset Classes disclosed in Marketing Materials would need to conform to the asset allocation disclosure contained in the fund's prospectus. Target Date Funds that operate as funds-of-funds would have to disclose the percentage allocations among Asset Classes of the investments made by underlying funds, not the allocation among underlying funds. A Target Date Fund that is permitted to invest within a percentage range in an Asset Class could disclose the range in response to the Amendment.

If Marketing Materials were submitted for publication prior to a fund's Target Date, they would have to disclose the Target Date Fund's intended allocation among Asset Classes at the Target Date. Alternatively, if the Marketing Materials were submitted for publication at or after the Target Date of the Target Date Fund, the Marketing Materials would have to disclose the Target Date Fund's actual allocation among Asset Classes as of the most recent calendar quarter end. In either case, the disclosure would have to clearly indicate that the allocations among Asset Classes are as of the Target Date or quarter end, as applicable.

The Asset Class disclosure would have to appear immediately adjacent to the first use of the Target Date Fund's name in print Marketing Materials, or immediately following the Target Date Fund's name in radio or television Marketing Materials; and in either case, would have to be presented in a manner reasonably calculated to draw investor attention to the information.

ASSET ALLOCATION TABLE, CHART, OR GRAPH AND LANDING POINT ALLOCATION

Under the Amendments, Marketing Materials (whether printed or delivered through an electronic medium), that place a more than insubstantial focus on one or more Target Date Funds would also be required to include a prominent table, chart, or graph that clearly depicts the percentage allocations among Asset Classes over the life of the Target Date Fund at identified periodic intervals that are no longer than five years in duration (the "Graphic Depiction"). Additionally, the Graphic Depiction would be required to depict the percentage allocations among Asset Classes at (i) the inception of the Target Date Fund, (ii) the Target Date, (iii) the first date, including a year, at which the Target Date Fund reaches its final allocation among Asset Classes (the "Landing Point"), and, (iv) in the case of Marketing Materials that relate to a single Target Date Fund, as of the most recent calendar quarter ended prior to the submission of the Marketing Materials for publication. The requirement to include a Graphic Depiction would apply to all Target Date Funds, including those that do not include the Target Date in their name.

The Amendments would also require that Marketing Materials related to a single Target Date Fund submitted for publication prior to the Landing Point or to multiple Target Date Funds with different Target Dates that all have the same pattern of allocation among Asset

Classes include a statement immediately preceding the Graphic Depiction that provides the following information: (i) that the allocation among Asset Classes will change over time; (ii) the Landing Point (or for a multiple Target Date Fund presentation, the number of years after the Target Date at which the Landing Point will be reached), an explanation that the allocation among Asset Classes will become fixed at the Landing Point, and the intended allocation among Asset Classes at the Landing Point; and (iii) whether, and the extent to which, the intended allocation among Asset Classes may be modified without a shareholder vote.

The requirement to include a Graphic Depiction would not apply to radio or television Marketing Materials; however, any radio or television Marketing Materials that place a more than insubstantial focus on a Target Date Fund that includes the Target Date in its name would have to disclose (i) the Landing Point, (ii) an explanation that the allocation among Asset Classes becomes fixed at the Landing Point, and (iii) the intended allocation among Asset Classes at the Landing Point.

DISCLOSURE OF RISKS AND CONSIDERATIONS RELATING TO TARGET DATE FUNDS

The Amendments would require Marketing Materials that place more than an insubstantial focus on one or more Target Date Funds to include statements advising the investor (i) to consider, in addition to his or her age or retirement date, other factors, including the investor's risk tolerance, personal circumstances, and complete financial situation, (ii) that an investment in the Target Date Fund is not guaranteed and that it is possible to lose money by investing in the Target Date Fund, including at and after the Target Date, and (iii) unless disclosed as part of the statement immediately preceding the Graphic Depiction, whether, and the extent to which, the intended allocation among Asset Classes of the Target Date Fund may be modified without a shareholder vote.

Although the Amendments contain no express provision relating to board oversight, the release proposing the Amendments states that the SEC expects a Target Date Fund's board of directors to monitor the exercise of any discretion an investment manager may have to modify the fund's "glide path."

ANTIFRAUD GUIDANCE

The SEC is also proposing amendments to the general anti-fraud guidance regarding investment company sales literature provided in Rule 156 under the Securities Act. Specifically, Rule 156 would be amended to clarify that statements regarding the appropriateness of an investment in an investment company could be misleading if they (i) place emphasis on a single factor, such as an investor's age or tax bracket, as the basis for determining that an investment is appropriate, or (ii) suggest, whether express or implied, that investing in the securities of an investment company is a simple investment plan or that it requires little or no monitoring by the investor. The proposed changes would apply to all types of investments companies, not just Target Date Funds.

PROSPECTUS DISCLOSURE

The Amendments do not propose any changes to current prospectus disclosure requirements; however, in addition to requesting comments on the Amendments, the SEC is requesting comments on whether current prospectus disclosure for Target Date Funds is sufficient. In making this request, the SEC notes that current prospectuses for Target Date

Funds generally include the following elements, which the SEC believes must be disclosed as part of a Target Date Fund's principal investment strategies and principal investment risks: (1) a description of the glide path, often presented as a table or graph broken down by Asset Class; (2) the significance of specific points along the glide path, such as the Target Date and the Landing Point, and any flexibility retained by the investment manager to deviate from the glide path; and (3) the specific risks attendant to investments in Target Date Funds, such as the risk of loss up to and after the Target Date, and the risk of loss due to the absence of guarantees associated with the investment. The SEC requests comment on whether such disclosure should be expressly required by Form N-1A, and whether any additional disclosures should be required in Target Date Fund prospectuses.

REQUEST FOR COMMENTS

Comments on the Amendments and on the necessity for adopting express prospectus disclosure requirements for Target Date Funds are due by August 23, 2010.

FRB Issues Final Guidance on Sound Incentive Compensation Practices

The FRB issued final guidance relating to the incentive compensation policies and practices of banking organizations under the FRB's supervision. The guidance applies to all banking organizations supervised by the FRB, the Office of the Comptroller of the Currency, the Office of the Thrift Supervisors and the Federal Deposit Insurance Corporation (the "Agencies").

The final guidance contains three key principles that banking organizations should follow to ensure that compensation incentives do not encourage employees to take risks that could jeopardize the safety and soundness of the organization. These principles are:

- Incentive compensation arrangements at a banking organization should provide employees incentives that appropriately balance risk and financial results in a manner that does not encourage employees to expose their organizations to imprudent risk.
- These arrangements should be compatible with effective controls and risk-management.
- These arrangements should be supported by strong corporate governance, including active and effective oversight by the organization's board of directors.

The final guidance provides banking organizations with considerable flexibility in structuring their incentive compensation arrangements in ways that both promote safety and soundness and that help achieving the arrangement's other objectives. It does not impose any pay cap requirement or use a "one size fits all" approach. It also includes several provisions designed to reduce burdens on smaller banking organizations and other banking organizations that are not significant users of incentive compensation. Large banking organizations ("LBOs") are expected to develop and adhere to more systematic and formalized policies, procedures and processes relating to incentive compensation.

The FRB also announced that the Agencies' special horizon review of incentive compensation at the LBOs is well underway. The Agencies intend to continue to regularly review incentive compensation arrangements at LBOs through the supervisory process.

GOODWIN PROCTER FINANCIAL SERVICES PRACTICE

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The review of incentive compensation at other banking organizations will be part of the regular, risk-focused examination process for those organizations.

OTHER ITEMS OF NOTE

FDIC Postpones Planned Deposit Insurance Premium Increases

The FDIC staff recommended that the FDIC Board of Directors postpone additional planned premium increases beyond the increase of three basis points scheduled for January 1, 2011. At their June 22, 2010 meeting, each of the five members of the FDIC Board of Directors concurred with the FDIC staff's recommendation. For background on the FDIC premium increases and prepayment requirements, please see the November 24, 2009 *Alert*.

FDIC Adopts Final Rule Extending the Transaction Account Guarantee Program

The FDIC Board of Directors adopted a final rule (the "Final Rule") that extends the Transaction Account Guarantee ("TAG") Program from June 30, 2010 to December 31, 2010 for insured depository institutions currently participating in the TAG Program. The TAG Program provides customers of participating banks with full deposit insurance coverage on transaction accounts. The Final Rule gives the FDIC Board of Directors the option to extend the TAG Program until December 31, 2011 without further rulemaking. For background on the proposed versions of the Final Rule, please see the April 13, 2010 *Alert* and the June 30, 2009 *Alert*.

FinCEN Publishes Administrative Rulings Regarding Application of Section 311 Special Measures

FinCEN published two administrative rulings regarding special measures adopted by FinCEN pursuant to Section 311 of the USA Patriot Act. In both rulings, FinCEN considered the application of special measures prohibiting U.S. financial institutions from opening or maintaining a correspondent for the sanctioned non-U.S. bank. In the first ruling, FinCEN determined that a U.S. bank may make a one-time transfer of funds to a non-U.S. bank subject to special measures when the transfer is made to satisfy the U.S. bank's obligations under a standby letter of credit on behalf of a U.S. company. In the second ruling, FinCEN concluded that a U.S. bank was not prohibited from cashing redemption and dividend checks issued by the U.S. bank on behalf of a U.S. customer to a bank subject to Section 311 special measures that is a shareholder of the U.S. customer.

FinCEN Releases 14th SAR Activity Review-By the Numbers

FinCEN released its "14th SAR Activity Review – By the Numbers," which covers suspicious activity reports ("SARs") filed in 2009. According to the report, the total number of all SARs filed by financial institutions declined from 1.29 million in 2008 to 1.28 million in 2009, the first time since 1996 that the total number of SARs filed declined over a one-year period.