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## Dodd-Frank Act Score Card June 28, 2010

### Current Status

- On the morning of Friday, June 25, following an all-night push, House and Senate conferees concluded their work on the conference report to the Dodd-Frank Wall Street Reform and Consumer Protection Act.
- The House will vote on – and pass – the final bill on Tuesday, June 29 or Wednesday, June 30. The timing of Senate consideration has been complicated by the passing of Senator Robert Byrd (D-WV). Senate passage is still highly likely; there are several ways for the Senate Democratic Leadership to put together the 60 votes needed for “cloture” (which will cut off debate and allow for a vote on final passage). The conference report is not subject to further amendment in the House or Senate.
- The final bill (technically a conference report) reflects a number of community bank victories as well as one notable disappointment.

### Key Community Bank Victories

**Deposit insurance assessment base** – Changing the assessment base from domestic deposits to assets (minus tangible equity) will save community banks \$4.5 billion over the next 3 years.

**Too-Big-To-Fail** – The final bill goes a long way toward reining in the megabanks and correcting their funding advantages. The TBTF provisions – including new systemic risk regulations, a systemic risk council, and resolution authority – will help level the playing field and focus efforts on the mega-institutions.

**Regulation of nonbank competitors** – The new CFPB will examine and enforce consumer protection rules against nonbank competitors of community banks, ending the unfair advantage these competitors have long enjoyed.

**SOX 404(b)** – The final version of the conference report permanently exempts public companies with capitalization of less than \$75 million from the auditor attestation requirements of SOX 404(b). ICBA has led the fight for this exemption since SOX was enacted in 2002.

**Deposit insurance limit increase** – The final bill will increase the deposit insurance limit to \$250,000.

**Transaction Account Guarantee (TAG) extension** – The final bill extends unlimited deposit insurance coverage for non-interest bearing transaction accounts for two years, offsetting the TBTF advantage enjoyed by large banks in attracting business deposits.

**Volcker Rule** – The final bill generally prohibits banks from engaging in proprietary trading or holding or obtaining an interest in a hedge fund or private equity fund, though there is a *de minimus* exception. ICBA advocated for a strong Volcker Rule. The final bill contains exceptions for securities that community banks typically invest in.

### **ICBA Removed, Exempted Community Banks From, or Improved Adverse Provisions of the Bill**

**Community bank exam exemption from CFPB** – Banks under \$10 billion in assets are exempt from primary examination and enforcement by the CFPB and will continue to be examined by their bank regulators for consumer compliance. ICBA fought for this exemption and defeated a House effort to give the CFPB “backup enforcement” authority over community banks.

**Prudential regulator say over CFPB rules** – Despite the carveout from CFPB examination and enforcement, community banks will be subject to CFPB rules. During conference negotiations, there was significant controversy over the role of the prudential regulators in CFPB rule writing. In the final bill, the CFPB will consult with the prudential regulators prior to proposing a rule and during the comment process. The CFPB will have to respond in writing to any objections raised by prudential regulators.

Once the CFPB has finalized a rule, the Financial Stability Oversight Council may set it aside if, upon a two-thirds vote, the Council finds that the regulation or provision would put “the safety and soundness of the U.S. banking system or the stability of the financial system at risk.”

**Capital treatment of TRUPS** – The “Collins Amendment” bars bank holding companies from holding less capital than their bank subsidiaries. TRUPS proceeds are excluded from Tier 1 capital, but, as a result of the ICBA’s advocacy, BHCs of less than \$500 million are exempt (the Fed’s small BHC policy statement is protected) and TRUPS issued before May 19 by BHCs of less than \$15 billion are grandfathered. BHCs of greater than \$15 billion must begin to transition after two and a half years starting in Jan. 2013, and the transition period will be three years.

**States will continue to set lending limits for state-chartered banks** – The Senate bill would have subjected state banks to national bank lending limits. The final version of the bill allows state banks to continue to follow state lending limits. However, states will have to revise those limits to include credit exposure arising from derivatives transactions. Defeating the Senate bill provision was one of ICBA’s top priorities, and we are satisfied with this outcome.

**Community banks exempt from new fee** – In the final hours of consideration, the conferees adopted a new \$19 billion special assessment on financial firms to offset the costs of the bill. ICBA succeeded in inserting a carve out for financial institution with less than \$50 billion assets.

**“Skin in the game” rule made workable** – The conference report requires that loan originators retain 5% of any loan sold and securitized, unless it is a “qualified residential mortgage.” The conference report exempts from the risk retention requirement low-risk loans that meet certain standards outlined in the legislation, and promulgated under rules to be developed by regulators. It also specifically exempts from risk retention FHA, VA, Farmer Mac and Rural Housing Service loans. In addition, regulators have authority to exempt commercial loans “sold and securitized” which meet certain underwriting standards.

**Fed given flexibility to exempt rural mortgages held in portfolio from new restrictions** – The base text definition of “qualified loans” – which exempts the lender from heightened legal liability to ensure the borrower as the “ability to repay” the loan – excludes balloon loans and contains a points-and-fees threshold, among other provisions. Generally, mortgage lenders have to escrow taxes and insurance. However, as a result of ICBA’s advocacy, the conference report gives the Fed flexibility in applying these requirements to rural loans and requires them to adjust the points-and-fees threshold for smaller loans.

**Derivatives largely exempt community banks** – The derivatives title of the final bill contains provisions advocated by ICBA. Banks that engage in swaps with their customers in connection with providing loans will not trigger the definition of “swaps dealer,” which carries a host of regulatory burdens, nor will banks that use swaps to hedge their own interest rate risk. A de minimus provision will exempt banks and other entities that use swaps infrequently.

The final bill does not mandate higher capital and margin requirements for customized swaps, as previous versions of the bill had. Instead, it would base capital and margin requirements on the economic risks of swaps, rather than whether they are cleared or uncleared.

Unfortunately, conferees removed an exemption from margin requirements for uncleared swaps where one party is an end user.

**The Fed will continue to examine state-chartered community banks and small BHCs** – The Senate bill would have shifted this authority to the FDIC. ICBA fought to reverse this provision.

**CFPB reporting requirements removed** – The Senate bill required banks to collect and submit comprehensive and onerous deposit account data to the CFPB. This provision was removed at the request of ICBA.

**Accredited investor standards** – The Senate bill would have raised the accredited investor wealth test from \$1 million to \$2.25 million and the income test from \$200,000 to \$400,000, thereby making it more difficult for community banks to raise capital in private offerings. The final version of the bill changes the current wealth test to exclude the value of the investor’s principal residence. The SEC will review the income test every four years.

**Federal Home Loan Banks (FHLB) exemption from concentration limits** – The Senate bill would have subjected the FHLBs to concentration limits, cutting off FHLB advances to community banks. ICBA fought to exempt the FHLBs.

**Office of Minority and Women Inclusion** – The House bill would have required each federal banking agency to establish an Office of Minority and Women Inclusion, with a Director

appointed by the President, that would make an assessment of each bank as part of the regular examination process. The conference report significantly dilutes this provision: the Director will be appointed by the agency head, not the President, and the Office will merely develop standards for assessing diversity, it will not make assessments.

## **Disappointments**

**Debit interchange** – ICBA fought tooth and nail against this provision and orchestrated a Dear Colleague letter signed by 131 members of the House. Defeating it was our highest priority. But the determination of Senator Durbin – who is the second ranking member of the Senate – to include his amendment in the conference report ultimately proved decisive. The final bill requires the Fed to set rates for debit interchange that will not account for the full cost of supporting debit transactions. Despite the small bank carve out, which ICBA told Congress was not workable in the marketplace, community banks will likely see a significant reduction in debit interchange. Merchants will be allowed to discriminate based on payment type and to set minimum amounts for acceptance of debit and credit cards. ICBA will work with the Fed to get the best possible implementation.

**Auto dealers** – Despite the opposition of ICBA (and the White House and Pentagon), the final bill exempts auto dealers from the CFPB.

## **New Requirements for Community Banks**

**Executive Compensation** – For publicly-traded community banks, the final bill provides shareholders with a non-binding vote on executive compensation ("a say on pay"). Compensation committees are required to include only independent directors and must have the authority to hire compensation consultants. The SEC has authority to exempt small companies from "say on pay," or at least make it less burdensome.

**Risk Committees** – In addition to nonbank financial companies supervised by the Fed, publicly traded BHCs of more than \$10 billion must establish risk committees with independent directors and at least one "risk management expert." The Fed may also require publicly traded BHCs of less than \$10 billion to establish such committees.

**Expanded affiliate transactions rules** – The definition of "covered transaction" in the affiliate transactions rules would be expanded to include repurchase agreements, derivatives transactions, and securities borrowing and lending.

**New Insider Transaction Rules** – Banks would be subject to new Fed rules governing purchases of assets from, or sales to, insiders.

**Source of Strength Rules for BHCs** – BHCs would be subject to new "source of strength" rules with regard to their depository institution subsidiary.

## **Unfinished Business**

**ILCs** – The final bill imposes a 3-year moratorium on new industrial loan company charters. This statutory moratorium is preferable to the de facto moratorium which is currently in effect. ICBA pressed for a permanent closing of the loophole in the legislation.