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DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT

On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act") into law. The legislation, a response to the recent economic crisis, is intended to restructure the regulatory framework of the United States financial system, with significant impact on the financial services industry.

The Act is designed to establish a comprehensive framework for monitoring and regulating systemic risk. While the central focus of the Act is directed at regulating banks and non-bank financial institutions, it also includes provisions affecting the Securities and Exchange Commission (the "SEC") and numerous other areas of our country's economic life.

While many of the provisions of the Act took effect upon signing, implementation of numerous provisions is expected to take place over several months.

Some of the highlights of the Act are summarized below:

Creation of the Financial Stability Oversight Council

One of the most significant provisions in the Act creates the Financial Stability Oversight Council.

- This council will monitor sources of systemic risk and promulgate rules to be implemented by various financial regulators to address those risks.
- It will be chaired by the Treasury Secretary and made up of the heads of the most significant federal financial regulators.
- The Financial Stability Oversight Council will identify those companies deemed "too big to fail" with the Federal Reserve providing oversight of such companies.
- The Council can make recommendations to the Federal Reserve and other federal banking agencies for stricter supervision and requirement standards to be applied to the significant institutions on an individual basis or by category.

Financial Regulatory Agency Reform and New Capital Rules

While the Act does not completely overhaul the federal banking agency structure, it does provide the various federal agencies charged with supervising and regulating financial institutions with more authority over banks and non-bank financial firms.

- The FDIC will be empowered to act as a receiver and dissolve certain bank holding companies and non-bank financial companies.
- The Act also consolidates some of the existing federal banking agencies.
- The Federal Reserve will become subject to increased scrutiny with certain audit and disclosure obligations being imposed, as well as limitations on the Federal Reserve's emergency lending authority.
- The federal banking agencies will also issue new capital rules relating to minimum leverage and risk-based capital requirements for all insured depository institutions, depository institution holding companies and significant institutions.
- The Act contains new requirements for publicly-traded financial institutions, including requiring risk committees, to be comprised of independent directors and at least on "risk expert."
- The Act also phases in a requirement that bank holding companies and significant institutions exclude trust preferred securities from Tier I capital requirements.

Creation of the Consumer Financial Protection Bureau

The Act creates a semi-independent Consumer Financial Protection Bureau that will oversee regulation of providers of consumer financial products and services. The Act also amends various consumer laws, imposing new regulations on credit card companies and other providers of financial services.

- The Bureau will be within the Federal Reserve and will consolidate federal regulation of financial services to consumers.
- Credit providers, including mortgage lenders, banks, credit unions and other non bank financial companies with assets over $10 billion will be subject to new regulations, including disclosure and registration requirements.
- The Act provides that state consumer protection laws are

preempted if the state law prevents or significantly interferes with the exercise by a national bank of its powers or if it would have a discriminatory effect on the national banks.

- The Act provides consumers with significantly enhanced access to information regarding their accounts and related matters.
- The Act creates numerous new regulatory offices, including the Office of Fair Lending and Equal Opportunity, the Office for Financial Education, and the Office for Financial Protection of Older Americans.

Executive Compensation, Corporate Governance Provisions and Other Securities Regulations

These portions of the Act focus on ways to enhance corporate accountability to shareholders and investor protection overall as well as improve the transparency of decision making.

- The Act provides shareholders with a non binding vote (at least once every three years) on executive pay. In addition, companies are required to hold a vote of the shareholders once every six years to determine how often the non-binding vote must occur (every one, two or three years). Although this say-on-pay vote is not binding on the company it will put pressure on the Boards to consider shareholder viewpoints when determining executive compensation.
- In any proxy solicitation for the approval of a merger, acquisition, consolidation or disposition of all or substantially all of a company's assets, the company must provide clear disclosure of agreements with its named executive officers for compensation related to the transaction (so-called "golden parachutes") and must hold a separate non-binding vote to approve such agreements.
- Compensation committees for companies listed on an exchange may only include independent directors with a more stringent standard of independence. In addition, the compensation committee must have the authority to hire compensation consultants, to strengthen independence of the committee, but the Act establishes certain factors that must be considered in the selection and hiring process.
- The Act gives the SEC express discretionary authority to adopt rules and procedures relating to the inclusion of shareholder board nominees in a company's proxy solicitation materials. The SEC has the authority under the Act to mandate that shareholders be provided "proxy access".
- The SEC must direct national securities exchanges to prohibit member brokers from voting customer shares without first receiving voting instructions from the beneficial owner with respect to director elections, executive compensation and any other significant matter determined by the SEC.
- The Act requires the SEC to instruct the national securities exchanges to require each listed company to implement policies to clawback excess executive compensation for a period of three years if the compensation was based on inaccurate financial statements. Applies to all current and former executive officers, not just the CEO and CFO.
- Additional disclosures will be required regarding:

  (i) the relationship between compensation to named executives and stock performance and paid dividends;

  (ii) the ratio of CEO pay to the median pay of all other employees within the company; and

  (iii) whether any director or employee can hedge ownership of securities.
- The Act requires the SEC to investigate the state of short-selling and submit the study to Congress, as well as requiring more frequent disclosure of short positions and other reporting changes.
- The Federal Reserve will oversee executive compensation for financial institutions to ensure that it does not encourage excessive risk-taking and it will be provided with authority if payouts appear to promote risky business decisions to block the pay.
- Requires the federal financial regulators to issue and enforce compensation rules specifically applicable to financial institutions.
- The SEC will be required to prepare over 100 specified studies, enact new rules and create new offices, including the following:

  (i) clarify disclosures related to compensation including tables comparing executive compensation with stock performance over a five year period;

  (ii) adopt rules requiring companies to disclose in their proxy statements why they have combined or separated the role of CEO and Chairman;

  (iii) create an Office of Credit Rating Agencies with authority to fine agencies.
- The Act imposes a fiduciary duty on brokers who offer investment advice to consumers.
- The Act requires the SEC to create a whistleblower program to encourage people to report various violations (including under the securities laws, the Foreign Corrupt Practices Act, and other laws, rules, and regulations) with rewards of up to 30% of funds recovered.
- The SEC must create an Investor Advisory Committee to advise the SEC on its priorities and practices.
- Section 404(b) of the Sarbanes-Oxley Act of 2002 (the internal controls attestation provision) is amended to make permanent the exemption from compliance for non accelerated filers (less than $75 million in market capitalization).

This section had often been cited as the most expensive compliance provision under Sarbanes-Oxley.

- The SEC is charged with performing a study within nine months on how to reduce the burden of Section 404(b) compliance for companies with a market capitalization between $75 million and $250 million.
- Auditors of all broker dealers must register with the Public Company Accounting Oversight Board, just like the auditors of public companies have been required to do since the enactment of the Sarbanes-Oxley Act.

Private Equity Related Provisions

The Act contains many provisions relating to the private equity markets, including fund and adviser regulation.

- Private equity and hedge funds with assets of $150 million or more would be required to register with the SEC and will become subject to additional requirements under the Investment Advisers Act. The Act does create exemptions for venture capital advisers, foreign private advisers, advisers to SBIC's and family offices, but several current exemptions (including the "private adviser" exemption and the "intrastate adviser" exemption) are modified or eliminated.
- The Act also revisits the "accredited investor" standard for individuals contained in Regulation D, as promulgated under the Securities Act of 1933. The value of a person's or couple's primary residence now must be excluded from the calculation of the person's or couple's net worth in satisfying the accredited investor criteria. The SEC is also directed to increase the personal net worth criteria on the fourth anniversary of the Act from its current level of $1 million, and to review the criteria at least once every four years.

Derivatives

The Act attempts to resolve the perceived systemic risk and transparency deficiencies of the existing derivative market and provides more definitive oversight of swap dealers and major swap participants.

- Many derivatives will be subject to transparency and be required to be listed on an exchange.
- Banks will be permitted to continue to trade derivatives related to interest rates, foreign exchanges, gold and silver. Those that are deemed riskier may not be traded by banks but through affiliated companies with separate finances.
- The Act provides the SEC and CFTC with the authority to regulate over-the-counter derivatives.
- The Act requires central clearing and exchange trading for derivatives.
- The Act requires that swap dealers and major swap participants have adequate financial resources to meet responsibilities.
- In addition, the Act establishes a code of conduct for all registered swap dealers and major swap participants

Other

- Bank holding companies and their bank and non-bank subsidiaries will no longer be permitted to invest in, act as general partner of, or lend their name to hedge, private equity and other private investment funds. To permit bank holding companies and their subsidiaries to continue to manage and advise such funds, limited investments will be permitted up to 3% of the total investment in the fund.
- Bank holding companies and their bank and non-bank subsidiaries will no longer be able to engage in "proprietary trading."
- FDIC deposit insurance would be permanently raised to $250,000 per individual from $100,000.

Conclusion

It is important to note that the foregoing only provides a high level summary of certain significant provisions of the Act. The Act is exceedingly far-reaching, including provisions on such diverse topics as payday loan alternatives, private mortgage reform, "expertising" credit rating agencies in bond offerings and regulation of minerals from certain African countries. There is still substantial work to be done by a number of federal agencies in order to fully implement the provisions of the Act. We will continue to monitor the progress of the implementation of the Act.

Additional Information

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