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# ADVISORY | Dodd-Frank Act

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# REVISIONS TO BANK HOLDING COMPANY ACT, OTHER BANKING REFORMS AND FEDERAL BANK REGULATORY AGENCY RESTRUCTURING

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Act). The Act imposes new restrictions and an expanded framework of regulatory oversight for many financial institutions, including depository institutions.

The Act will realign, in certain respects, the jurisdictions of the existing bank regulatory agencies and in particular abolish the Office of Thrift Supervision, establish a new federal consumer protection regulator, and a new financial oversight council composed of senior financial policy makers and regulators, as well as make numerous changes in existing federal bank holding company and bank regulatory requirements.

## Key Highlights for Revisions to the Bank Holding Company Act and Agency Restructuring

- Creation of two new regulatory bodies, the abolition of one existing bank regulatory agency, and the restructuring of the authority of the remaining three bank regulatory agencies.
- Enhanced supervisory and regulatory authority of the Fed over non-bank subsidiaries of bank holding companies.
- Greater regulation of transactions with affiliates, insiders and of lending limits.
- Increased regulation of bank activities including debit-card interchange fees, mortgage origination and underwriting.
- Expanded opportunities for interstate branching by banks and bank holding companies, but with tighter supervision of capital and management for institutions entering into such transactions.
- Reform of the federal bank regulators' "bailout" authority.

## Restructuring of Existing Bank Regulatory Agencies

### Abolition of the Office of Thrift Supervision; Preservation of the Thrift Charter

- OTS is abolished, effective 90 days after the transfer date.
- The federal thrift charter is preserved.

### OCC

- OCC retains authority over national banks.
- OCC given OTS regulatory authority over federal savings associations.
- Comptroller directed to appoint new deputy comptroller responsible for the examination and supervision of federal savings associations.

- OCC can continue to charter new federal thrifts.

### FDIC

- FDIC Board seat held by Director of OTS, given to the Director of the new Consumer Financial Protection Bureau.
- FDIC retains authority over state-chartered insured non-Fed member banks.
- FDIC given authority over state-chartered savings associations.

### Federal Reserve Board

- Fed retains authority over bank holding companies.
- Fed retains authority over state Fed-member banks.
- Fed given OTS regulatory authority over savings and loan holding companies.

## New Federal Agencies

### Financial Stability Oversight Council

- New council composed of the Secretary of Treasury as Chair of the Council, together with the Chairmen of the Fed, SEC, CFTC, FDIC, NCUA, the Directors of FHFA, the CFPB, the Comptroller of the Currency, and a member appointed by the President having insurance expertise.
- Authority to identify as a systemic risk (subject to special prudential regulation) limited to U.S. and foreign nonbank financial companies "predominantly engaged" (as defined in the Act) in the U.S. in activities that are "financial in nature" under Section 4(k) of the BHC Act.
- Special federal regulation triggered "if the Council determines [by 2/3 vote, including an affirmative vote of the Chair of the Council] that material financial distress at the U.S. [or foreign] nonbank financial company . . . could pose a threat to the financial stability of the U.S."
- Council authorized to recommend to primary federal regulators "new or heightened standards and safeguards" with respect to a "financial activity," "if the Council determines that the conduct, scope, nature, size, scale, concentration, or inter-connectedness of such activity or practice could create or increase the risk of significant liquidity, credit, or other problems spreading among bank holding companies and nonbank financial companies, financial markets of the United States, or low-income, minority, or underserved communities."

### Bureau of Consumer Financial Protection (CFPB)

- New independent bureau is established within the Federal Reserve System, headed by a presidentially-appointed Director with Senate confirmation and firewalls to preserve the independence of the Bureau, especially with respect to the issuance of rules and the conduct of enforcement actions.
- Empowered to exercise broad regulatory, supervisory and enforcement authority over "covered persons" and "service providers" with respect to both new consumer financial protection laws and an array of existing consumer financial protection laws (with responsibility for the latter being transferred from the federal banking agencies).

## Bank Holding Company Act Revisions

### Institutions Exempt From the Definition of “Bank” Under the BHC Act

- Imposition of a three-year moratorium on approval of FDIC insurance applications and Change in Bank Control Act notices for ILCs, credit card banks, and trust companies that would qualify for exception from the BHC Act definition of “bank” and that are or would be controlled by a “commercial company” (*i.e.*, a company that derives more than 15 percent of its annual gross revenues from activities that are not “financial in nature” under the BHC Act), except in the case of an institution in danger of default, or a merger or whole acquisition of the commercial company.
- Direction that the GAO conduct a study to determine whether elimination of bulk of exceptions to BHC Act’s definition of “bank” – including exceptions for credit card banks, ILCs, trust companies, and savings associations – is “necessary … to strengthen the safety and soundness of institutions or the stability of the financial system.”
- Credit card banks permitted to make credit card loans to small businesses without endangering their exclusion from the definition of a bank under the BHC Act.

### New Requirements that BHCs Remain Well-Capitalized and Well-Managed

- BHCs required to be “well-capitalized” and “well-managed” to maintain financial holding company status under BHC Act.

### Functional Regulation

- Elimination of strict limitations on Fed exercise of rulemaking, supervisory and enforcement authority over functionally regulated BHC subsidiaries (§ 1848a).
- Fed still required to use, “to fullest extent possible,” examinations and reports of other federal and state regulatory authorities.

### Source of Strength

- New provision added to FDI Act that expressly directs federal regulators to require depository institution holding companies to serve as a source of strength for their depository institution subsidiaries; source of strength obligation extends to any company that controls an insured depository institution, even if that company is not itself a registered bank or savings and loan holding company.

### Fed Acquisition Approval Requirement For FHCs

- Prior approval requirement imposed on any acquisition of a non-insured depository institution company by a financial holding company where the assets to be acquired exceed $10 billion.
- Fed given express statutory authority to consider the “risk to the stability of the United States banking or financial system” when reviewing the acquisition of a non-insured depository institution company by a bank holding company.

### Capital Requirements

- Federal bank regulators would be required to impose on all depository institutions and holding companies a generally applicable leverage capital requirement regardless of the size of the institution and not less than those in effect for insured depository institutions on the date of enactment; effect is to disqualify tier 1 capital treatment for “hybrid” capital items like trust preferred securities issued by bank holding companies. The “regulatory capital deductions” for such hybrid capital instruments issued before May 19, 2009 would be phased in between January 1, 2013 and January 1, 2016. Holding companies with less than $15 billion in assets as of December 31, 2009, would not be forced to make any deductions for instruments issued before May 19, 2009.

- In establishing capital requirements, federal bank regulators required to “seek to make such requirements countercyclical.”

### New Fed Assessment Authority

- Fed directed to assess large bank and thrift holding companies (with total consolidated assets in excess of $50 billion) as well as entities subject to systemic regulation by the Council, in an amount that is “equal to the total expenses the Board estimates are necessary or appropriate to carry out the supervisory and regulatory responsibilities of the Board with respect to such companies.”

## Other Bank Activity/Bank Holding Company Act Revisions

### Enhanced Affiliate Transactions Restrictions

- Restrictions on transactions with affiliates are enhanced by (i) including among “covered transactions” transactions between bank and affiliate-advised investment fund; securities repurchase agreements and derivatives transactions; (ii) adopting stricter collateral rules; and (iii) imposing tighter restrictions on transactions between banks and their financial subsidiaries.

### Lending Limits

- National bank lending limits expanded to include credit exposures to counterparties arising from derivative transactions, repurchase agreements, reverse repurchase agreements, and securities lending or borrowing transactions.
- Insured state banks may only engage in derivative transactions if “the law with respect to lending limits” of the state chartering the bank “takes into consideration credit exposure to derivative transactions.”

### Insider Transactions

- Derivatives are included within the scope of credit for which member banks must negotiate on market terms for insiders.
- New restrictions on insured depository institutions’ purchases of assets from insiders imposed via the FDI Act; FDIC given rulemaking authority over these new asset-purchase restrictions subject to prior consultation with the OCC and FDIC.

### Payment of Interest on Demand Deposits

- Current prohibition on payment of interest on demand deposits (12 U.S.C. § 371a) repealed, effective one year after the date of enactment.

### Interstate Branching

- BHC required to be well-capitalized and well-managed to obtain Fed approval of an interstate acquisition.
- For interstate merger transactions, the responsible federal banking agency must conclude the resulting institution will be well-capitalized and well-managed in order to approve the transaction.
- *De novo* interstate branching authorized for national and state banks; current requirement of individual state opt-in eliminated.

### Interchange Fees

- Fed directed to establish “reasonable and proportional” interchange fees that large issuers (assets equal to or in excess of $10 billion) and payment card networks may charge with respect to electronic debit transactions.
- Payment card networks prohibited from contractually or otherwise preventing merchants from offering discounts for use of another payment network, payment medium and/or setting minimum and maximum dollar values for the acceptance of any type of payment.
- Regulatory authority of Fed extends to network fees and prevention of exclusive network routing arrangements.

### Mortgage Loan Origination and Underwriting

- TILA amended to restrict the payment of fees to real-estate mortgage originators.
- TILA amended to impose minimum underwriting standards on real-estate mortgage creditors, including nonbanks as well as bank creditors and verified ability to pay and income verification.

### FDIC Insurance Reforms

- Permanent increase in deposit insurance level to $250,000; retroactive increase for certain failed institutions. Unlimited deposit insurance for noninterest-bearing transaction accounts statutorily mandated effective December 31, 2010, expiring January 1, 2013.
- Deposit insurance assessment base for an insured depository institution equals the institution’s total assets minus the sum of (1) its average tangible equity during the assessment period, and (2) any additional amount the FDIC determines is warranted for custodial and banker’s banks.
- Minimum reserve ratio increased to 1.35 percent of estimated annual insured deposits or assessment base; FDIC directed to “offset the effect” of the increased reserve ratio for insured depository institutions with total consolidated assets of less than $10 billion.
- FDIC authority to suspend dividends from fund to eliminate procyclical assessments.

### Bank Agency “Bailout” Reforms

- Fed’s emergency lending authority under Section 13(3) now confined to lending facilities with “broad-based eligibility.”
- FDIC authorized to create “widely-available program” to guarantee obligations of *solvent* insured depository institutions and *solvent* depository institution holding companies (including any of their affiliates), but only upon FDIC and Fed determination that there exist “times of severe economic distress.”

- Secretary of Treasury may request that FDIC and Fed act to establish such a program upon a determination that there exists a "liquidity event".
- Such a program may not involve receipt of equity; no express exception for the receipt of warrants.
- Secretary of Treasury (in consultation with the President) to determine maximum amount initially guaranteed under any such program (and any additional amounts), subject to Congressional disapproval.
- FDIC's current authority to establish such debt guarantee programs under section 13(c)(4)(G)(i) of the FDI Act is limited to institutions that have been placed into receivership (as opposed to *solvent* institutions and holding companies).

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If you would like to discuss the Act and our capabilities to assist you in the upcoming rulemaking process, please contact the following members of our firm:


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