Banking & Financial Services Alert

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Dodd-Frank Wall Street Reform and Consumer Protection Act – Summary of Title VI "Improvements to Regulation of Bank and Savings Association Holding Companies and Depository Institutions"

On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act. This new law contains sweeping regulatory reforms. Title VI, which is one of sixteen titles in the more than 2,300 page Act, directly affects banks, thrifts and their holding companies.

This Alert is one of a series, including a previous alert concerning mortgage lending provisions. Other titles of the Dodd-Frank Act contain important provisions that will significantly affect banks and their affiliates, such as additional backup supervisory authority for the FDIC, changes in capital requirements and elimination of regulatory references to credit rating agency grades, such as "investment grade".

We summarize briefly below ten provisions from Title VI that we believe may have the greatest impact on our bank clients:

1. **Interstate Branching:** The law removes essentially all impediments to interstate branching. The previous regime, which permitted states to opt out of interstate banking, which a majority of states, either completely or with conditions had done, has been cast aside. Key southeastern states that had restrictions on branching, including Alabama (which had a reciprocity condition), Florida, Georgia and Mississippi, are now open to branching by state and national banks located outside their borders. This provision is effective immediately.
2. **Regulators to Set Capital Requirements in a Countercyclical Way:** The law directs regulators to consider, among other things, setting capital requirements in a countercyclical manner, "so that the amount of capital required to be maintained by an insured depository institution increases in times of economic expansion and decreases in times of economic contraction, consistent with the safety and soundness of the depository institution." This approach would be markedly different from what has been seen during the current credit crisis where regulators have sharply increased capital requirements for banks notwithstanding severe economic conditions. This provision of the law is effective July 21, 2011.
3. **Interest-Bearing Transaction Accounts Authorized:** Restrictions on the ability to pay interest on transaction accounts have been repealed. This is effective July 21, 2011.
4. **Limitations on Purchase of Assets from Insiders:** The law now prohibits a bank from purchasing assets from, or selling assets to, any officer, director or principal shareholder unless the transaction is on market terms and, if the transaction

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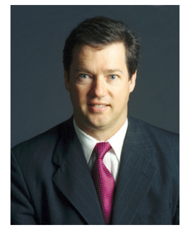

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represents more than 10% of capital, is approved in advance by a majority of the members of the board of directors of the insured depository institution who do not have an interest in the transaction. This provision could impact longstanding practices in community banks where directors, as an accommodation, acquire property or branch facilities for the bank and other routine transactions, such as permitting officers to purchase vehicles from the bank.

5. **Expansion of Lending Limit Restrictions for National Banks and State Member Banks:** Derivative transactions, repurchase transactions and securities lending and borrowing transactions are now swept under the definition of extension of credit for lending limit purposes.
6. **Modification of the Source of Strength Doctrine:** The Board of Governors of the Federal Reserve System has long had a policy that bank holding companies are to serve as a source of strength for their bank subsidiaries. However, this policy has had a mixed record when sought to be enforced by the Federal Reserve. The law now codifies this provision and expands it to any company, whether or not a bank holding company or a savings and loan holding company, that directly or indirectly controls a depository institution. This provision likely means that the Federal Reserve will, in the future, issue mandates for holding companies to provide capital to depository institution subsidiaries.
7. **Restrictions on Proprietary Trading May Have Unforeseen Impact:** The law, in the so-called Volcker Rule, provides a broad prohibition against proprietary trading or acquiring any equity, partnership or other ownership interest in a hedge fund or private equity fund. Because both types of funds can be fairly broadly defined (both investment companies and companies that would be investment companies without the application of certain exemptions and other funds designated by regulatory authorities would be covered), this could impact various types of bank investments in ways not yet fully identified. For instance, the drafters of the law felt it necessary to specifically carve out, and thereby permit, investments in GSE securities, in public welfare investments, such as low income housing tax credit partnerships, and historic tax credit supported investments.
8. **Concentration Limits – Large Financial Firms:** The law establishes concentration limits which prohibit an institution from acquiring a financial company if, upon consummation of the transaction, the resulting company would exceed 10% of the aggregate liabilities of all financial companies or 10% of domestic deposits. There is an exception for acquiring institutions in danger of default. Interestingly, though, Bank of America, Wells Fargo and, possibly, JP Morgan Chase already exceed this threshold. In comparison, other large U.S. banks, such as SunTrust and BB&T, are less than 2% presently.
9. **Restrictions on Transactions with Affiliates Expanded:** Section 23A of the Federal Reserve Act, which limits, and in some cases prohibits, certain transactions with affiliates, has been expanded to include repurchase arrangements, borrowing and lending of securities and derivative transactions. In addition, it now makes clear that a letter of credit is the equivalent of a guaranty for purposes of Section 23A.
10. **Acquisition of Industrial Loan Companies Limited:** The FDIC may not approve an application for deposit insurance for an industrial loan bank, credit card bank or trust bank that is directly or indirectly controlled by a commercial firm prior to July 21, 2013.

If you have any questions, about this new law, please contact one of the attorneys in our Financial Services practice group, http://www.babc.com/Banking-and-Financial-Services. Upcoming Alerts will focus on other portions of this law.