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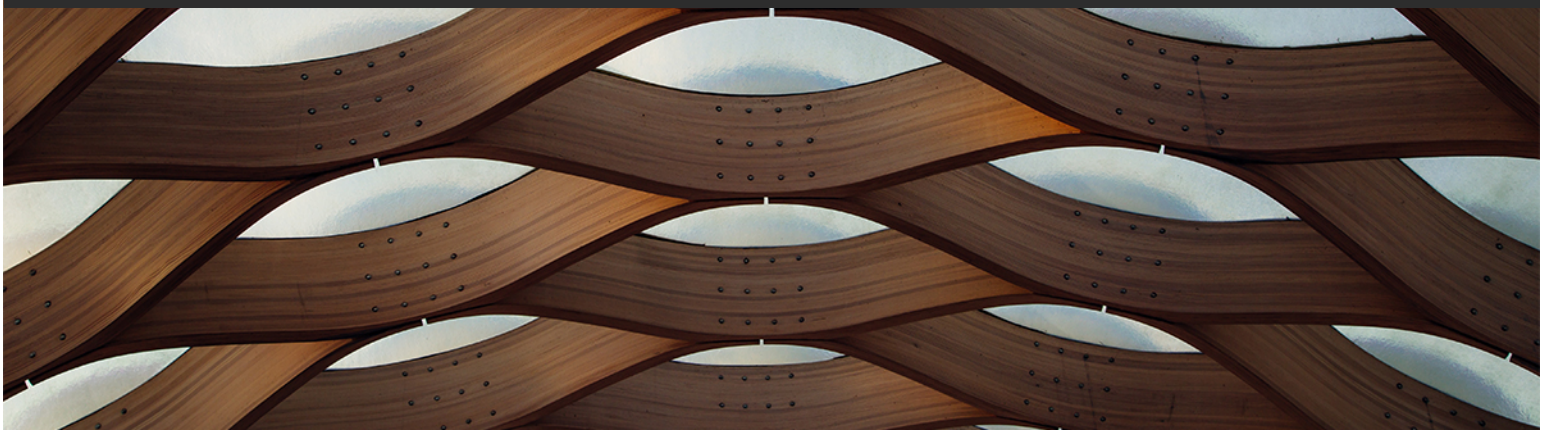

May 2018

Overview of Key Provisions of the 2018 Financial Regulatory Reform Act

On May 24, 2018, President Donald Trump signed into law the Economic Growth, Regulatory Relief, and Consumer Protection Act (the 2018 Financial Reform Act or the Act). The Act rolls back certain provisions of the Dodd-Frank Act of 2010, providing relief to all but the largest banking organizations in the United States.

This ***GT Alert*** provides a high-level overview of the following key provisions of the 2018 Financial Reform Act.

- Amending Mortgage Rules
- Regulatory Relief for Community Banks
- Consumer Protection
- Regulatory Relief for Large Banks
- Capital Formation

Amending Mortgage Rules

- Section 101 - Qualified Mortgage (QM) Status for Loans Held by Small Banks.

QM compliance status will now apply to mortgages originated by and held in the portfolios of small banks, defined as insured depository institutions with less than $10 billion in assets. The practical effect of having QM status for loans is that it will enable small banks to be compliant with the Dodd Frank Act's ability-to-repay (ATR) requirement, which may reduce the legal risk of small banks' residential mortgage lending business. The current size threshold is a much lower $2 billion in assets. Additionally, the Act provides for less stringent loan and underwriting criterion for small banks as defined in this section.

- Section 106 - Mortgage Loan Originator (MLO) Licensing and Regulation.

State-licensed MLOs will receive a grace period and may temporarily work as an MLO in a new state while obtaining license approval in that new state. The grace period will also apply if an MLO moves from being a division of a depository institution to being a non-depository institution, which requires the MLO to be licensed in that state.

- Section 108 - Escrow Requirements Relating to Certain Consumers.

The Act amends the Truth in Lending Act. Certain escrow requirements for loans may be exempted if an insured depository institution or credit union (1) has no more than $10 billion in assets, (2) originated no more than 1,000 first-lien principal dwelling loans in the preceding calendar year, and (3) meets other specified criteria.

- Section 109 - Waiting Period Requirement for Lower-Rate Mortgages.

The required three business day waiting period to provide a consumer with mortgage disclosures prior to the closing of a residential real estate mortgage is waived, if the lender provides the consumer with an amended disclosure that results in lower mortgage interest.

- Section 310 - Consider Use of Alternative Credit Scores for Mortgage Underwriting.

Fannie Mae and Freddie Mac must establish a process to allow for applications of new credit score models. New credit score models must be reviewed and may be approved as new credit score models to be utilized in mortgage underwriting for residential mortgages.

Regulatory Relief for Community Banks

- Section 201 - Community Bank Leverage Ratio (CBLR).

The Act defines the CBLR as the tangible equity capital held by a bank compared to the average total consolidated assets of the bank, regardless of the risk level of the assets. A bank with less than $10 billion in assets may be exempt from current leverage and risk-based capital ratio requirements, if the bank maintains a CBLR above the threshold to be set by regulators between eight and 10 percent. The bank will be deemed "well capitalized" if it meets the CBLR.

- Section 202 - Allowing More Banks to Accept Reciprocal Deposits.

Banks that are deemed "not well capitalized" may be able to accept reciprocal deposits by or through deposit brokers, subject to certain limitations. The total amount of reciprocal deposits of an agent institution (defined as the bank that places the deposit at another bank through a deposit placement network) may not exceed the lesser of $5 billion or an amount equal to 20 percent of the total liabilities of the agent institution.

- Sections 203 and 204 - Changes to the Volcker Rule.

Under certain restrictions, a bank may be exempted from the Volcker Rule, which generally prohibits banks and their holding companies from engaging in proprietary trading and investing in hedge funds. The exemption would apply if (1) a bank has less than $10 billion in assets and (2) trading assets and liabilities are less than five percent of total assets.

Section 204 eases certain Volcker Rule restrictions for any bank, regardless of total assets, related to sharing a name with hedge funds and private equity funds they organize. Under certain circumstances, a hedge fund or private equity fund may share the same name or a variation of the same as a banking entity that is an investment advisor to the fund.

- Section 205 - Financial Reporting Requirements for Small Banks.

Under the Act, the federal banking agencies will be required to issue regulations that reduce reporting requirements of call reports for banks with assets of less than $5 billion. Significantly, this section reduces reporting requirements from every quarter to only the first and third quarter of each year.

- Section 207 - Small Bank Holding Company Policy Statement Threshold.

Section 207 provides for the Board of Governors of the Federal Reserve System to meet within 180 days to increase the threshold of total consolidated assets from $1 billion to $3 billion with respect to the Small Bank Holding Company and Savings and Loan Holding Company Policy Statement. This policy statement currently allows bank holding companies with $1 billion or less in total consolidated assets which also meet other requirements to assume more debt than allowed by larger banks in order to complete a merger.

- Section 210 - Frequency of Examination for Small Banks.

Section 210 of the Act reduces the frequency of federal banking agency examinations from every 12 months to every 18 months for banks with less than $3 billion in total assets.

- Section 213 - Identification when opening an account online.

The Act makes clear that financial institutions may rely on an image or scan of a government-issued identification card or driver's license received electronically by a prospective customer to open a bank account or provide certain online services.

- Section 214 - Classifying High Volatility Commercial Real Estate (HVCRE) Loans.

Under certain circumstances, a bank may now be able to classify certain credit facilities as a regular commercial real estate loan, which previously would have been classified as a HVCRE loan (which carries with it a higher capital risk-weight). Additionally, other opportunities are provided to assist in avoiding a HVCRE classification, including, but not limited to, incorporating the appraised value of the property as a capital contribution, which would reduce the required capital necessary for a bank to hold due to the risk exposure of a HVCRE loan.

Consumer Protection

- Section 215 - Reducing Identity Theft.

This section allows banks to collect electronic signatures from consumers when banks are attempting to verify identities while using the Social Security Administration (SSA) Consent Based Social Security Verification system. The use of the SSA verification system may assist in reducing synthetic identity theft.

- Section 301 - Fraud Alerts and Credit Report Security Freezes.

A consumer reporting agency (CRA) will now be required to increase the length of time that a fraud alert remains on a consumer's credit report for one year, increased from 90 days. Additionally, consumers may directly request for a CRA to place a security freeze on their credit report, which would prevent the CRA from disclosing details of the consumer's credit report if there are new credit report inquiries from third party companies.

- Section 303 - Whistleblowers on Senior Exploitation.

Employees of financial institutions will receive immunity from any lawsuit if the employee makes a report to a regulatory or law enforcement agency of a suspected abuse or unauthorized use of the assets of a senior citizen (defined under the Act as 65 years of age or older).

- Section 304 - Protecting Tenants at Foreclosure.

The Protecting Tenants at Foreclosure Act of 2009 will be restored within 30 days. This 2009 law, which expired in 2014, includes certain notification and eviction requirements to be provided to renters living in foreclosed-upon properties.

Regulatory Relief for Large Banks

- Section 401 - Enhanced Prudential Regulation and the $50 billion threshold.

(1) Effective immediately, banks below $50 billion in assets are **not** subject to:

A. Enhanced prudential standards

B. Mandatory company-run stress testing

C. Mandatory risk committee requirements

(2) Effective immediately, banks between $50 billion and $100 billion in assets are **not** subject to:

A. Enhanced prudential standards

B. Mandatory company-run stress testing

However, are still subject to mandatory risk committee requirements

(3) Effective 18 months from the date of enactment of the Act, banks with assets between $100 billion and $250 billion are **not** subject to enhanced prudential standards or company run-stress tests

However,

A. Such banks are still subject to mandatory risk committee requirements

B. Regulators can later determine that the bank is subject to the enhanced prudential standards

C. Regulators shall, on a periodic basis, conduct mandatory supervisory stress testing

(4) Banks deemed as globally systematically important banks (G-SIBs) and foreign banks with global assets more than $250 billion are still subject to the enhanced prudential standards. Additionally, regulators, at their discretion, can impose enhanced prudential standards for foreign banks with global assets between $100 billion and $250 billion.

- Section 402 - Custody Banks and the Supplementary Leverage Ratio (SLR).

The SLR determines how much capital banks must hold relative to their assets without adjusting for the risk associated with their assets. Custody banks, defined as depository institutions predominately engaged in custody, safekeeping, and asset servicing activities, will not be required to incorporate funds deposited with a central bank when calculating their SLR. The amount of funds deposited at a central bank that may be exempted from the SLR calculation may not exceed the amount of customer deposits linked to fiduciary, custodial, and safekeeping accounts.

Capital Formation

- Section 504 - Registration Requirements for Small Venture Capital Funds.

This section creates a new category for small venture capital funds called Qualifying Venture Capital Funds (QVCFs), which will allow an exemption from the investment company categorization under the Investment Company Act of 1940 (the 1940 Act). There are several registration and disclosure requirements under the 1940 Act that a QVCF would avoid. A venture capital fund is classified as a QVCF if it has (1) no more than 250 investors and (2) no more than $10 million in aggregate capital contributions and uncalled committed capital.

- Section 506 - U.S. Territories Investor Protection.

Investment pools, including mutual funds, in the Commonwealth of Puerto Rico and in the U.S. Territories of the Virgin Islands and Guam are now subject to and must comply entirely with the 1940 Act's disclosure requirements and must register with the SEC. The investment pools that were previously exempt must comply within three years of the date of enactment of the 2018 Financial Reform Act unless the SEC makes a determination to extend the deadline for one additional three-year period.

- Section 507 - Disclosure Requirements for Companies Paying Personnel in Stock.

Within 60 days of the date of enactment of the 2018 Financial Reform Act, the SEC must increase the limit in the amount of stock a company can sell to its personnel without additional disclosure requirements from $5 million annually to $10 million annually. Additional conditions may need to be met for eligibility.

- Section 509 - Streamlined Closed End Fund Registration.

Within one year of the date of enactment of the 2018 Financial Reform Act, the SEC must propose rules that will allow closed-end funds to use certain streamlined reporting procedures that are available under the well-known seasoned issuer (WKSI) status. A closed-end fund is a publicly traded investment company that sells shares to investors during an IPO and share trade on secondary markets. Generally, WKSI status has been reserved for companies that produce goods and services, rather than investment companies, including closed-end funds.

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