Complex Structured Finance Activities

FIL-52-2004
May 20, 2004

TO: CHIEF EXECUTIVE OFFICER

SUBJECT: Regulatory Agencies Seek Comment on Interagency Statement on Sound Practices Concerning Complex Structured Finance Activities

Summary: *The financial regulatory agencies and the Securities and Exchange Commission are seeking comment over a 30-day period on an interagency statement governing complex structured finance activities arranged by banking organizations for their customers and/or for their own purposes. Comments are due by June 18, 2004.*

The Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Office of Thrift Supervision, and the Securities and Exchange Commission (the agencies) are seeking public comment on a proposed interagency statement on sound practices concerning complex structured finance activities of entities that the agencies supervise. Comments are due by June 18, 2004.

As recent events have highlighted, a financial institution may assume substantial reputational and legal risk if it enters into a complex structured finance transaction with a customer who uses the transaction to circumvent regulatory or financial reporting requirements, to evade tax liabilities, or to further other illegal or improper behavior.

Structured finance transactions encompass a broad array of products with varying levels of complexity. This guidance addresses *complex* structured finance transactions, which usually share several common characteristics. First, they typically result in a final product that is often nonstandard and is structured to meet the specific financial objectives of a customer. Second, they often involve professionals from multiple disciplines within the financial institution and may have significant fees or high returns in relation to the market and credit risks associated with the transaction. Third, they may be associated with the creation or use of one or more special purpose entities (SPEs) designed to address the economic, legal, tax or accounting objectives of the customer and/or the combination of cash and derivative products. Finally, and perhaps most important, they may expose the financial institution to elevated levels of market, credit, operational, legal or reputational risks.

The interagency statement describes the types of internal controls and risk-management procedures that the agencies believe are particularly effective in assisting financial institutions to identify and address the reputational, legal and other risks associated with complex structured finance transactions. The statement, among other things, recommends that financial institutions have effective policies and procedures in place to:

- identify those complex structured finance transactions that may involve heightened reputational and legal risk,
- ensure that those transactions receive enhanced scrutiny by the institution, and
- ensure that the institution does not participate in illegal or inappropriate transactions.

For further information, please contact William A. Stark, Associate Director, Capital Markets Branch, on (202) 898-6972, or Jason C. Cave, Chief, Policy Section, Capital Markets Branch, on (202) 898-3548, in the FDIC's Division of Supervision and Consumer Protection.

For your reference, FDIC Financial Institution Letters may be accessed from the FDIC's Web site at http://www.fdic.gov/news/news/financial/2004/index.html. To learn how to automatically receive FDIC Financial Institution Letters through e-mail, please visit http://www.fdic.gov/news/announcements/index.html.

Michael J. Zamorski
Director
Division of Supervision and Consumer Protection

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Attachments:

- May 19, 2004, Federal Register, pages 28980-28991 - PDF 91k

Distribution: FDIC-Supervised Banks (Commercial and Savings)

NOTE: Paper copies of FDIC financial institution letters may be obtained through the FDIC's Public Information Center, 801 17th Street, NW, Room 100, Washington, DC 20434 (1-877-275-3342 or (703) 562-2200).