Thoughts on the Future of U.S. Banking Regulation

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Key Themes

- Deregulatory Agenda: The deregulatory agenda under the Trump Administration should render the U.S. financial services regulatory environment hospitable to international banks with U.S. operations
- Regulatory Balkanization: If left unchecked, the balkanization of the international financial services regulatory landscape could further complicate foreign bank participation in the U.S. market (and, as well, U.S. bank participation in foreign markets)
- Regulatory Concerns: Current areas of concern/focus among the U.S. banking regulators include financial crimes and conduct issues, data management, integration and aggregation, vendor management and cybersecurity

The New Deregulatory Agenda

- The deregulatory agenda under the Trump Administration should render the U.S. financial services regulatory environment hospitable to international banks with U.S. operations
- Canadian banks well positioned for U.S. growth
- Secretary of the Treasury Mnuchin recently released a report on existing banking laws and regulations in light of core principles for the supervision and regulation of the U.S. financial system contained in the President’s February 2017 Executive Order 13772

The New Deregulatory Agenda

Treasury Report's overarching themes:

- Insufficiently tailored rules not aligned with risk and complexity of banks
- Multiple banking agencies have overlapping jurisdiction and do not coordinate sufficiently
- Cost of compliance is disproportionate to benefits
- DFA has inhibited economic growth, particularly market liquidity and provision of credit
- Need to harmonize rules and standards

The New Deregulatory Agenda

- Regulatory reform more likely to emanate from the Treasury recommendations and regulatory action than from legislative proposals
- The deregulatory agenda has the potential to benefit international banks through:
  - Higher thresholds for the application of **enhanced prudential standards**
  - **Recalibrating IHC regulatory standards** including a focus on U.S. assets and risk profile
  - Greater consideration of **parent support and home country standards**
  - Providing relief under the **Volcker Rule**, particularly for foreign funds offered solely outside of the U.S.
  - More stringent **impact analysis** and greater agency accountability and transparency in supervision

U.S. Banking Agency Leadership

- U.S. banking agency leadership is in flux
- Expect significant change in the leadership of the U.S. banking agencies in 2017 including:
  - A new Comptroller of the Currency has been nominated
  - Three vacancies on the Federal Reserve Board
  - Fed Chairmanship may change
  - Key officer positions at the Fed
  - A new head of the FDIC has been nominated

U.S. Banking Agency Leadership

- U.S. banking agency leadership is in flux – impact:

  - Unsettled leadership has led to delay and inertia
  - Slow progress in White House and Congress on key appointments
  - Hopes for full-blown regulatory reform may not be realistic in the short term, given time frames for legislative and regulatory action and inability to achieve interagency consensus

International Regulatory Balkanization

- If left unchecked, the balkanization of the international financial services regulatory landscape could further complicate foreign bank participation in the U.S. market (and, as well, U.S. bank participation in foreign markets)
- International standard setters encountering roadblocks to convergence
    - Disagreement over Basel capital floors
    - Implementation of the Fundamental Review of the Trading Book and Net Stable Funding Ratio
    - Not just a U.S. issue
    - Not just a banking issue
- No transparent assessment of cumulative impact of multiple regulations

International Regulatory Balkanization

- The effort to adopt prescriptive international standards ultimately leads to divergent national rules-based approaches to supervision and regulation that create unintended consequences:
  - Increased operational and compliance **costs**, which are magnified for banks operating across multiple jurisdictions
  - **Barriers** to market entry, which impede innovation
  - **Constrained flows** of capital and liquidity across global markets
  - **Uncertainty**, which impedes planning and absorbs critical resources
  - Incentives for firms to **reduce** global footprint

U.S. Banking Regulatory Agenda

- Current areas of concern among the U.S. banking regulators include **financial crimes and conduct issues**
  - Expect financial crimes and conduct issues to remain top of mind for U.S. regulators
  - Enforcement actions in response to conduct issues not likely to slow, especially those related to consumer harms
  - Cannot underestimate the risk and impact of private litigation
  - FinTech solutions can mitigate litigation and reputational risk
  - Banking regulators increasingly demand sophisticated compliance and surveillance solutions

U.S. Banking Regulatory Agenda

- Current areas of concern among the U.S. banking regulators include **financial crimes and conduct issues** *(continued)*

  - Focus on AML/AFT/OFAC programs amid heightened expectations for more robust detection and response capabilities
  - Conflict between customer demand for faster and greater access to accounts and banking services and need to mitigate risk of financial crime
  - Foreign banks need to consider cross-border differences in scope of application, definitions, requirements and multiplicity of responsible agencies; additional considerations for correspondent relationships

U.S. Banking Regulatory Agenda

- Current areas of concern among the U.S. banking regulators include **data management, integration and aggregation systems and vendor management**
- Different systems for payment processing and clearing across the U.S. – Canada border pose challenges
  - Pending upgrades to Canadian payments infrastructure should improve interoperability and increase payment speeds
  - Near-term back office pressures should be well offset by long-term improvements to cross-border banking

U.S. Banking Regulatory Agenda

- Current areas of concern among the U.S. banking regulators include **data management, integration and aggregation systems and vendor management** *(continued)*

- Data management, integration and aggregation are key for banks operating cross-border
  - Clear data mapping and end-to-end data flows
  - Identification and automation of remaining points of manual intervention
- Vendor management focus on continuity of critical operations and vendor substitutability
- Importance of contingency planning

U.S. Banking Regulatory Agenda

- Current areas of concern among the U.S. banking regulators include **cybersecurity**

- Canadian banks well sensitized to cyber risks given high penetration of electronic banking channels

- Cyber risk is a priority for federal and state banking regulators in the U.S.
  - FFIEC Cybersecurity Assessment Tool
  - ANPR issued by U.S. federal bank regulatory agencies
  - Final rule issued by the New York Department of Financial Services

U.S. Banking Regulatory Agenda

- Current areas of concern among the U.S. banking regulators include **cybersecurity** *(continued)*
- Better coordination among U.S. and international regulators needed
  - Divergent standards are dangerous as well as costly and inefficient
  - Need for common lexicon – speaking the same language
  - Need for continued public-private partnership
    - Financial and Banking Information Infrastructure Committee (FBIIC) U.S. regulatory coordination
    - G-7 and BIS initiatives (e.g. Fundamental Elements of Cybersecurity for the Financial Sector)
    - Financial Services Information Sharing and Analysis Center (FS-ISAC) private industry forum for global financial services sector

Executive Order on Cybersecurity

- The President's May 2017 Executive Order on Cybersecurity requires greater alignment of national efforts to manage cybersecurity risk
- The EO requires a report from the Secretaries of State, Treasury, Defense, Commerce and Homeland Security by end-June on international cybersecurity priorities including for investigation, attribution, cyber threat information sharing, response, capacity building and cooperation
- The EO requires an engagement strategy for international cooperation in cybersecurity
- Differing national standards could complicate efforts

Risk Mitigation

- FinTech can partner with banks and banking regulators to reduce cyber risks and compliance burdens
- Need to see FinTech less as a disruptor and more as a strategic partner
- Big Data technologies can aid detection and prevention of cyber threats and reduce compliance and surveillance challenges through a systematic approach to data review and analysis
- Adoption of FinTech and Big Data tools can provide a competitive advantage

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