

Dodd-Frank Act Implementation:

Executive Overview for Bankers

The 2,319 pages of the Dodd-Frank Act (DFA), daunting as they are in themselves, set in motion a regulatory implementation process several multiples greater than the statute. While the details are all important and must be kept in mind, a consideration of the major themes of the first stages of implementation—and the related statutory timetable—can help in organizing individual banks and the industry as a whole in our efforts to respond to the challenges and opportunities of the new law.

We present an Executive Overview of the key themes of DFA likely to be of most interest to the banking industry more generally. There flow from these themes many more details, in addition to the fine points of issues not presented in this Executive Overview but which can be of major importance to individual institutions. To help with the details the name of a lead ABA expert for each topic is listed in parentheses. Moreover, ABA has provided and will continue to develop additional aids that can be found at www.aba.com/regreform.

DEPOSIT INSURANCE (Jim Chessen)

- 250 K deposit insurance limit effective immediately. Some details may need to be addressed in regulation.
- Transaction Accounts, defined as non-interest bearing, to have unlimited deposit insurance for two years beginning December 31, 2010. Coverage is automatic, no additional premium; existing TAG program continues through the end of 2010.
- Assessment Base changed from deposits to assets on day of enactment, but FDIC must write regulations to deal with significant implementation issues for the change to become operative. Expected toward end of 2010, with likely application for 2011 Q1.
- DIF recapitalization plan: FDIC to revise recapitalization plan in the fall of 2010, to include new minimum DIF ratio of 1.35% to be reached by 2020, a new Designated Reserve Ratio (long-run target), and consider whether to include a dividend policy (made optional under DFA) once targeted ratio is reached.

BUREAU OF CONSUMER FINANCIAL PROTECTION (BCFP) (Rich Riese)

- BCFP created upon enactment of DFA. Transfer Date announced for July 21, 2011, when designated consumer laws will be transferred to BCFP, and when enforcement, reporting, and general regulatory authorities become effective. Treasury has interim authority to set up the new bureau's infrastructure.
- Preliminary fact-finding and policy-development likely to occur leading up to the BCFP Transfer Date.
- New "UDAAP" standard, allowing BCFP to identify practices that are *abusive* (added to authority regarding "unfair" or "deceptive").
- Examination Program: BCFP will develop program for examination of financial firms (to go into effect after the BCFP Transfer Date), especially non-bank firms,

and banks with more than \$10 billion in assets; may develop a program for back up examination of banks with less than \$10 billion in assets and request reports.

- State attorney general authority to enforce federal financial consumer laws becomes effective on the BCFP Transfer Date.
- Federal preemption for consumer rules more limited, perhaps resulting in a more case-by-case application.

MERGER OF OCC AND OTS (Mark Tenhundfeld)

- By mid-January 2011, OCC, OTS, FDIC, and Federal Reserve must submit joint plan for merger, to be completed by July 21, 2011—the OCC-OTS **Transfer Date** (which can be extended by 6 months).
- Changes in Bank Supervisors: Supervision of all federal savings associations goes to OCC, state-chartered savings associations to FDIC, all bank and S&L holding companies to Federal Reserve on OCC-OTS Transfer Date.
- On the OCC-OTS Transfer Date, Federal Reserve acquires responsibility to supervise non-depository subsidiaries of holding companies.
- On OCC-OTS Transfer Date, Federal Reserve obtains authority to set capital standards for bank and S&L holding companies.

PRUDENTIAL SUPERVISION (Mark Tenhundfeld)

- Position of Federal Reserve Board Vice Chairman for Supervision is created.
- Collins Amendment on Capital: BHCs over \$500 million may not count newly-issued trust preferred securities as capital; BHCs over \$15 billion must phase out existing TruPS from capital. Banks/thrifts and holding companies will become subject to the same minimum capital rules.
- On OCC-OTS Transfer Date parent companies of insured banks and savings associations can be required to serve as source of strength for insured institutions
- After the OCC-OTS Transfer Date, all financial holding companies required to meet well-capitalized and well-managed tests. S&L holding companies must meet well-capitalized/well-managed tests to engage in financial activities otherwise only permitted for financial holding companies. Well-capitalized/well-managed test required for interstate mergers/acquisitions.
- Credit exposure on derivatives included in national bank lending limit, beginning July 21, 2011. Applied to state bank lending limits, beginning January 21, 2012.
- Charter conversions prohibited where there is a pending enforcement order/MOU
- De novo branching allowed for out of state banks wherever permitted for in-state banks.
- Insider lending restrictions expanded to include derivative, repos and reverse repos, and securities lending/borrowing, beginning one year after OCC-OTS Transfer Date.
- Interest on business checking: starting July 21, 2011, banks will be permitted to pay interest on business checking accounts.
- References to credit ratings removed from statutes, effective July 21, 2012.

NEW SAVINGS ASSOCIATION RULES (Bob Davis)

- As of date of enactment, failure of QTL test by a savings association no longer requires conversion to a bank charter, but rather results in being subject to same activity, branching, and dividend restrictions applicable to national banks.
- Unitary thrifts that conduct non-financial activities may be required by the Federal Reserve, no sooner than within 90 days of OCC-OTS Transfer Date, to form an intermediate holding company to conduct some or all financial activities.
- Mutual holding company dividends: as of the OCC-OTS Transfer Date, savings association subsidiaries of mutual holding companies must give banking regulators 30 day prior notice of declaring dividends, and mutual holding companies must provide regulators 30 day prior notice of any waiver to receive dividends.

MORTGAGE MARKETS (Joe Pigg)

- Most mortgage provisions of DFA are to be under the jurisdiction of the BCFP, but many of the regulations are to be developed by the Federal Reserve or other agencies as specified below.
- 18 months after OCC-OTS Transfer Date the Federal Reserve is to publish regulations on a variety of mortgage origination topics, including steering consumers, discrimination, abusive or unfair lending practices, predatory lending.
- 18 months after OCC-OTS Transfer Date the Federal Reserve is to publish rules setting minimum standards for mortgage underwriting. A “qualified mortgage” safe harbor is created for mortgages meeting these standards.
- New definition established for “high cost mortgages” imposing significant restrictions on mortgages caught by the definition.
- Mortgage creditors will be required to establish escrow accounts, with some exceptions, effective by Federal Reserve Board rule 18 months after OCC-OTS Transfer Date.
- Bank regulators and the SEC are to issue rules by about mid-April 2011 setting 5% risk retention requirements for mortgage-backed securities; rules become effective one year after publication. Bank regulators, HUD, and FHFA are to define “qualified residential mortgages”, exempt from risk retention requirements; no deadline for creating definition.

INTERCHANGE AND DEBIT CARD PROCESSING (Steve Kenneally)

- By April 21, 2011, Federal Reserve to publish rules limiting debit card interchange fees to “reasonable” and “proportional” to the transactions. Exemptions for government-issued cards and for banks with less than \$10 billion in assets. Rules to become effective July 21, 2011.
- The Federal Reserve must finalize rules by July 21, 2011, banning requirements that debit card transactions be processed through any one particular network.

SECURITIES, SWAPS AND OTHER DERIVATIVES (Carolyn Walsh)

- SEC/CFTC joint authority to regulate swaps markets, effective mid July 2011, including swap data reporting requirements; registration of swaps clearing organizations, swap execution facilities, and designated contract markets.

- Exemption from SEC filing for asset backed securities (ABS) held by fewer than 300 persons repealed, with SEC authority to provide rules that vary according to classes. SEC to issue regulations setting new disclosure requirements for all ABS issuers.
- SEC to issue rules requiring ABS issuers to conduct a review of underlying ABS assets.
- By mid-April 2011 SEC is required to issue regulations on conflicts of interest involving ABS, applicable to underwriters, placement agents, initial purchaser/sponsor, or any affiliate or subsidiary thereof.
- By about mid-April 2011, bank regulators and the SEC are to issue rules setting risk retention requirements for ABS classes other than mortgages; rules become effective two years after publication.

EMPLOYEE COMPENSATION (Phoebe Papageorgiou)

- SEC is directed to issue rules requiring public disclosure of executive compensation, including relationship with the company's actual performance; and also disclosure of median compensation of all employees (other than the CEO), total compensation of the CEO, and the ratio of these two amounts.
- National stock exchanges directed to prohibit, by mid-July 2011, listing securities of firms that do not have independent compensation committees.

CORPORATE GOVERNANCE (Phoebe Papageorgiou)

- For the first shareholder meeting occurring after January 21, 2011, SEC registered firms must provide for a non-binding shareholder "say on pay" vote on executive compensation, and a vote on whether to vote again in 1, 2, or 3 years.
- After January 21, 2011, SEC registered firms must provide for a non-binding vote on "golden parachutes" if shareholders are voting on a business combination.
- Upon enactment, SEC is authorized to revise rules to facilitate ability of shareholders to nominate board members.
- Upon enactment, non-accelerated filers under Sarbanes-Oxley not subject to section 404(b) requirements for attestation by outside auditors.

SYSTEMIC SUPERVISION ISSUES

FINANCIAL STABILITY OVERSIGHT COUNCIL (FSOC) (Mark Tenhundfeld)

- Established immediately, made up of 15 members, including all financial regulators. Chaired by Treasury Secretary. First meeting held October 1, 2010.
- Duties include identifying systemically important non-bank financial institutions and subjecting them to enhanced supervision; making recommendations to the Federal Reserve and other financial regulators regarding systemic risk supervisory standards, risk management, living wills. Includes the responsibility to consider systemic impact of accounting standards.
- Also tasked to provide policy guidance to FDIC for resolution of systemically significant firms.

- Immediate responsibility will include coordination of regulatory efforts and facilitating information sharing. Also tasked to give guidance to Office of Financial Research.
- Has unworkable authority to overrule BCFP regulations.

SYSTEMIC SUPERVISION (Mark Tenhundfeld)

- All BHCs with \$50 billion or more in assets immediately subject to enhanced prudential supervision; FSOC can vote to add other BHCs and non-banks to the list; details to be developed, but likely to result in additional capital and liquidity standards, and in potential limitations on activities/practices.
- Concentration limit, financial firms: prohibiting mergers or acquisitions resulting in a firm holding more than 10% of financial industry liabilities. The ban is effective immediately but is subject to a 6-month study by the FSOC and subsequent modification by Federal Reserve rule making 9 months after the study. Exceptions permitted (with Federal Reserve approval) for acquisitions of endangered firms.
- Concentration limit, banks and savings associations: prohibiting interstate merger/acquisitions of insured depository institutions resulting in a firm holding more than 10% of U.S. insured deposits. Exceptions allowed in cases involving FDIC assistance.
- Federal Reserve approval required, after the OCC-OTS Transfer Date, for any acquisition of non-bank firm by bank holding company having more than \$10 billion in assets.
- “Volcker Rule” prohibitions on proprietary trading and sponsorship/investment in hedge funds and private equity funds go into effect earlier of July 21, 2012, or 12 months after agencies write rules. Any required divestitures must be completed within 2 years after effectiveness of Volcker Rule; deadline can be extended for up to 3 times for one year each time.
- Federal Reserve, in consultation with other bank regulators and SEC, to provide to Congress by mid-January 2011, results of a study of the credit market impact of risk retention requirements of DFA and FASB rules 166 and 167.
- Federal Reserve required to publish by December 1, 2010, detailed information on users of any of its recent emergency facilities (up through July 21, 2010).
- Going forward, Federal Reserve required to release information, including rates and terms, on firms that use emergency credit facilities, discount window, and open market operations, within 1 or two years following the activity (release date varies according to the activity).
- FDIC given upon enactment emergency stabilization authority, with Federal Reserve, Treasury, and Congressional sign-off. FDIC might develop in 2010 and publish some guidelines regarding its use/procedures. FDIC’s systemic risk exception authority (used in recent months for TAG and TLGP) is repealed.

SYSTEMIC RESOLUTION (Mark Tenhundfeld)

- Effective immediately, FDIC has systemic resolution authority, applies to holding companies and designated non-bank financial firms; triggered by approval of Treasury Secretary and various agencies relevant to the firm. Does not apply to

federally insured banks/thrifts. FDIC on September 17 issued interim regulations. Losses paid for by fees assessed by FDIC on all systemically significant firms.

- Effective immediately, FDIC has back up examination authority for troubled firms subject to systemic resolution authority; FDIC likely to develop an examination program in the fall 2010.

OFFICE OF FINANCIAL RESEARCH (Mark Tenhundfeld)

- Immediately authorized to begin operations, has authority, including subpoena authority, to ask for any information it considers necessary to consider systemic risk issues.
- Likely to spend initial weeks setting up a research plan and priorities.
- Develop program for obtaining data, including new data submission mandates on banks, potentially of any size.