



Single Counterparty Credit Limits Rule (SCCL): Market update

Implementation challenges and moving forward

Since the Federal Reserve Board (FRB) issued final rules on June 18, 2018 to establish the Single Counterparty Credit Limit (SCCL) Rule,¹ in-scope banks have been busy implementing capabilities to comply with the calculation, reporting, and monitoring requirements. On November 20, 2019, the FRB published the final Instructions² for the preparation of FR 2590 Single-Counterparty Credit Limits Reporting Form, which will be effective in March 2020. Be on the lookout for an upcoming publication on the final release of FR 2590.

On October 10, 2019, FRB published final rules that tailor its regulations for domestic and foreign banks to more closely match their risk-based profile categories. The final rules introduced the below changes on banks' SCCL compliance requirements:

- Application of SCCL requirements for intermediate holding companies (IHCs) of foreign banking organizations (FBOs) is now based on the risk profile of the US IHCs instead of the risk profile of the foreign bank's combined US operations (CUSO). For some FBOs, this has removed the formal compliance requirements, though given the relevance to overall risk management capabilities there is interest at some FBOs in continuing to move forward with key aspects of implementation.
- The final rules extend the compliance date for US IHCs with less than \$250 billion in assets that are subject to Category II or III standards from January 1, 2020 to January 1, 2021. This extension provided additional time for the covered US IHCs to enhance their capabilities to comply with the monitoring and reporting requirements.

On November 8, 2019, the FRB proposed to amend the final SCCL rule to extend the initial compliance dates for the CUSO of FBOs by 18 months. The proposed initial compliance dates applicable to the CUSO of an FBO would be July 1, 2021 for an FBO that has the characteristics of a global systemically important bank and January 1, 2022, for any other FBO. The initial SCCL compliance dates applicable to any US IHC of an FBO were not extended. Any US IHC of an FBO is expected to be in compliance with the final SCCL rule as of January 1, 2020, or by July 1, 2020, as applicable per the final SCCL rule.

Industry challenges

Many domestic and foreign banks have experienced challenges in their SCCL implementations, the nature of which have been highly dependent on bank-specific data management and credit risk management capabilities. Some examples of challenges include:

Data requirements

The SCCL ruleset requires data inputs which, in many cases, are not consistently available or require new processes to allow the banks to reliably extract source system data. Below are some examples in which banks are developing solutions to meet the requirements on additional data elements:

- Ultimate parent company – identification of the ultimate parent company and reporting the credit exposure against each counterparty and its affiliates collectively
- Counterparty exemption status – categorization of the counterparties that may be exempted or excluded from certain aspects of the SCCL rule
- Collateral and guarantee eligibility – incorporation of only the collateral and guarantees that meet eligibility criteria
- Economic interdependence – collection of additional information on the economic connectivity among select counterparties
- Control relationships – collection of additional information on the control relationships among select counterparties

Exposure calculations

For banks that have immature calculation processes related to Exposure at Default (EAD) measures, the SCCL final rule requires alignment with the calculation logic defined in Federal Reserve Regulation Q.³ Even in cases in which a bank may have a mature EAD process in place, the daily monitoring requirement presents challenges for banks that have a less frequent approach to sourcing relevant data and applying exposure calculations for some or all business lines.

FR 2590 report processes

Many banks are facing some challenges in their journey to build a robust FR 2590 process as they work to ensure that not only are sufficient controls in place but also that they are operating effectively to provide appropriate assurance over regulatory reports (e.g., data quality checks, reconciliation with data sources and other regulatory reports). The FRB requires the FR 2590 report to be attested and signed by the Chief Financial Officer before submission. Banks must develop processes to ensure that the attestation is supported by an acceptable level of due diligence on the quality and integrity of data being provided on the FR 2590.

What can banks do to ensure they are ready for SCCL?

As banks continue to progress against plans for SCCL compliance and FR 2590 reporting deadlines, below are some areas that can assist in enabling readiness and reducing regulatory risk on this set of requirements:

Assess data quality and integrity impacts on SCCL compliance

The process for banks to sustain the appropriate level of data quality is an ongoing journey. For SCCL, a holistic approach should be taken to manage the bank's data risk to meet the heightened regulatory expectations.

- Data quality and integrity assessment usually begins with developing an understanding of the current state of data quality in the context of the bank's data architecture.
- Banks should document the end-to-end logical process, the information flows from source systems to the FR 2590 report, and the data quality program that assures the quality of data. This will better enable the identification of key data elements based on impact to SCCL result to determine the level of controls needed to provide materially correct data.
- Implementing data quality management processes that include senior management oversight, accountability frameworks, monitoring of data quality metrics and issue resolution, as well as firm-wide training programs for relevant stakeholders. These processes should also consider regulatory expectations related to independent data quality assurance functions and their coverage of SCCL calculation and reporting.

Understand alignment with regulations, guidelines, and other reports

Implementation considerations related to SCCL should be viewed in connection with other regulatory guidance where there should be alignment either in terms of underlying end-to-end data process or actual report outputs to achieve potential synergies. The FRB emphasizes the importance of data consistency among different regulatory reports, which is evidenced by the significant amount of exposure calculation logic in the SCCL final rule that is referenced to the requirements from FRB's Regulation Q Subpart D and Subpart E:

- Several of the FRB's banking regulations and guidance (Lending Limit,⁴ SR 11-10,⁵ SR 14-10⁶) have broad impact on the end to end infrastructure and processes related to counterparty exposure aggregation and reporting.
- Connection points should be analyzed, and long-term strategies should be identified to meet the "spirit" of the FRB's expectations across counterparty exposure regulations. As part of the bank's control framework, a comparison between the FR 2590 report and other regulatory reports may identify common sources of data and reconciliation points to enhance data quality.
- Identification of dependencies, common requirements, and key infrastructure decisions can yield synergies during implementation and other benefits in enhancing the counterparty/credit risk management processes.

Functional alignment

As roles transition from change-the-bank to business as usual, firms need to ensure there are clear lines in the division of roles and responsibilities between Risk, Finance, Business Lines, and reporting teams. While attestation will be performed by the CFO, data owners are responsible for data quality and availability. Below are some illustrative examples of high-level responsibilities:

- Attestation process (CFO and Finance delegates to ensure accuracy)
- Monitoring, management, and control of large exposures (CRO and Credit Risk delegates)
- Data ownership and report preparation (varies by organization)

Conclusion

SCCL is a firm-wide effort requiring senior management attention and cross-functional cooperation and focus. Banks should align with peers and leading practices to meet the regulatory requirements and timelines. As regulators are looking for continuous improvements on the reporting instruction and interpretation, banks should view SCCL compliance as an ongoing journey, and be ready to manage changes.

Endnotes

1. Single-Counterparty Credit Limits for Bank Holding Companies and Foreign Banking Organizations <https://www.federalregister.gov/documents/2018/08/06/2018-16133/single-counterparty-credit-limits-for-bank-holding-companies-and-foreign-banking-organizations>
2. Single-Counterparty Credit Limits Reporting Form (FR 2590) https://www.federalreserve.gov/reportforms/formsreview/FR2590_20191120_i_draft.pdf
3. PART 217—CAPITAL ADEQUACY OF BANK HOLDING COMPANIES, SAVINGS AND LOAN HOLDING COMPANIES, AND STATE MEMBER BANKS (REGULATION Q) https://www.ecfr.gov/cgi-bin/retrieveECFR?gp=&SID=46f958dd5e7b4402b9c91fc47b77b34c&mc=true&n=pt12.2.217&r=PART&ty=HTML#se12.2.217_132
4. 12 CFR Part 32 – Lending Limits <https://www.ecfr.gov/cgi-bin/text-idx?SID=df334e5ef4d33c9d5a6c61af72462ae&mc=true&node=pt12.1.32&rgn=div5>
5. SR 11-10: Interagency Counterparty Credit Risk Management Guidance <https://www.federalreserve.gov/supervisionreg/srletters/sr1110.htm>
6. SR 14-10: Release of the 2014 Federal Financial Institutions Examination Council's Bank Secrecy Act/Anti-Money Laundering Examination Manual <https://www.federalreserve.gov/supervisionreg/srletters/sr1410.htm>

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