



Insights: Alerts

Regulatory Relief Legislation Eases Regulatory Burdens

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On May 24, 2018, President Trump signed the Economic Growth, Regulatory Relief, and Consumer Protection Act (the Act) into law, taking the first step in paring back some of the post-crisis banking regulations imposed under the Dodd-Frank Wall Street Reform and Consumer Protection Act.

This alert summarizes the sections of the Act that most directly impact the regulation of financial institutions. Nearly all of these provisions require the federal banking regulators to adopt regulations to implement the Act or to amend their regulations to conform to the statutory changes contained in the Act.

Section 101 – Minimum standards for residential mortgage loans

The Act amends the Truth in Lending Act to allow depository institutions and credit unions with less than \$10 billion in total consolidated assets to forgo certain ability-to-pay requirements regarding residential mortgage loans. Specifically, loans originated by those institutions are granted a qualified mortgage safe harbor (which carries with it a legal presumption of complying with the ability-to-repay requirements) if the loan: (1) is originated by and retained by the institution; (2) complies with requirements regarding prepayment penalties and points and fees; and (3) does not have negative amortization or interest-only terms. Furthermore, in order for a loan to qualify for such safe harbor status, the institution must consider and verify the debt, income, and financial resources of the consumer during its underwriting process. The Act also provides for circumstances in which the qualified mortgage safe harbor is extended to loans that are sold, assigned, or otherwise transferred: (1) by reason of bankruptcy or failure of the originating institution, (2) to a similar institution, (3) in the event of a merger, or (4) to a wholly owned subsidiary of the institution.

Section 104 – Home Mortgage Disclosure Act adjustment and study

The Act amends the Home Mortgage Disclosure Act of 1975 (HMDA) to exempt depository institutions and credit unions that originate fewer than 500 closed-end mortgages or open-end lines of credit in each of the two preceding calendar years from specified HMDA requirements (particular data points regarding the number and dollar amount of mortgage loans and completed applications). However, a depository institution that has received a rating of “needs to improve record of meeting community credit needs” during each of its two most recent examinations, or a rating of “substantial noncompliance in meeting community credit needs” on its most recent Community Reinvestment Act (CRA) examination, is not exempt from such disclosure requirements.

Section 105 – Credit union residential loans

The Act amends the Federal Credit Union Act so that loans from credit unions to members for non-owner-occupied, one- to four-family residences are not considered member business loans for purposes of the cap on member business loans. Under current law, a loan secured by a one- to four-family residence is excluded from the definition of member business loan only if the dwelling is the member's primary residence. The effect of this change is to expand the ability of credit unions to make loans secured by non-owner-occupied, one- to four-family residences, thereby increasing their ability to compete with banks.

Section 108 – Escrow requirements relating to certain consumer credit transactions

The Act amends the Truth in Lending Act to require the Consumer Financial Protection Bureau to issue regulations to exempt from certain escrow requirements a residential mortgage loan held by a depository institution or credit union that: (1) has assets of \$10 billion or less, (2) originated 1,000 or fewer mortgages in the preceding year, and (3) meets other specified requirements applicable to higher-priced mortgage loans. Under current law, except in certain specified circumstances, a lender, in connection with the consummation of a consumer credit transaction secured by a first lien on the principal dwelling of the consumer, other than a consumer credit transaction under an open end credit plan or a reverse mortgage, must establish an escrow or impound account for the payment of taxes, hazard insurance and certain other periodic payments.

Section 109 – No wait for lower mortgage rates

The Act amends the Truth in Lending Act to eliminate the required mortgage disclosure waiting period (currently three business days prior to consummation of the transaction) with respect to a second offer of credit if the creditor offers a consumer a lower annual percentage rate (APR) in the second offer.

Section 201 – Capital simplification for qualifying community banks

The Act requires the Federal banking agencies to develop a Community Bank Leverage Ratio (defined as the ratio of tangible equity capital to average total consolidated assets) for banks and holding companies with total consolidated assets of less than \$10 billion and an appropriate risk profile. The required regulations must specify a minimum Community Bank Leverage Ratio of not less than 8% and not more than 10%, as well as procedures for treatment of a qualifying community bank that has a Community Bank Leverage Ratio that falls below the required minimum. Qualifying banks that exceed the minimum Community Bank Leverage Ratio shall be deemed to be in compliance with all other capital and leverage requirements, which effectively means that qualifying banks need only manage to a single capital ratio.

Section 202 – Limited exception for reciprocal deposits

The Act amends the Federal Deposit Insurance Act to exclude reciprocal deposits of an insured depository institution from certain limitations on prohibited broker deposits if the total reciprocal deposits of the institution do not exceed the lesser of \$5 billion or 20% of its total liabilities. Reciprocal deposits are defined in the Act as deposits that a bank receives through a deposit placement network with the same maturity (if any) and in the same aggregate amount as deposits (other than deposits obtained through a deposit broker) placed by the bank in another network bank.

To qualify for the exception, a bank must either (1) have been found in its most recent examination to have a composite condition of outstanding or good and must be well capitalized, (2) have obtained a waiver, or (3) not

have an amount of reciprocal deposits in excess of the average of the total amount of reciprocal deposits held on the last day of each of the four calendar quarters preceding the calendar quarter in which the bank was found to not have a composite condition of outstanding or good or was determined to be not well capitalized.

The Act also extends to reciprocal deposits the restrictions on the interest rate paid on brokered deposits by an institution that is adequately capitalized, but not well capitalized, or for which the FDIC has been appointed as conservator.

Section 203 – Community bank relief (Volcker Rule relief)

The Act amends the Bank Holding Company Act of 1956 to exempt from the “Volcker Rule” banks with: (1) total assets of \$10 billion or less, and (2) trading assets and liabilities comprising not more than 5% of total assets. Under current law, the Volcker Rule prohibits banking entities from engaging in proprietary trading or entering into certain relationships with hedge funds and private-equity funds.

Section 205 – Short form call reports

The Act amends the Federal Deposit Insurance Act to require federal banking agencies to issue regulations allowing depository institutions with less than \$5 billion in total consolidated assets and that satisfy such other criteria that the federal banking agencies determine to satisfy reporting requirements with a reduced Report of Condition and Income (i.e., call report) for the first and third reports for a year. Presumably, the federal banking agencies will continue to require a full call report for the second and fourth quarters.

Section 206 – Option for federal savings associations to operate as covered savings associations (with the powers of a national bank)

The Act amends the Home Owners' Loan Act to permit federal savings associations with total consolidated assets of \$20 million or less as of December 31, 2017, to elect to operate, subject to supervision by the Office of the Comptroller of the Currency, with the same rights and duties as national banks (including operating without the lending restrictions applicable to federal savings associations). Subject to rules established by the Comptroller, federal savings associations that make an election to be regulated as a national bank can continue to be regulated as such after they exceed \$20 million in assets.

A federal savings association that has made the election to be regulated as a national bank would continue to be treated as a federal savings association for purposes of governance matters (such as incorporation, bylaws, boards of directors, shareholders and capital distributions), consolidation, merger, dissolution, conversion from mutual to stock form or to another charter, conservatorship, receivership, and such other matters as determined by regulation of the Comptroller.

The Act directs the Comptroller to issue rules with respect to a number of matters relating to the election to be regulated as a national bank, including (1) establishment of required documentation and timelines for making the election, (2) identification of assets and subsidiaries that do not conform to the requirements for a national bank and establishment of a process for bringing those assets and subsidiaries into conformance with requirements for a national bank and procedures for allowing retention of those assets and subsidiaries.

The Act does not address whether the Federal Reserve Board would be able to regulate the holding company for a federal savings bank that elects to be regulated as a national bank as a bank holding company.

Section 207 – Small bank holding company policy statement

The Act requires the Federal Reserve Board to raise the consolidated asset threshold in its Small Bank Holding Company and Savings and Loan Holding Company Policy Statement from \$1 billion to \$3 billion. A bank holding company or savings and loan holding company that has consolidated assets below this threshold and that: (1) is not engaged in significant nonbanking activities; (2) does not conduct significant off-balance-sheet activities; and (3) does not have a material amount of debt or equity securities, other than trust-preferred securities, outstanding, is not subject to consolidated capital requirements. If warranted for supervisory purposes, the Federal Reserve Board may exclude a company from this threshold increase.

Section 210 – Examination cycle

The Act amends the Federal Deposit Insurance Act to allow well-managed and well capitalized banks with up to \$3 billion in assets to have full-scope, on-site examinations every 18 months, rather than every 12 months. Under current law, only banks with up to \$1 billion in assets may qualify for the 18 month examination cycle.

Section 213 – Making online banking initiation legal and easy

The Act facilitates “know your customer” compliance and online account opening by authorizing banks, credit unions and their affiliates to record personal information from a scan, copy, or image of an individual's driver's license or personal identification card and store the information electronically when an individual initiates an online request to open an account or obtain a financial product. The financial institution may use the information for the purpose of verifying the authenticity of the driver's license or identification card, verifying the identity of the individual, or complying with legal requirements. The financial institution must permanently delete any copy or image of an individual's driver's license or personal identification card after use. The Act expressly preempts state law that conflicts with this section.

The utility of this provision may be limited if automatic back-up and archiving systems are not compatible with the Act's requirement to permanently delete any copy or image of an individual's driver's license or personal identification card after use.

Section 214 – Promoting construction and development on main street

The Act amends the Federal Deposit Insurance Act to specify that a federal banking agency may not subject a depository institution to higher capital standards with respect to a high-volatility commercial real-estate (HVCRE) exposure unless the exposure is an HVCRE acquisition, development, or construction (ADC) loan. Under current regulations, which will need to be revised to conform to the Act, a bank must assign a 150% risk weight to an HVCRE exposure.

An HVCRE ADC loan: (1) is secured by land or improved real property; (2) has the purpose of providing financing to acquire, develop, or improve the real property such that the property becomes income-producing; and (3) is dependent upon future income or sales proceeds from, or refinancing of, the real property for the repayment of the loan.

The Act expands the exclusions from the current definition of an HVCRE exposure by (1) excluding loans for (a) the acquisition or refinancing of existing income-producing real property if the cash flow of the property is sufficient to support the debt service and expenses of the property and (b) for improvements to existing income-

producing real property if the cash flow of the property is sufficient to support the debt service and expenses of the property and (2) by counting paid development expenses and contributed real property or improvements towards the borrower's contributed capital.

Upon substantial completion of the project and cash flow being generated sufficient to support the debt services and expenses of the property, an HVCRE ADC loan may be reclassified as a non-HVCRE ADC loan.

Section 401 – Enhanced supervision and prudential standards for certain bank holding companies

The Act amends the Financial Stability Act of 2010 with respect to nonbank financial companies supervised by the Federal Reserve Board and certain bank holding companies, to:

- increase the asset threshold at which certain enhanced prudential standards shall apply, from \$50 billion to \$250 billion, while allowing the Federal Reserve Board discretion in determining whether a financial institution with assets equal or greater than \$100 billion must be subject to such standards;
- increase the asset threshold at which company-run stress tests are required, from \$10 billion to \$250 billion; and
- increase the asset threshold for mandatory risk committees, from \$10 billion to \$50 billion.

The amendments made by this section will take effect on the date that is 18 months after the date of enactment of this Act, except that the amendments will take effect on the date of enactment with respect to any bank holding company with total consolidated assets of less than \$100 billion.

Section 403 – Treatment of certain municipal obligations

The Act amends the Federal Deposit Insurance Act to require certain municipal obligations to be treated as level 2B liquid assets if they are investment grade, liquid, and readily marketable. Under current law, corporate debt securities and publicly traded common-equity shares, but not municipal obligations, may be treated as level 2B liquid assets (which are considered to be high-quality assets).

The Act requires the federal banking agencies to revise their liquidity coverage ratio regulations within 90 days.

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