



Maine Bankers Association  
Bank Expo 2011

# **A Dodd-Frank Update**

**(or, How I Learned to Stop  
Worrying and Love the Government)**

# A bit of perspective....

## Important laws throughout the ages

- **10 Commandments: 2 stone tablets**
- **United States Constitution: 22 pages**
- **Dodd-Frank Act: 2319 pages**
- **Why so many?**  
Yogi Berra: “I knew I would take the wrong train so I left early.”

# Core/brokered deposits

- **DFA requires FDIC to study core and brokered deposit definitions (§ 1506)**
- **FDIC in early stages of study**
- **Focusing on continuum of stable to volatile**
- **May result in changes in how certain deposits are classified**
- **Change in definition of “non-core” for purposes of UBPR**

# Interest on business checking

- **Current rule:**
  - Banks may not pay interest on “demand deposit” accounts
  - Banks may pay interest on “NOW” accounts, but businesses can’t have a NOW account
- **DFA repeals the prohibition against paying interest on demand deposits (§ 627)**
- **Will allow banks to compete for more commercial accounts but cost of funding may increase**
- **Fed recently approved proposed rule inviting comments on repeal’s impact**
- **Remaining issue: How is “interest” defined for purposes of FDIC insurance rule?**

# Changes to insurance coverage

- **Increase to \$250,000 per account, retroactive to January 1, 2008 and indexed to the CPI going forward (§ 335)**
- **DIF floor to be increased from 1.15% to 1.35% by September 30, 2020**
- **Banks over \$10 billion to pay difference (§ 334)**
- **No cap on DIF**

# Capital

- **Basel III announcements – Capital can't be too rich or too good looking**
  - **More capital and more of it in common stock**
  - **Question about applicability to community banks**
- **Collins Amendment limits ability to use trust preferred securities (§ 171)**
- **Countercyclical requirements (§ 616)**

# Preemption

- **Relevant for all banks, both state and federal, large and small**
- **Codification of “Barnett standard” for national banks; application of Barnett standard to federal thrifts**
- **No preemption for operating subsidiaries, affiliates, or agents**
- **Preemption on a case-by-case basis going forward -- do OCC rules survive?**
- **Exportation of interest rates survives**
- **Stay tuned for State AG enforcement actions**

# Mortgage issues

## Key distinction:

- **“Qualified residential mortgage (QRM)” vs. “Qualified mortgage (QM)”**
- **QRM for “skin in the game” requirement**
- **QM for “ability to repay” requirement**

# Skin in the game

- **Banks and issuers of asset-backed securities must hold 5% of risk, subject to exceptions (§ 941)**
- **“Qualified residential mortgages” excluded from rule**
- **FDIC recently approved the QRM proposal**

# QRM proposal

## The basics:

- **Need 20% down (25% if a refi and 30% if a cash-out refi); even loans with PMI must comply.**
- **28% front-end and 36% back-end DTI the minimum.**
- **Borrower credit history restrictions including the requirement that there be no 60-day delinquencies on any debt obligation within the previous 24 months.**

The good: Unlikely to derail already fragile mortgage market, as QRM proposal is quite narrow. Loans with a federal guarantee excluded (including loans sold to Fannie and Freddie while in conservatorship and FHA loans).

The bad: Will be harder to end the conservatorship of Fannie and Freddie and to shrink FHA.

The ugly: When Fannie and Freddie emerge from conservatorship, the rules will apply to a many more loans. Fewer borrowers will qualify for loans to purchase or refinance a home.

# Ability to repay

- **Lenders must act in the best interest of consumers (§ 1405(a))**
- **Lenders must ensure borrowers have the ability to repay (§ 1411)**
- **“Qualified mortgages” presumed to comply with “ability to repay” standard (§ 1412)**

# So what is a “qualified mortgage”?

- **Periodic payments cannot result in increased principal or defer payments of principal**
- **Balloon payments generally not allowed**
- **Income and financial resources must be verified**
- **Rules (to be established) on debt-to-income must be followed**
- **Total points and fees may not exceed 3% of the loan amount**
- **Term of loan may not exceed 30 years**
- **For fixed-rate loans, underwriting must be based on fully amortizing payments, including taxes & insurance**
- **For ARMs, underwriting must be based on the maximum rate during the first 5 years**

# Interchange

- **DFA directs Fed to set “reasonable” interchange fees for debit card transactions (§ 1075)**
- **Fed has published a proposal:**
  - **Two options:**
    - **Calculate allowable costs? Can get up to 12 cents per transaction.**
    - **Safe harbor (i.e., no calculation)? Get 7 cents.**
  - **Alternatively, network may set fees that vary with value of transaction, up to 12 cents.**
  - **No recovery of fixed costs**
  - **No recovery of fraud losses**
- **\$10 billion threshold does not protect community banks**
- **ABA attacking from all angles**

# Inability to use credit ratings

- **A sleeper of an issue**
- **Problem: many credit ratings performed poorly**
- **Response:**
  - Improve credit rating rules
  - Prohibit banking agencies from using ratings in regs (§ 939A)
- **Affected rules:**
  - Capital
  - Permissible investments
  - Certain securities issuances
- **Status**
  - Two ANPRs published but no proposals
  - Agencies really struggling with this

# Affiliate Transaction Rules

- **“Covered transactions” under Section 23A to include, among other things, credit exposure on derivative transactions (§ 608)**
- **Collateral requirements must be met at all times and not just at inception.**

# Lending Limits

## National Banks and Savings Associations

**Added: any credit exposure to a person arising from a derivative transaction, a repurchase agreement, a reverse repurchase agreement, or a securities borrowing or lending transaction. (§ 610)**

## State Banks

**State bank may not engage in derivative transactions unless the lending limit laws of the state in which the bank is chartered take into consideration credit exposure to derivative transactions. (§ 611)**

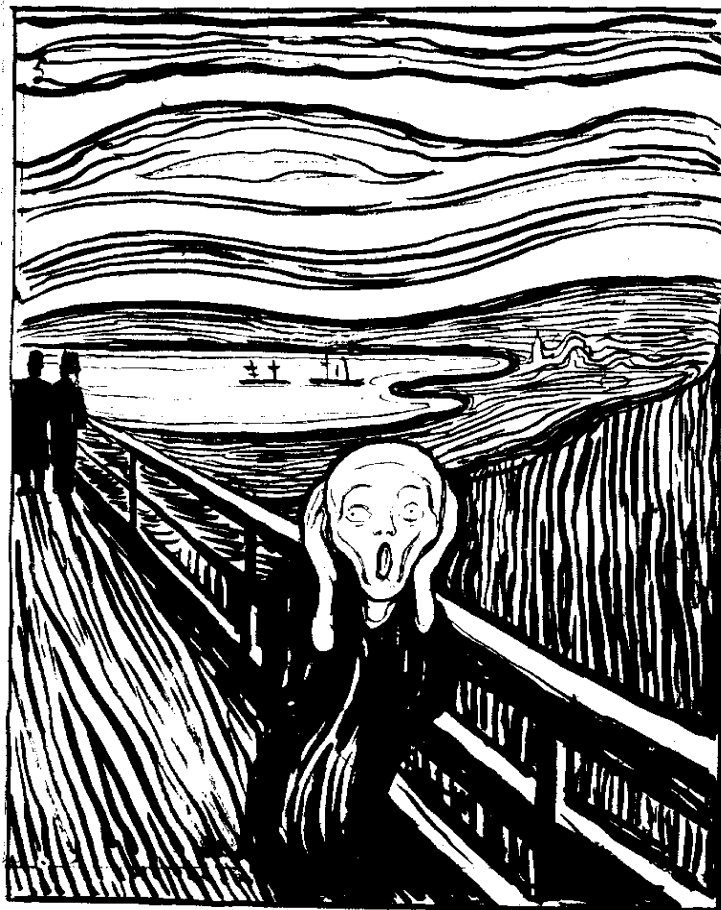
# Other insider transactions

## Insider Asset Purchases and Sales

**Bank may not buy an asset from, or sell an asset to, its executive officers, directors, or principal shareholders (or related interests) unless:**

- **The transaction is on market terms; and**
- **Is approved by majority of disinterested directors if the transaction represents more than 10% of the capital of the bank.**

# Consumer Financial Protection Bureau



# So what's next?

- **Change in Congress likely to impact DFA only at the margins**
- **Likely will be a “technical corrections” bill**
- **Some areas of ABA focus:**
  - **Interchange**
  - **500 shareholder registration threshold**
  - **Muni advisors**
  - **Credit exposures from derivatives**
  - **Use of credit ratings**
  - **BCFP (funding, corporate governance)**
- **Lots more oversight**
- **For consumers, higher fees and less access to credit**

# ABA resources

- ABA's "DFA Tracker" available at <http://regreformtracker.aba.com/>
- Treliant "Dashboard"
- ABA "Experts on Call" (1-800-BANKERS)
- ABAWorks and Toolboxes as needed
  - List of existing ones available at <http://www.aba.com/About+ABA/abatoolboxes.htm>
  - Recently published one on liquidity; working on compensation Toolbox
  - Others to follow as need arises



# Questions?

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