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# Foreword

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This report was prepared primarily to inform Congressional members and key staff of ongoing assignments in the General Accounting Office's Financial Institutions and Markets issue area. This report contains assignments that were ongoing as of January 2, 1996, and presents a brief background statement and a list of key questions to be answered on each assignment. The report will be issued quarterly.

This report was compiled from information available in GAO's internal management information systems. Because the information was downloaded from computerized data bases intended for internal use, some information may appear in abbreviated form.

If you have questions or would like additional information about assignments listed, please contact James Bothwell, Director; Helen Hsing, Associate Director; or Thomas McCool, Associate Director, on (202) 512-8678.

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## *Financial Institutions and Markets*

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### **ENSURING EFFECTIVE REGULATION**

**TITLE: FEDERAL RESPONSES TO FINANCIAL CRISES (233391)**

**BACKGROUND :** Linkages among financial and market sectors make it easier for local disturbances to spread widely and rapidly throughout the financial system. Responsibility related to defusing threats to system stability is shared among U.S. agencies with different agendas and different authorities to act.

**KEY QUESTIONS :** 1) What were the problems that led to financial crises in the past 20 years? 2) What players (public and private) responded--what did each do, why, how did they interact, what uncertainties existed? 3) What can be learned from past federal responses to these financial crises?

**TITLE: FARM CREDIT SYSTEM: FEDERAL INSURANCE PROGRAM ISSUES (233403)**

**BACKGROUND :** The Farm Credit System Insurance Corporation (FCSIC) administers a federal insurance program for System banks. The local lending associations that cooperatively own these banks now hold most System capital. However, FCSIC cannot tap association capital to shore up troubled banks.

**KEY QUESTIONS :** 1) To what extent should local System lending associations be required to participate with System banks in Farm Credit System Insurance Corporation's (FCSIC) insurance program? 2) How much flexibility should FCSIC have to set insurance premiums?

**TITLE: SURVEY OF THE FEDERAL RESERVE SYSTEM'S FINANCIAL TRENDS AND OPERATIONS (233416)**

**BACKGROUND :** The Federal Reserve System (FRS) is the nation's central bank & sets monetary/ economic policy, supervises/regulates banks, & provides services to banks & the public. The FRS also provides an important source of federal revenue, last year it earned nearly \$17 billion. The FRS is unique, however, since its member banks are owned by the private sector--not the gov't.

**KEY QUESTIONS :** 1) What has been the Fed. Reserve System's (FRS) expense/revenue trends for the last 5 yrs.? 2) Does FRS have reasonable procedures for operating areas such as prsnl., travel, ethics, and oversight? 3) How does FRS budget/operations compare with other bnkng. agencies? 4) Are there issues affecting the operating areas that could impact FRS finances during the next svrl. yrs.?

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### ENSURING EFFECTIVE REGULATION

**TITLE: REVIEW OF THE COMMODITY FUTURES TRADING COMMISSION'S USE OF ITS AUTHORITY TO EXEMPT CONTRACTS FROM FEDERAL REGULATION (233442)**

**BACKGROUND :** Under the Futures Trading Practices Act of 1992, CFTC may exempt any contract from its regulation, provided the contract is consistent with the public interest & will not adversely affect CFTC's ability to oversee the regulated markets. CFTC has exempted 3 over-the-counter (OTC) contracts & has issued a proposed rule to exempt certain exchange-traded contracts.

**KEY QUESTIONS :** Q1: What standards has the Commodity Futures Trading Commission (CFTC) developed and applied to exempt swaps, hybrids, and energy contracts? Q2: Do these standards provide CFTC with a coherent framework within which to review future exemptive proposals?

**TITLE: STUDY OF THE FEDERAL DEPOSIT INSURANCE CORPORATION IMPROVEMENT ACT OF 1991 (FDICIA) PROVISIONS FOR PROMPT CORRECTIVE ACTION AND STANDARDS FOR SAFETY AND SOUNDNESS (233448)**

**BACKGROUND :** GAO was instrumental in inserting the Prompt Corrective Action (PCA) provisions into the FDIC Improvement Act (FDICIA). Since FDICIA's passage in 1991, concerns have been raised that regulators have not actively taken PCA actions and that additional tripwires are needed to improve the condition of problem banks and protect the insurance funds from losses.

**KEY QUESTIONS :** 1) Are the regulations implementing FDICIA Sec's 131 & 132 in place & adequate to meet congressional intent? 2) Are regulators promptly imposing Prompt Corrective Action (PCA) enforcement actions on institutions having capital and/or safety and soundness problems? 3) Have PCA actions improved problem institutions and protected the depository insurance funds?

**TITLE: REVIEW OF THE NASD INVESTOR HOTLINE (233460)**

**BACKGROUND :** The Penny Stock Reform Act of 1990 mandates a toll-free NASD Hotline to provide investors with broker disciplinary history information. Congressional hearings, the press and GAO reports have raised concerns about the accuracy of the Hotline information and its effectiveness in protecting investors.

**KEY QUESTIONS :** 1) How accessible is the Hotline's toll-free number to investors? 2) How accurate is the Hotline information? 3) How useful is the information to the investor? 4) What methods are used to inform investors of the Hotline number?

**ENSURING EFFECTIVE REGULATION**

**TITLE: UPDATE OF OTC DERIVATIVES REPORT (233468)**

**BACKGROUND:** In May 1994, we issued a report on derivative financial products. Since then there has been widespread press coverage of and congressional interest in large losses attributed to derivatives. Legislation has been introduced and regulators and the FASB have taken numerous actions related to derivatives.

**KEY QUESTIONS:** 1. Since May 1994, what changes have there been in the nature and extent of the use of derivative products? 2. What lessons can be learned from recent losses? 3. How have regulators and the FASB responded to derivatives developments?

**TITLE: GOVERNMENT-SPONSORED ENTERPRISES: OVERSIGHT OF DERIVATIVES ACTIVITY (233470)**

**BACKGROUND:** Government-sponsored enterprises (GSEs) issue and use derivative products. One particular product, structured notes, played a rôle in Orange County's bankruptcy. These notes are designed to pay returns based on changes in some underlying index. At year end 1994, GSE structured notes totaled over \$100 billion. Questions have been raised about oversight of such GSE activity.

**KEY QUESTIONS:** (1) What are the benefits and risks of issuing structured notes? (2) What are the GSEs' duties for disclosing information to investors and ensuring suitability of investors? (3) What is the nature and extent of federal regulators' oversight of GSEs? (GSEs include Fannie Mae, Freddie Mac, Sallie Mae, Farm Credit System, and Federal Home Loan Bank System).

**TITLE: COMPARISON OF RISK BASED CAPITAL REQUIREMENTS ACROSS FINANCIAL SERVICES INDUSTRIES (233478)**

**BACKGROUND:** GAO has reported how inadequate capital requirements hindered prompt regulatory action in major bank, thrift, and insurance failures. New risk based capital requirements for banks and insurers still may not adequately reflect all solvency risks. Capital requirements, which vary across financial services industries, could create competitive disparities.

**KEY QUESTIONS:** 1) How do capital requirements and regulatory uses of capital compare across financial services industries? 2) How do regulators measure and assess capital adequacy?

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### **ENSURING EFFECTIVE REGULATION**

**TITLE: STATEMENT ON NATURAL DISASTER PROTECTION PARTNERSHIP ACT OF 1995 (233484)**

**KEY QUESTIONS :** Does this bill reduce GAO's concerns about the cost, administration, and oversight of the proposed disaster insurance program compared with last years bill?

**TITLE: QUESTIONS FROM 10/25/95 HEARING ON SECURITIES AND EXCHANGE COMMISSION AND COMMODITIES FUTURES TRADING COMMISSION ENFORCEMENT PRACTICES (233487)**

**KEY QUESTIONS :** As a result of our testimony, the requester has asked that we respond in writing to a list of 21 questions, about Securities and Exchange Commission and Commodities Futures Trading Commission enforcement activities.

### **CONSUMER PROTECTION & ACCESS TO SERVICES**

**TITLE: SURVEY OF CONTROLS OVER INITIAL PUBLIC OFFERINGS OF SECURITIES (233430)**

**BACKGROUND :** SEC processed over 500 equity initial public offerings valued at over \$40 billion in 1993. Recent press accounts allege that insiders have access to IPOs to the exclusion of the general investing public.

**KEY QUESTIONS :** 1) Do initial public offering (IPO) practices by large and small underwriters ensure that all investors are treated fairly and given equal access to information and trading opportunities? 2) Should SEC amend its rules to require the disclosure of the disciplinary actions by underwriters for violating IPO related rules?

### **CONSUMER PROTECTION & ACCESS TO SERVICES**

**TITLE: OTC DERIVATIVES SALES PRACTICES (233441)**

**BACKGROUND :** During recent hearings, questions were raised on the adequacy of over-the-counter (OTC) derivatives sales practices. Corporations, governments, and other entities have reported large losses using OTC derivatives. Some have blamed those losses on dealer sales practices.

**KEY QUESTIONS :** 1) How widespread is the usage of complex Over-The-Counter (OTC) compared with mortgage-backed derivative products or structured notes? 2) What is the nature and extent of sales practice problems associated with these products? 3) What corrective actions, if any, are appropriate?

**TITLE: REVIEW OF AUDIT TRAIL COMPLIANCE (233462)**

**BACKGROUND :** The Futures Trading Practices Act of 1992 (FTPA) requires implementation of enhanced audit trail requirements by the futures exchanges. The Commodity Futures Trading Commission (CFTC) reviewed the exchanges' efforts to meet the enhanced requirements and issued a report on November 28, 1994. The Act requires that GAO comment on the CFTC report.

**KEY QUESTIONS :** Q1: Has CFTC issued any rules or guidance since FTPA was enacted and did these address the act's intent? Q2: What progress have the exchanges made in meeting the new audit trail standards? Q3: What methodology did CFTC use to assess compliance with audit trail standards? Q4: How do the exchanges and CFTC use audit trail data to identify trade practice abuse?

**TITLE: THE FAIR LENDING LAWS AND THEIR ENFORCEMENT (233463)**

**BACKGROUND :** In response to persistent reports that lending discrimination is a major problem in the financial services industry, Congress has begun to question the effectiveness of bank regulation and oversight in the fair lending area and the zeal with which the Equal Credit Opportunity Act, the Fair Housing Act, and the Home Mortgage Disclosure Act have been enforced.

**KEY QUESTIONS :** (1) How is credit discrimination defined? (2) What is the magnitude of the problem? (3) How effectively are the Equal Credit Opportunity Act, the Fair Housing Act, and the Home Mortgage Disclosure Act being implemented and enforced? (4) Are there ways to improve voluntary compliance with these laws?

**CONSUMER PROTECTION & ACCESS TO SERVICES**

**TITLE: IMPLEMENTATION AND EFFECTIVENESS OF BANK HOLDING COMPANY ACT PROHIBITIONS ON BANKS TYING OF CREDIT AND RELATED SERVICES (233474)**

**BACKGROUND :** The Bank Holding Company Act Amendments of 1970, Sec. 106(b) prohibits banks from tying products and services with those of affiliated companies. The requestors expressed concern that banks have increasingly tied credit to a customer's use of a bank's, or an affiliate's, underwriting and insurance services. Banks believe regulatory barriers should be removed.

**KEY QUESTIONS :** 1) How have the sources of and availability of credit changed over the last 25 year in regards to providers and their market share? 2) What are regulators doing to prevent and discover tying abuses? 3) What are the views of regulators and financial industry officials on the continued need for section 106(b)?

**TITLE: EXAMINATION OF STATES' INSURANCE AGENT LICENSING SYSTEM (233479)**

**BACKGROUND :** Insurance and securities regulators rely on licensing to screen out incompetent/unethical sellers. State licensed agents sell over 98 percent of all life insurance policies. Agents selling life insurance in a state must be licensed by that state. Sellers of securities, including variable insurance, must be Nat'l Assoc. of Securities Dealers registered.

**KEY QUESTIONS :** 1) How does state-by-state insurance agent licensing and National Association of Securities Dealers registration for sellers of securities differ? 2) What is the role of insurance/securities companies in licensing/registration? 3) How and what data do insurance and securities regulators share?

**TITLE: DESCRIPTION OF THE U.S. AND INTERNATIONAL PAYMENT SYSTEMS AND CLEARANCE SETTLEMENT SYSTEM, INCLUDING THE ON-GOING DEVELOPMENTS AND EMERGING ISSUES WITHIN THESE SYSTEMS (233483)**

**BACKGROUND :** Payment and clearance systems are the means through which various financial transactions are executed by the affected parties; e.g., check clearing and foreign exchange transactions. These services are increasingly being offered by non-banks. This has led to Congressional concern about how these systems operate. Senate Banking has suggested a primer could be useful.

**KEY QUESTIONS :** 1) What services do the key players in the U.S and foreign payment and clearance systems provide? 2) What are the interactions among the various systems of payments/clearance? 3) What are the current issues involving payment and clearance systems? 4) What regulatory structure and/or oversight mechanisms are in place for these systems?

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### **ORGANIZATION & EFFCNCY OF FINANCIAL REGS**

**TITLE: INTERSTATE BANKING AS IT APPLIES TO THE BRANCHES AND AGENCIES OF FOREIGN BANKS (233428)**

**BACKGROUND :** Recent studies have shown that foreign banks hold a relatively large share of the U.S. commercial banking market, especially of commercial and industrial loans. Although there are likely many reasons for this, there is concern that U.S. laws and regulations give foreign banks a competitive advantage over domestic banks operating in the U.S.

**KEY QUESTIONS :** 1) Under what forms of organization do foreign banks operate in the U.S. and how are most organized? 2) Do U.S. banking laws and regulations apply to foreign banks operating in the U.S.? 3) What roles do foreign banks play in the U.S. economy? 4) Do differences in regulation of U.S. and foreign shell branches give foreign banks advantage(s) in U.S. markets?

**TITLE: COMPARISON OF FOREIGN BANKING SYSTEMS TO THE UNITED STATES (233435)**

**BACKGROUND :** The requester wants objective information about the bank regulatory structures in other countries, specifically the role of central banks, to help in considering various US regulatory consolidation proposals.

**KEY QUESTIONS :** 1)How are foreign bank regulatory systems structured? 2)How do the various participants charged with regulating, supervising, and examining, work together to carry out their various responsibilities? 3)How do the foreign systems compare to the current US system? 4)How do the foreign systems relate to the US regulatory consolidation proposals?

**TITLE: REVIEW OF FEDERAL DEPOSIT INSURANCE CORPORATION OPERATIONS AND THE IMPLICATIONS OF BANK REGULATORY CONSOLIDATION (233438)**

**BACKGROUND :** FDIC experienced significant growth in the 1980s due to unprecedented bank failures. However, with current improvements in the health of the banking industry FDIC is now downsizing its organization. At the same time, the effectiveness of the total bank regulatory structure is being debated as to its relevance in today's complex financial environment.

**KEY QUESTIONS :** (1) How will FDIC's missions, strategies, priorities, and programs be reflected in its downsized operations and processes? (2) How will FDIC's major operating divisions (Supervision, Resolutions, and Depositor and Asset Services) complement each other in serving FDIC's mission? (3) How would the 3 integrate into a consolidated reg. structure?

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### **ORGANIZATION & EFFCNCY OF FINANCIAL REGS**

**TITLE: EFFECTS THE INTERSTATE BANKING AND BRANCHING ACT WILL HAVE ON REPORTED LENDING AND DEPOSIT DATA (233467)**

**BACKGROUND :** The Interstate Banking and Branching Act requires GAO to review the act's effect on the lending and deposit information currently provided to the regulators and the Congress. The primary concern is that consolidated bank reporting will not provide information about loans and deposits at the state and regional level.

**KEY QUESTIONS :** Will the Interstate Banking and Branching Act result in a material loss of information that depository institutions currently provide to the regulators and the Congress?

**TITLE: EXAMINATION OF THE BANKING REGULATORY STRUCTURE IN JAPAN (233475)**

**BACKGROUND :** The Japanese regulatory system regulates the largest banks in the world. Our work on foreign banking regulatory systems has concentrated on major European and North American regulatory structures. To provide additional and comprehensive perspective on worldwide bank regulatory structures, we are reviewing the Japanese bank regulatory structure.

**KEY QUESTIONS :** (1) What is the structure of the Japanese bank regulatory system? (2) How do the participants in the regulatory structure work together to carry out their responsibilities? (3) What role(s) does the Bank of Japan play in this structure including (a) the development and implementation of monetary policy and (b) financial crises resolution?

### **CREDIT ALLOCATION & CAPITAL FORMATION**

**TITLE: EFFECTS OF PRIVATIZATION OF THE FEDERAL NATIONAL MORTGAGE ASSOCIATION AND THE FEDERAL HOME LOAN MORTGAGE CORPORATION (233420)**

**BACKGROUND :** As Gov't. Sponsored Enterprises (GSEs), Fannie Mae & Freddie Mac received certain benefits from, & are restricted in certain ways by their federal charters. These charters also give rise to potential risks to the taxpayer & may grant competitive advantages to these entities. A statutory mandate requires GAO to review issues involved with removing federal sponsorship of these GSEs.

**KEY QUESTIONS :** 1) How desirable and feasible would it be to repeal Fannie Mae's and Freddie Mac's (GSEs) federal charter? 2) What would be the legal and regulatory effects? 3) What would be the effects on the secondary market for mortgage loans? 4) What would be the effect on the GSEs' required capital and its cost? 5) What would be the effect on housing availability and affordability?

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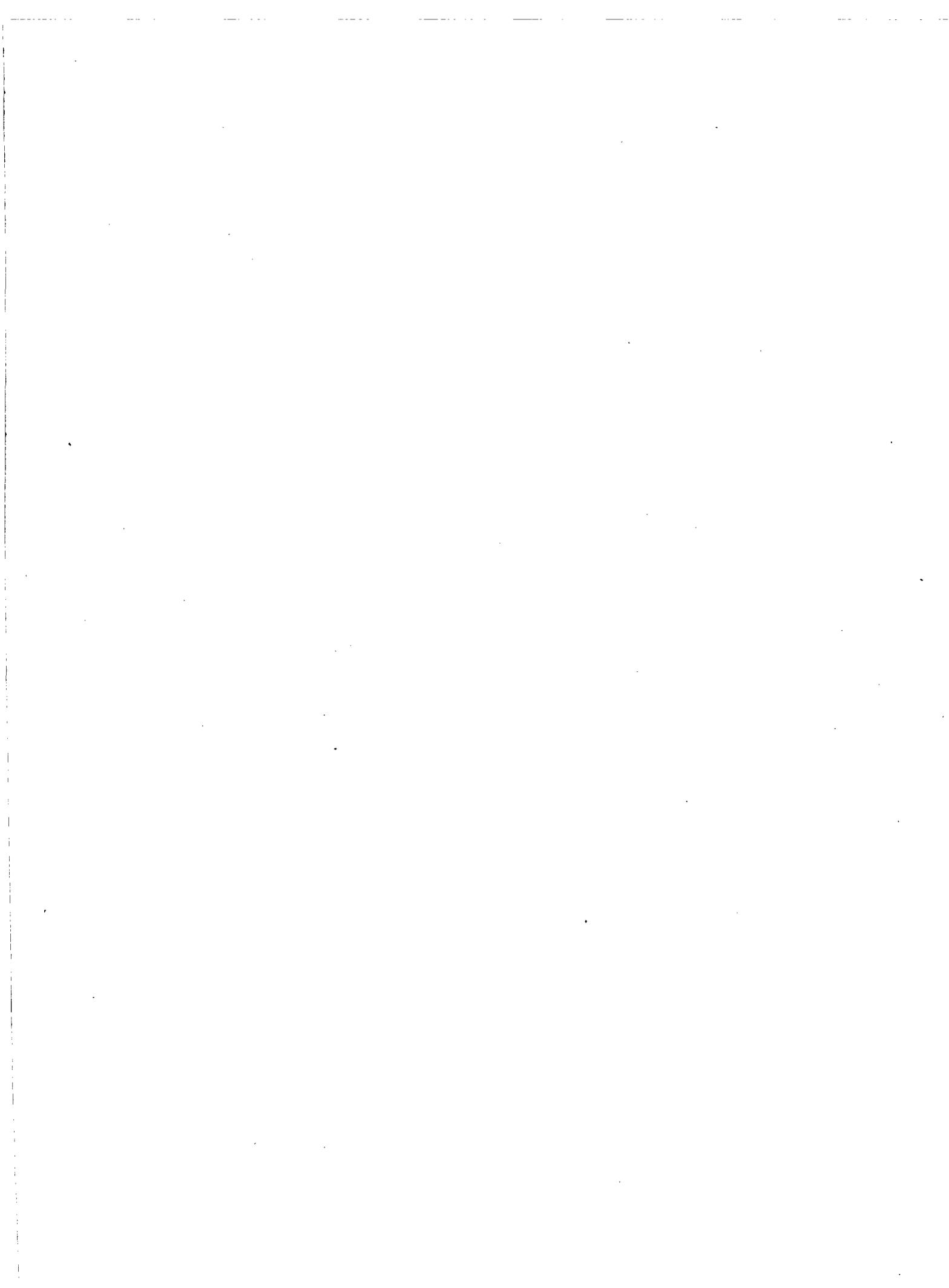
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### **CREDIT ALLOCATION & CAPITAL FORMATION**

**TITLE: MUTUAL FUNDS: BANK PROFITABILITY (233421)**

**BACKGROUND :** The banking industry is losing some deposit business, and the earnings therefrom, to mutual funds. At the same time, a number of banks are generating earnings by providing mutual funds services themselves.

**KEY QUESTIONS :** (1) What is the profitability to banks of providing mutual funds services? (2) Is this profitability greater than the earnings lost because of competition with mutual funds? This is part of a body of work responding to requests on bank relationships with mutual funds.



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