

FINANCIAL REGULATORY REFORM UPDATE

From: Patton Boggs Financial Services Policy Group
Date: July 21, 2010
Subject: President Obama Signs Historic Dodd-Frank Wall Street Reform and Consumer Protection Act

Today, President Obama signed into law the “Dodd-Frank Wall Street Reform and Consumer Protection Act” (the “Dodd-Frank Act”). The House of Representatives and the Senate had approved the Conference Report of this legislation on June 30 and July 15, respectively.

This historic legislation is, however, merely the end of the first phase of the effort to modernize our financial regulatory system. The Dodd-Frank Act directs a number of Federal agencies, including the U.S. Securities and Exchange Commission (SEC), the Federal Reserve Board of Governors (Federal Reserve), the Commodity Futures Trading Commission (CFTC) and the Federal Trade Commission (FTC), to undertake significant rulemakings to effectuate the goals of the legislation.

Among a number of important provisions, the legislation establishes a new independent Consumer Financial Protection Bureau within the Federal Reserve to regulate the mortgage industry, credit cards and other financial products; creates a new Financial Stability Oversight Council to identify and address systemic risks posed by large, complex companies, products and activities before they threaten the stability of the economy; and establishes new regulations for the over-the-counter derivatives markets.

Unlike typical rulemakings where the agency initiates the process and acts with a greater degree of autonomy, the Dodd-Frank Act specifically directs a number of agency rulemakings that Congress will continue to monitor throughout the rulemaking process. Interested stakeholders should view this as the opportune time to engage regulators and participate in the process that will produce these new rules and regulations.

The Patton Boggs Financial Services Policy Group will continue to monitor implementation of this historic legislation for the latest developments and welcomes the opportunity to assist clients in not only understanding but impacting the often confusing U.S. federal agency rulemaking process.

Key Elements of the Dodd-Frank Act

The following is a summary of selected key provisions of the legislation, including (1) the Financial Stability Oversight Council; (2) a new orderly liquidation mechanism; (3) changes in bank regulatory structure; (4) regulation of investment advisers to private funds; (5) regulation of the insurance industry; (6) prohibitions on proprietary trading and certain relationships with hedge funds and private equity funds; (7) over-the-counter derivatives markets; (8) a possible new fiduciary standard for investment advisers to retail customers; (9) credit rating agencies; (10) the Consumer Financial Protection Bureau; (11) changes to the Federal Reserve System; (12) mortgage reform; (13) the Financial Crisis Assessment Fund; and (14) executive compensation.

1. Financial Stability Oversight Council

The Dodd-Frank Act establishes a Financial Stability Oversight Council (FSOC) to identify, monitor and address systemic risks posed by large, complex financial firms as well as products and activities that spread risk across firms. The FSOC is authorized to make recommendations to the Federal Reserve for increasingly stringent rules regarding capital, leverage, liquidity, risk management and other requirements on companies that pose a systemic threat to the financial stability of the United States.

Membership. The FSOC will be comprised of nine federal financial regulators, one independent member and five nonvoting members. Agencies included on the FSOC are: (1) the Treasury (the Secretary of the Treasury will serve as Chairperson of the Council); (2) the Federal Reserve Board, (3) the Comptroller of the Currency; (4) the new Consumer Financial Protection Bureau (CFPB); (5) the SEC; (6) the CFTC; (7) the Federal Housing Finance Agency (FHFA); (8) the Federal Deposit Insurance Corporation (FDIC); (9) National Credit Union Administration (NCUA); and (10) an independent member appointed by the President, with the advice and consent of the Senate. The non-voting members will include the Office of Financial Research; the Federal Insurance Office (FIO); and state banking, insurance and securities regulators.

Authority. The bill grants the FSOC the authority to, among other things, mitigate against systemic risk by: (1) making recommendations to the Federal Reserve to write increasingly strict rules for capital requirements, leverage limits, liquidity requirements, risk management and other requirements as companies grow in size and complexity to prevent companies from becoming “too big to fail”; (2) identifying and monitoring emerging risks to the economy through the Office of Financial Research (to be established within the Treasury) and making periodic reports and testimony to Congress; (3) approving by a 2/3 vote a Federal Reserve decision to divest some of a financial company’s holdings “as a last resort” if the company poses a grave threat to the financial stability of the United States; (4) authorizing by a 2/3 vote a requirement that unregulated nonbank financial companies that pose systemic risks to the financial stability of the United States be regulated by the Federal Reserve; (5) ensuring that the Federal Reserve establishes a floor for capital holdings that cannot be lowered below the standards in effect today; and (6) identifying systemically important nonbank financial companies to be regulated by the Federal Reserve. The Office of Financial Research includes a newly-created Office of Financial Research Data Center tasked with collecting, validating and maintaining data from member agencies, commercial data providers,

publicly available data sources, and financial entities in order to assess the extent to which a financial activity, financial market, or the financial company poses a threat to the financial stability of the United States.

Office of Financial Research. The Dodd-Frank Act creates an Office of Financial Research (OFR) within the Treasury Department. The Research and Analysis Center, as part of the OFR, is required to develop and maintain independent analytical capabilities to promote best practices for financial risk management, monitor, and report on changes in system-wide risk and evaluate and report on stress tests. The OFR's primary goal is to collect and standardize data on financial firms and their activities to aid and support the work of the federal financial regulators to measure and monitor financial systemic risk. The OFR has independent authority to issue regulations and collect reports, data and information without approval from the Council. Further, it is required to issue, and FSOC-member agencies are required to implement, regulations that standardize the scope and format of data collected by Council-member agencies.

Trust Preferred Securities, Tier 1 Capital. Section 171 of the Dodd-Frank Act restricts the ability of banks to apply trust preferred securities towards the regulatory capital requirements. This provision permits small bank holding companies to continue to issue trust preferred securities and have them count as Tier 1 capital. This requirement is less onerous than proposals offered by Senator Susan Collins (R-ME) during Senate consideration of the bill because it grandfathers Tier 1 capital treatment for trust preferred securities issued before May 19, 2010 for bank holding companies with less than \$15 billion in consolidated assets as of December 31, 2009, as well as organizations that were mutual holding companies on May 19, 2010. The legislation also allows savings and loan holding companies with less than \$15 billion in consolidated assets as of December 31, 2009 to include trust preferred securities issued before May 19, 2010 as Tier 1 capital, once such savings and loan holding companies become subject to consolidated capital requirements. To soften the impact of this provision, the elimination of trust preferred securities as an element of Tier 1 capital will be implemented over an extended period of time.

2. Orderly Liquidation Authority

The Dodd-Frank Act creates a new orderly liquidation mechanism for the FDIC to unwind failing systemically significant financial companies. Under the mechanism, shareholders and unsecured creditors would bear the losses (not taxpayers), and management and responsible directors would be removed from office. The bill provides that the FDIC, Treasury, and Federal Reserve must agree to place a company into the liquidation process, with an up front judicial review. The bill further specifies that the resolution process is meant for emergencies only and that most large financial companies will be resolved through the bankruptcy process. Under these provisions, the FDIC can guarantee debt of insolvent insured banks through Presidential and Congressional approval only after a 2/3 majority of the Federal Reserve Board and the FDIC board determine there is a serious threat to financial stability; and an approval by the Treasury Secretary as to a cap on overall guarantee amounts and the terms and conditions of the guarantee.

Determination for Orderly Liquidation. The bill requires written recommendations to be issued which include: (1) an evaluation of whether the financial company is in default or in danger of default; (2) a description of the effect that the default of the financial company would have on financial stability in the United States; (3) a description of the effect that the default of the financial company would have on low income, minority, or underserved communities; (4) a recommendation regarding the nature and the extent of actions to be taken regarding the financial company; (5) an evaluation of the likelihood of a private sector alternative to prevent the default of the financial company; (6) an evaluation of why a case under the Bankruptcy Code is not appropriate for the financial company; and (7) an evaluation of the effects on creditors, counterparties, and shareholders of the financial company and other market participants.

Receivership Appointment Process. When an institution is failing, the Treasury Secretary has the ultimate authority to recommend that the FDIC be appointed as receiver. If the board of directors for the failing financial company does not consent to the FDIC receivership appointment, the Treasury Secretary shall then petition the United States District Court for the District of Columbia for an order authorizing the appointment. The district court then must evaluate the Secretary's determination under an arbitrary and capricious standard. If the court fails to render a decision within 24 hours, the petition shall be granted by operation of law and the Secretary shall appoint the FDIC as receiver. The Treasury Secretary must submit written notice of the recommendations and determinations reached by the Treasury Department to Congress within 24 hours of the date of appointment of the FDIC as receiver.

Orderly Liquidation of Covered Brokers and Dealers. The bill provides that the Securities Investor Protection Corporation (SIPC) be appointed as trustee of a covered broker/dealer. However, the bill clarifies that the FDIC would retain its power to perform various functions (without being impeded by the SIPC), including the FDIC's ability to: (1) make funds available, (2) organize, establish, operate, or terminate any bridge financial company; (3) transfer assets and liabilities; (4) enforce or repudiate contracts; or (5) take any other action relating to such bridge financial company.

Funeral Plans. The bill requires large, systemically significant companies to submit plans for a rapid and orderly shutdown in the event that the company becomes insolvent. As an incentive to provide these plans, the government will impose higher capital requirements, divestments, and restrictions on growth on companies that fail to submit acceptable plans. The funeral plans are intended to assist regulators in understanding the structure of the companies they oversee and to provide a roadmap for shutting them down if the company fails.

Cost of Liquidating Financial Companies. The Dodd-Frank Act limits the amount of money that the FDIC is permitted to borrow for purposes of liquidation as well as what the FDIC may reasonably expect to be repaid from the liquidation of a company's assets. The government will automatically be first in line for repayment during a liquidation event. If any proceeds exist following the sale of a company's assets, the remaining funds would be repaid, through a claw back mechanism, first to creditors whose claims exceed liquidation value, and then secondly as an assessment fee on large financial companies. A risk matrix will decide the portion to be paid by each financial company to ensure the riskiest pay more.

Federal Reserve Emergency Lending. The bill significantly alters the Federal Reserve's authority to lend under the emergency lending authority of Section 13(3) of the Federal Reserve Act. The Federal Reserve would be prohibited from bailing out individual companies. Additionally, the Secretary of the Treasury must approve any lending program and companies seeking assistance must offer sufficient collateral to offset the loan amount, a safeguard designed to protect taxpayers from potential loss in such a lending program.

3. Changes to Bank Regulatory Structure

The Dodd-Frank Act merges the Office of Thrift Supervision (OTS) into the Office of the Comptroller of Currency (OCC) within 18 months of enactment and designates certain lines of responsibility to reduce regulatory arbitrage, including:

Federal Reserve. The bill provides that the Federal Reserve will in light of its capital markets supervisory experience, regulate bank and thrift holding companies with assets over \$50 billion. The Vice Chairman for Supervision will be responsible for supervising and regulating depository institution holding companies and other financial firms supervised by the Board. In addition, the Vice Chairman for Supervision is required to report semi-annually to Congress on the efforts of the Board of the Federal Reserve.

FDIC. The bill provides that the FDIC would regulate state banks and thrifts, regardless of size, as well as bank holding companies of state banks with assets below \$50 billion.

OCC. The bill merges the OTS into the OCC, which would regulate national banks and federal thrifts of all sizes and the holding companies of national banks and federal thrifts with assets below \$50 billion.

Dual Banking System. The bill preserves the dual banking system, leaving in place the state banking system that governs community banks.

4. Regulation of Investment Advisers to Private Funds

Limitations on Certain Exemptions. Title IV of the Dodd-Frank Act, the "Private Fund Investment Advisers Registration Act of 2010" (PFIAR Act) eliminates the private fund adviser exemption contained in Section 203(b) of the Investment Advisers Act of 1940 (Advisers Act). The exemption registration with the SEC for "private fund"¹ investment advisers will no longer be available.

¹ The PFIAR Act defines a "private fund" as a fund that would be an "investment company" under the Investment Company Act of 1940 (Investment Company Act) but for the exceptions to that definition under Sections 3(c)(1) and 3(c)(7) of the Investment Company Act. This definition includes all such funds wherever organized or located, whether in the U.S. or in off-shore jurisdictions.

The PFIAR Act retains the foreign private fund adviser exemption already contained in the Advisers Act, but defines the term “foreign private fund adviser” as an investment adviser who has: (1) no place business in the U.S.; (2) fewer than 15 clients and investors in the U.S.; (3) aggregate assets under management attributable to clients and investors in the U.S. of less than \$25 million (or such higher amount as determined by the SEC); and (4) does not hold itself out to the public in the U.S. as an investment adviser, nor acts as an investment adviser to a registered investment company or a business development company.

Collection of Data. The PFIAR Act requires the collection of certain types of data from registered investment advisers and their managed funds, and provides that any records of funds managed by such advisers will be considered to be the adviser’s records, as well, for reporting purposes. The specific information that required to be maintained and subject to periodic and special inspection by the SEC includes: (1) amount of assets under management and use of leverage, including off-balance sheet leverage; (2) counterparty credit risk exposure; (3) trading and investing positions; (4) valuation policies and practices of the underlying funds; (5) the types of assets the funds hold; (6) side arrangements or side letters with investors; (7) trading practices; and (8) other information deemed relevant, which may include the establishment of different classes of fund advisers, with different reporting requirements, based on size or type of fund being advised. This list of items will greatly expand the reportable information that registered investment advisers are currently obligated to report and may, in certain respects, be greeted with some resistance by participants in the private fund community (e.g., investing positions, side letters, trading practices).

Loosening Prohibition Against Disclosure. The PFIAR Act broadens the scope of exceptions to Section 210(c) of the Advisers Act, which in its current form severely limits the SEC’s ability to require a registered investment adviser to disclose the identity, investments or business affairs of its clients. This increased disclosure will be achieved by allowing disclosure for the assessment of potential systemic risk and permitting the SEC to create rules and regulations to define terms used in the PFIAR, such as “venture capital fund” and “client.”

Non-Disclosure of Proprietary Information and Confidentiality. To address concerns regarding this expanded authority to collect data, the PFIAR Act also provides that any proprietary information of a registered investment adviser gathered in required filings will be subject to the same limitations on public disclosure as any facts collected during an exam by the SEC. Registered advisers will be subject to periodic and special examinations of their books and records by the SEC, which will be required to provide data to the FSOC that is necessary for assessing systemic risk posed by a private fund. However, the information filed with the SEC will be kept confidential except for required disclosures to Congress when accompanied by the proper confidentiality agreement. Disclosure to other appropriate bodies, such as other federal departments or agencies, potential self-regulatory organizations, or pursuant to a Federal court order, will also be required. “Proprietary information” is defined to include sensitive, non-public information concerning the investment adviser’s investment or trading strategies, analytical or research methodologies, trading data, computer hardware or software containing intellectual property, and any additional information the SEC determines to be proprietary.

Exemption for Advisers Registered with the CFTC. The PFIAR Act exempts investment advisers registered with the CFTC as commodity trading advisers and that advise private funds from registering and reporting under the Advisers Act. However, if after the enactment of the Investor Protection and Securities Reform Act of 2010 the adviser's business becomes predominately providing securities-related advice, then dual registration with the SEC will be required.

Exemption for Advisers to Small Business Investment Companies. The PFIAR Act exempts from registration and reporting advisers (who are not business development companies) who solely advise small business investment companies (SBICs), entities that have received notice that they qualify as an SBIC, or affiliated entities of SBICs that have a pending application for an SBIC license.

Exemption for Advisers to Venture Capital Funds. The PFIAR Act also exempts from registration and reporting requirements advisers who solely advise one or more "venture capital funds," but only to the extent they provide investment advice to venture capital funds. The SEC is tasked with defining the term "venture capital fund" within one year of enactment of the PFIAR Act.

Exemption for Private Equity Fund Advisers. Under the PFIAR Act, there are no separate exemptions for advisers to private equity funds.

Exemption for Family Offices. The PFIAR Act also excludes advisers to "family offices" from the definition of "investment advisers" under the Advisers Act, and thus, exempts them from required registration with the SEC. The SEC is obligated to formulate rules that define "family office" and capture the SEC's previous exemptive policy regarding family offices, no matter how structured or arranged. The PFIAR Act also requires that the SEC exemptive rules not exclude persons who were either not registered before January 1, 2010 or should have been registered on that date, and who solely provide investment advice (and was engaged prior to January 1, 2010) to certain "accredited investor" officers, directors, employees of the family office; companies owned exclusively and controlled by the family or family office; and registered investment advisers providing advice on funds in which they also invest, in a limited manner, to the family office.

Exemption for Advisers with Less Than \$150 Million Assets Under Management. The PFIAR Act would exempt from registration requirements, but not reporting requirements, advisers who solely advise private funds and have less than \$150 million in assets under management in the U.S. In carrying out the registration and reporting requirements for these mid-sized private fund advisers, the SEC is be obligated to take into account the size, governance and investment strategy of the private funds being advised and systemic risk issues, and then would create procedures reflecting these factors.

Increased Threshold for Assets Under Management for State Registration. The PFIAR Act also increases the assets under management threshold, below which all investment advisers are generally required to register with state regulators rather than the SEC. The threshold is increased from \$25 million to \$100 million (or such higher amount as may be determined by the SEC). However, if this requires registration with 15 or more states, then the subject adviser can register at the SEC instead. As discussed in the prior paragraph, however, an investment adviser who solely advises private funds would benefit from the higher threshold of \$150 million before being required to register with the SEC.

Clarification of Rulemaking Authority. The PFIAR Act clarifies the SEC's rulemaking authority, and permits the SEC to issue, amend and rescind rules and regulations defining technical, trade and other terms used in the PFIAR Act. However, the SEC may not define "client" for certain purposes, to include an investor in a private fund managed by the adviser if the fund has entered into an advisory contract with the adviser. In addition, the PFIAR Act provides the SEC and CFTC with 12 months to draft registration rules for dually-registered investment advisers.

Comptroller General Studies and SEC Study. The Comptroller General of the U.S. is directed to perform several studies following enactment of the PFIAR Act: (1) within three years after enactment of the PFIAR Act, (a) the compliance costs for investment advisers to comply with current SEC rules concerning the custody of clients' funds or securities; (b) the costs of rules regarding operational independence, if eliminated; and (c) the appropriate thresholds for "accredited investor" status and eligibility to invest in private funds; and (2) within one year after the date of enactment, whether a self-regulatory private fund body could work. The SEC is directed to perform a study within two years on the state of short selling including the effect of the newer short sale rules and subsequent trading behaviors. The SEC must also perform a study within one year on the feasibility of requiring real-time public reporting of short sale positions of publicly listed securities. The PFIAR Act would require the SEC to report to Congress annually as to how it has used the data it has collected from private funds and their advisers to monitor the markets and protect investors.

Miscellaneous. The PFIAR Act permits the SEC to promulgate rules requiring advisers to take steps to safeguard clients' assets over which the adviser has custody. It also requires the SEC to increase the standard for natural persons to achieve "accredited investor" status at least once every four years to reflect the percentage increase in the cost of living. Similarly, the PFIAR Act requires the SEC to adjust for inflation every five years any dollar amounts used in connection with qualified client standards. Finally, the PFIAR Act goes into effect on the one-year anniversary of its enactment, although investment advisers may register with the SEC prior to such date pursuant to rules and regulations prescribed by the SEC.

5. Regulation of the Insurance Industry

Creation of a New Federal Insurance Office in Treasury. Title V of the Dodd-Frank Act creates the Federal Insurance Office (FIO) as a new office within the Treasury Department to monitor all aspects of the insurance industry (e.g., access to affordable insurance by various population demographics) and to identify issues or gaps in regulation of insurers that could contribute to systemic risk, among other information-gathering authorities articulated in the Dodd-Frank Act.

Study on Modernizing Insurance Regulation. The Dodd-Frank Act requires the FIO to conduct a study and submit a report to Congress, within 18 months of enactment of the legislation, on ways to modernize the system for regulating insurance companies. The study shall take into consideration, among other things, systemic risk regulation, capital standards and the relationship between capital allocations and liabilities, consumer protection and gaps between states, the degree of national uniformity of state insurance regulation, the regulation of insurance companies and affiliates on a consolidated basis, and international coordination of insurance regulation.

Systemic Risk. The Dodd-Frank Act provides that the Director of the FIO shall act in an advisory capacity to the FSOC. Further, the FIO shall consider systemic risk regulation with respect to insurance in its required study to be submitted to Congress.

Relation to State Law. The Dodd-Frank Act preserves the authority of state regulators to regulate the insurance industry. Further, the legislation provides for very limited preemption. FIO has authority to preempt state insurance regulations to the extent that: (1) the measure results in less favorable treatment of a non-United States insurer domiciled in a foreign jurisdiction that is subject to a covered agreement than a United States insurer domiciled, licensed, or otherwise admitted in that State; and (2) the measure is inconsistent with a covered agreement. The bill discusses a procedure for publishing such decisions in the Federal Register and provides for public comment.

Role in International Negotiations. The Dodd-Frank Act directs the FIO to serve as a national voice in coordinating policy on prudential aspects of international insurance matters, including representing the United States, as appropriate, in the International Association of Insurance Supervisors, among other international forums of negotiation. The FIO must consult with four congressional committees; the Treasury Department may be required to defend agreements in court. Further, the Treasury and the U.S. Trade Representatives Office would share negotiating authority.

Streamlined Regulation of Surplus Lines of Insurance. The Dodd-Frank Act streamlines the regulation of surplus lines insurance and reinsurance through state-based reforms. This provision would specify that in multistate placement of surplus lines, the state whose rules (e.g., due diligent search requirements, premium tax allocations, eligibility standards) that govern access to the products would be the “home state” (e.g., the principal place of business of the insured). Further, the bill provides that no state other than the insured’s home state may require a surplus lines broker to be licensed in order to sell, solicit, or negotiate non-admitted insurance with respect to the insured.

Effective Date. The insurance title takes effect 12 months after the date of the enactment of the bill.

6. Prohibitions on Proprietary Trading and Certain Relationships with Hedge Funds and Private Equity Funds (“Volcker Rule”)

The Dodd-Frank Act contains a modified version of the Obama Administration’s so-called “Volcker Rule,” which, as discussed in further detail below, prohibits banks, bank affiliates and bank holding companies from engaging in proprietary trading² and requires nonbank financial companies under the supervision of the Federal Reserve engaging in proprietary trading to meet additional capital requirements and quantitative limits. The “Volcker Rule” would also prevent banks and nonbank financial companies under the supervision of the Federal Reserve from sponsoring or investing in a hedge fund or private equity fund with more than a de minimis interest.

Permitted Activities. The proprietary trading ban is not absolute. Permitted activities that fall outside the prohibition include: (1) the disposition of U.S. government, state, municipal, and Fannie and Freddie Mac obligations, (2) the disposition of any security or other interest in connection with underwriting, market making-related activities (to the extent that these transactions are not designed to exceed near-term client demands) conducted on behalf of customers, or by a regulated insurance company directly engaged in the business of insurance for the general account of the company, and (3) risk mitigating hedging activities intended to reduce risk for a banking entity, small business investments, and certain “public welfare” investments, along with any other such activity that the appropriate regulator determines would promote and protect the safety and soundness of the U.S. financial system.

Study. The Dodd-Frank Act requires the FSOC to conduct a six month study to review the benefits and problems of various aspects of such a rule and its implementation. After reviewing the study’s findings, the appropriate Federal banking agencies and regulators will jointly create and adopt appropriate rules to carry out the legislation.

General Prohibition and Effective Date. Except to the extent permitted by the new law, a “banking entity”³ may not acquire or retain any equity, partnership, or other ownership interest in or sponsor a hedge fund or private equity fund. For this purpose, the terms “hedge fund” and “private

² When used with respect to a banking entity or nonbank financial company supervised by the Board of Governors, proprietary trading means engaging as a principal for the trading account of the banking entity or nonbank financial company supervised by the Board of Governors in any transaction to purchase or sell, or otherwise acquire or dispose of, any security, any derivative, any contract of sale of a commodity for future delivery, any option on any such security, derivative, or contract, or any other security or financial instrument that the appropriate Federal banking agencies, the Securities and Exchange Commission, and the Commodity Futures Trading Commission may, by rule, determine.

³ In addition to banking entities (i.e., depository institutions and certain of their affiliates), the Volcker Rule would also be applicable to non-bank financial companies that are supervised by the Federal Reserve Board. This category presumably is intended to cover non-bank financial companies that are determined to be systemically significant under other provisions of the legislation and thus subject to enhanced regulation and supervision.

equity fund” are defined to include any issuer that would be an investment company, as defined in the Investment Company Act, but for the application of the exceptions contained in sections 3(c)(1) and (7) of that Act (hereafter a “Covered Fund”). The definition of Covered Funds also includes such similar funds as the relevant federal regulatory agencies may designate.

The legislative prohibition would generally take effect on the earlier of (a) 12 months after date on which final implementing regulations are issued by the relevant federal regulatory agencies, or (b) two years after the date of enactment of the legislation. Transitional periods would be provided to enable banking entities to make divestitures as necessary to comply with the new restrictions (generally two years with three possible one-year extensions by the Federal Reserve) and special transition periods apply to illiquid funds (by application to the Federal Reserve, although no specific time periods are enumerated).

Permitted Fund Activities. Subject to certain conditions (described below), a banking entity will be permitted to organize and offer a Covered Fund, including serving as a general partner, managing member, or trustee of the Covered Fund and select or control a majority of the directors, trustees or management of the Covered Fund (including having employees, officers, directors, or agents who constitute that majority).

This exception applies only if (a) the banking entity provides bona fide trust, fiduciary, or investment advisory services; (b) the Covered Fund is organized in connection with the provision of such services and is offered only to persons who are customers of such services; (c) with certain exceptions described below, the banking entity does not acquire or retain more than a de minimis investment in the Covered Fund; (d) the banking entity does not directly or indirectly guarantee, assume or otherwise insure the obligations of the Covered Fund or of any fund in which the Covered Fund invests; (e) the banking entity does not share with the Covered Fund for corporate, marketing, promotional, or other purposes, the same name or a variation of the same name; (f) no director or employee of the banking entity takes or retains an equity interest in the Covered Fund except for directors or employees who are directly engaged in providing investment advisory or other services to the Covered Fund; and (g) the banking entity makes adequate disclosures that any losses sustained by the Covered fund will be borne solely by investors in the Covered Fund (collectively, the “Sponsor Requirements”).

A banking entity is also permitted to invest in SBICs and investments designed to promote the public welfare. This permitted activity is not subject to the same limitations on investing in hedge funds or private equity funds.

In addition, otherwise permitted activities with respect to Covered Funds and SBICs will become prohibited activities if they involve or result in a material conflict of interest between a banking entity and its clients, customers or counterparties; an unsafe or unsound exposure of the banking entity to high risk assets or high risk trading strategies; a threat to the safety and soundness of the banking entity; or a threat to the financial stability of the U.S.

Capital and Quantitative Limitations – 3 Percent Rules. Subject to certain limitations (described below), a banking entity may make and retain an investment in a Covered Fund that it organizes and offers for the purposes of either (a) establishing the Covered Fund and providing the fund with sufficient initial equity for investment to permit the fund to attract unaffiliated investors or (b) making a de minimis investment in the Covered Fund.

The banking entity must actively seek unaffiliated investors to reduce or dilute its investment in the Covered Fund to a de minimis amount. In addition, investments in a Covered Fund must (a) be reduced to 3 percent of the total ownership interests of the fund not later than one year after the Covered Fund is established and (b) be immaterial to the banking entity, but in no case may the aggregate of all interests of the banking entity in all Covered Funds exceed 3 percent of the tangible common equity of the banking entity. The relevant federal regulatory agency may extend the time for meeting the percentage of fund ownership requirement for two additional years.

Limitation on Relationships with Covered Funds. No banking entity that serves, directly or indirectly, as the investment manager, investment adviser, or sponsor to a Covered Fund, or that organizes and offers a Covered Fund, and no affiliate of the banking entity may enter into transactions with the Covered Fund, or funds controlled by the Covered Fund, that would be prohibited under section 23A of the Federal Reserve Act. Similar rules are provided so that the provisions of section 23B of the Federal Reserve Act would also apply.

Notwithstanding these limitations, the relevant federal regulators may permit a banking entity to enter into prime brokerage transactions with a Covered Fund if the following additional conditions are met: (i) the banking entity is in compliance with each of the Sponsor Requirements (described above) regarding a hedge fund or private equity fund organized and offered by such banking entity; (ii) the banking entity provides an enforceable undertaking that such transaction will not be used under any circumstance to avoid losses to any investor in any such fund; and (iii) the Federal Reserve has determined that such transaction is consistent with the safe and sound operation and condition of the banking entity.

7. Regulation of Over-the-Counter Derivatives Markets

The Dodd-Frank Act seeks to bring greater regulation and transparency to OTC derivatives markets by, among other things, granting greater authority to the CFTC and the SEC to oversee swaps and security-based swaps, OTC market participants and market activity. The legislation is designed to increase the regulatory burden upon dealers in swaps (and security-based swaps) and those who maintain a substantial net position in outstanding swaps (or security-based swaps) by imposing capital and margin requirements to participate in the OTC derivatives markets.

Mandatory Clearing. The bill seeks to improve regulatory oversight by imposing a requirement that standardized derivatives (as determined by the CFTC or SEC) be cleared through central clearinghouses. Further, uncleared swaps will be subject to margin and collateral requirements in order to offset the risk they pose. The Dodd-Frank Act also makes clear that derivatives clearinghouses must provide for non-discriminatory clearing of a swap (or security-based swap) (but not a contract of sale of a commodity for future delivery or option on such contract)

executed bilaterally or on or through the rules of an unaffiliated designated contract market or swap execution facility.

Mandatory Execution. The legislation also requires that clearable trades be executed on a board of trade designated as a contract market or on a swap execution facility, which is defined as a facility trading system or platform in which multiple participants have the ability to execute or trade swaps by accepting bids and offers made by other participants that are open to multiple participants in the facility or system, through any means of interstate commerce, including any trading facility, that facilitates the execution of swaps between persons and is not a designated contract market.

End User Exemption. There exists an exemption from the clearing and execution requirements for trades where one counterparty (i) is not a financial entity; (ii) is using swaps to hedge or mitigate commercial risk; and (iii) notifies the relevant regulator how it meets its obligations associated with the swap. “Financial entities” are not exempt from the clearing requirement, and the legislation indicates that the term includes swap dealers, major swap participants, commodity pool operators, a private fund under the Investment Advisers Act, an employee benefit plan, or an entity predominantly engaged in activities related to banking or that is financial in nature. The legislation permits regulators to consider further extending the exemption to small banks, savings associations, farm credit system institutions, and credit unions, including those with less than \$10 billion of total assets.

Major Swap Participants. The Dodd-Frank Act establishes a new entity called a major swap participant.⁴ Those entities deemed to be substantially involved in swaps activity will be classified as major swap participants, and, along with swap dealers, will be required to register with the CFTC (or the SEC, for major security-based swap participants). The CFTC will define what constitutes a ‘substantial position,’ which will be the threshold that the Commission determines to be prudent for the effective monitoring, management, and oversight of entities that are systemically important or that can significantly impact the financial system of the United States. Additionally, major swap participants and swap dealers must meet periodic reporting requirements, minimum capital requirements, minimum initial and variation margin requirements (which, in certain instances, may include noncash collateral) and business conduct standards.

Trade Reporting to Swap Data Repository. Additional transparency will be created by requiring that prescribed trade information for all swaps – both cleared and uncleared – must be reported to a registered swap repository. The repository, as recipient of the trade information, must meet certain specific duties and will be tasked with providing data to the regulatory agencies to minimize systemic risk and to publish certain aggregate market information to the public.

⁴ A major swap participant is any person who is not a swap dealer, and (i) maintains a substantial position in swaps for any of the major swap categories (as determined by the Commission), excluding (I) positions held for hedging or mitigating commercial risk; and (II) positions maintained by any employee benefit plan (or any contract held by such a plan) as defined in the Employee Retirement Income Security Act of 1974 for the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan; (ii) whose outstanding swaps create substantial counterparty exposure that could have serious adverse effects on the financial stability of the United States banking system or financial markets; or (iii)(I) is a financial entity that is highly leveraged relative to the amount of capital it holds and that is not subject to capital requirements established by an appropriate Federal banking agency; and (II) maintains a substantial position in outstanding swaps in any major swap category as determined by the Commission.

Clearing Requirement – Transition Rules. Notably, the conference committee added a provision to the legislation which grandfathers all swaps entered into prior to enactment from the mandatory clearing requirements if the trade information is reported to a registered swap data repository. This important change will mean that the holders of previously executed swaps can avoid the clearing requirement (and associated costs) for trades on their books by providing the trade information to the swap data repository. The result is that regulators are able to collect the needed trade information for systemic risk oversight without unduly burdening swap participants.

Swaps Entities' Access to Federal Assistance. The Dodd-Frank Act prohibits the provision of Federal assistance, including any advances from any Federal Reserve credit facility or discount window not part of a program or facility with broad based eligibility, to some swaps dealers and major swaps participants. These “swaps entities” exclude non-swap dealer depository institutions (though swap dealer depository institutions qualify if they limit activity to legitimate hedging purposes and only certain, less risky swaps) and systemically significant financial institutions subject to oversight by the Federal Reserve under conservatorship, receivership or resolution. These provisions become effective two years after the date of enactment but provide an additional two year transition period for insured depository institution. The purpose of this new regulation is to cause depository institutions engaged in derivatives activity to rely less on Federal assistance, or otherwise cause depository institutions to move derivatives trading desks into non-bank affiliates or divest from these activities.

Lynch Amendment. The final legislation did not adopt the House-proposed “Lynch Amendment”, which would have incorporated ownership restrictions on clearinghouses. Instead, the Dodd-Frank Act requires the CFTC to adopt rules within 180 days of enactment which limit (through numerical limits or voting rights) control of a clearinghouse, swap execution facility or board of trade by a bank holding company with total consolidated assets of \$50 billion or its affiliates, a systemically significant nonbank financial company or its affiliates, a swap dealer, major swap participant, or associated person of a swap dealer or major swap participant. The CFTC must only adopt rules if it determines that such rules are necessary or appropriate to improve the governance of, or to mitigate systemic risk, promote competition, or mitigate conflicts of interest. In making that determination, the CFTC is directed to consider conflicts of interest arising from the amount of equity owned by a single investor, the ability to control the vote entitled to be cast by the holders of the ownership interest, and the existing governance arrangements.

8. SEC Study of Fiduciary Standard for Investment Advisers

Section 913 of the Dodd-Frank Act requires the SEC to study the current legal and regulatory rules that apply to advisers providing personalized securities investment advice and recommendations to retail customers. The SEC must report the results of its study to Congress within the 6 month period following the enactment of the Dodd-Frank Act. The SEC is authorized to promulgate rules to address the standard of care that applies to those persons providing personalized investment advice, taking into account the results of its study, and may also provide rules that establish a fiduciary standard of care for brokers and dealers.

9. Regulation of Credit Rating Agencies

The Dodd-Frank act also includes a new regulatory regime for credit rating agencies (CRA). Among other things, this new regime is designed to increase transparency, accountability and oversight of CRAs. The linchpin of this new regulatory scheme will be the newly established Office of Credit Rating Agencies housed within the SEC. Once the SEC adopts rules, this office will have broad authority to regulate, oversee and discipline credit rating agencies.

Key aspects of the new legislation include: (1) requiring CRAs to demonstrate that they have adequate financial and managerial resources to consistently produce credit ratings with integrity. Failure to do so can lead to enforcement action by the SEC; (2) increasing transparency regarding how credit ratings are determined. CRAs will be required to issue, with each credit rating that it provides, a report disclosing their methodologies, including assumptions underlying the credit rating, the data relied upon in the analysis, any use of servicer or remittance reports, and any other information that can assist users in analyzing the credit rating, as well as requiring the CRA to reveal when it has relied upon diligence review services performed by a third party; (3) requiring CRAs to notify the users of the credit ratings of any material change in their procedure or methodology, or errors made in the formulation of credit ratings, as well as ensuring that changes to methodology are applied consistently to all credit ratings; (4) requiring that at least one-half of CRA boards be independent; and (5) minimizing potential conflicts of interest by prohibiting CRA compliance officers from working on the formulation of credit rating or methodologies.

Notably, the legislation also includes a provision granting a private right of action to an investor if a CRA knowingly or recklessly fails to investigate the quality of data provided to it or to obtain analysis of the information from a neutral, independent source. The SEC will have the authority to de-register an agency that has provided bad ratings over a given period of time.

10. Bureau of Consumer Financial Protection

The Dodd-Frank Act establishes an independent Consumer Financial Protection Bureau (CFPB) as a consumer watchdog. Housed within the Federal Reserve, the CFPB will regulate all consumer financial products and participants, including mortgages, credit cards, banks, payday loans and other financial products. The CFPB will be led by an independent Director appointed by the President and confirmed by the Senate for a five year term. The bill directs that the CFPB's budget will equal 10-12 percent (estimated at about \$550 million) of the Federal Reserve's budget but the Federal Reserve will have no authority to alter the budget or direct the manner in which the money is allocated by the CFPB. The Director may not hold any office, position, or employment in any Federal Reserve Bank, Federal Home Loan Bank, or covered entity while serving as Director.

Consolidation of Regulation. The CFPB will act as the consolidated regulator of consumer financial protection and assume certain functions currently handled by the OCC, OTS, FDIC, Federal Reserve, NCUA, the Department of Housing and Urban Development (HUD) and the FTC. The CFPB will also be responsible for enforcing various other federal laws intended to ensure fair, equitable, and nondiscriminatory access to credit for both individuals and communities.

Primary Role. The primary functions of the CFPB will be to: (1) promulgate rules, orders and guidance governing all financial institutions, including nonbanks, that offer consumer financial services and products, as well as the persons employed by these entities; (2) conduct examinations and enforce regulations for banks and credit unions with assets of over \$10 billion and all mortgage-related businesses, payday lenders, and student lenders as well as other large nonbank financial companies, such as debt collectors and consumer reporting agencies; (3) monitor the markets for consumer financial products and services to ensure that consumers are protected from abusive products; (4) conduct financial education programs; and (5) respond to consumer complaints.

Functional Units. Within the CFPB, the legislation allocates for the creation of specific offices to handle different aspects of consumer protection. Each “functional unit” will address a specific issue such as research, community affairs, or industry complaints. The Office of Fair Lending and Equal Opportunity will provide oversight and enforcement of Federal fair lending laws, and coordinate fair lending and fair housing efforts with other agencies. The complaint unit will utilize a national consumer complaint hotline for consumers to report problems with financial products and services. Further, an Office of Financial Literacy will be responsible for developing and implementing initiatives to better educate consumers as to how handle their finances and use financial products and services responsibly.

Small Businesses. To protect small businesses from overly burdensome regulations, the legislation requires that the CFPB coordinate with other regulators when it promulgates rules. Small businesses will also be exempted from CFPB regulation if they meet certain criteria, ensuring that these small businesses are not unintentionally overregulated. Following these consultations, regulators may appeal a regulation to the FSOC if they believe the regulation would risk the safety and soundness of the banking system or the stability of the financial system. The FSOC, by a two-thirds vote, with concurrence by the chairperson, can overturn actions by the CFPB.

Interchange Fees. The legislation requires the Federal Reserve to issue rules ensuring that the fees charged on transactions involving a debit card issued by a bank with more than \$10 billion in assets are reasonable and proportional to the costs incurred by the bank. Card networks would also be prohibited from requiring the exclusive use of a specific network. This measure will allow merchants to set a \$10 minimum for credit card purchases without penalty, and would not prohibit merchants from offering customers discounts for the use of cash, check or debit cards.

11. Role of the Federal Reserve System

Continued Oversight. The legislation permits the Federal Reserve to continue regulating bank and thrift holding companies with assets of over \$50 billion, which includes the 35 largest bank holding companies. State nonmember insured banks, foreign banks having an insured branch, and State savings associations with assets under \$50 billion, however, will now fall under FDIC oversight. A Vice Chair of the Federal Reserve will be placed in charge of the supervision and will report semi-annually to Congress on regulatory activities. Further, large bank holding companies that received TARP money may not evade Federal Reserve oversight simply by selling or disposing of their depository institution holdings.

Emergency Lending Powers. The Government Accountability Office will conduct a one-time audit of the Federal Reserve's emergency lending actions during the financial crisis under Section 13(3) of the Federal Reserve Act, and details of the audit must be published on the Federal Reserve's website by December 1, 2010. Further, the bill significantly restricts future Section 13(3) emergency lending activity. The bill requires approval of any such lending program by the Secretary of the Treasury, and the Federal Reserve is prohibited from propping up an individual company with the powers. Also, collateral must be sufficient to shield taxpayers from losses. In addition, the Federal Reserve will be required in the future to disclose counterparties and information about amounts, terms and conditions of discount window lending, and open market transactions on an on-going basis, with specified time delays to protect market stability.

Federal Reserve Bank Presidents. The presidents of the Federal Reserve Banks, including New York, will be elected by Class B directors, who are elected by member banks to serve the public and Class C directors, who are appointed by the Federal Reserve to serve the public. In an effort to curb conflicts of interest, the legislation no longer allows Class A directors, who are elected by member banks to serve member banks, to vote for the presidents of the Federal Reserve Banks.

12. Mortgage Reform and Anti-Predatory Lending

Repayment Ability Determination. The Dodd-Frank Act provides that a creditor must make a reasonable and good faith determination of a consumer's ability to repay before making a residential mortgage loan. The determination must be based on verified and documented information and must take into account all applicable taxes, insurance and assessments. Creditors are entitled to a presumption of compliance with the repayment ability determination requirements in connection with lower-risk loans defined as "qualified mortgage loans." With respect to certain federally insured or guaranteed loans, the applicable agencies may exempt refinancings for current borrowers under a streamlined refinancing from the income verification requirement, subject to certain conditions.

Combined TILA/RESPA Disclosure. The CFPB is directed to propose model disclosures that combine the initial and final disclosure statement required under the Truth in Lending Act (TILA) and the good faith estimate and HUD-1 settlement statement under the Real Estate Settlement Procedures Act (RESPA) into a single, integrated disclosure for mortgage loan transactions.

Mortgage Originators. The Dodd-Frank Act provides that mortgage originator compensation may not vary, directly or indirectly, based on the terms of the loan, other than the principal amount of the loan. The bill places additional restrictions on mortgage originator compensation and prohibits mortgage originators from steering consumers to loans they cannot afford or that have predatory characteristics. For purposes of the compensation and steering provisions, a mortgage originator would not include a creditor, except in a table funded transaction.

Escrow/Impound Requirements. Subject to exceptions, a creditor is required to establish an escrow account in connection with a closed-end consumer credit transaction secured by a first lien on a consumer's principal dwelling for the payment of taxes and hazard insurance and, if applicable, flood insurance, mortgage insurance, ground rents and any other required periodic payments or premiums with respect to the property or the loan terms.

HOEPA Loans. The Dodd-Frank Act modifies the trigger for a loan to be subject to the Home Ownership and Equity Protection Act (HOEPA) by requiring the APR to be compared to the average prime offer rate for a comparable transaction and not the rate on U.S. Treasury securities having a comparable maturity. The points and fees trigger is lowered, and a prepayment fee trigger is added.

Appraisal-Related Changes. The Dodd-Frank Act amends TILA to add appraiser independence requirements for mortgage loans secured by a principal dwelling. On the date that the interim final regulations are promulgated, the Home Valuation Code of Conduct will have no force or effect. The Dodd-Frank Act also addresses appraisal portability, appraiser compensation, registration of appraisal management companies, limitations on automated valuation models and broker price opinions, the provision of a copy of an appraisal to an applicant, and the use of appraisals for certain higher-risk mortgage loans.

Home Mortgage Disclosure Act. The Dodd-Frank Act significantly expands the data reporting requirements under the Home Mortgage Disclosure Act (HMDA).

S.A.F.E. Act. The Dodd-Frank Act amends the S.A.F.E. Mortgage Licensing Act (S.A.F.E. Act) by moving the enforcement and rulemaking authority under the S.A.F.E. Act from HUD to the CFPB.

TILA Servicing Requirements. The Dodd-Frank Act adds requirements to TILA that are similar to the servicing requirements that the Federal Reserve Board added to Regulation Z, regarding the crediting of payments and the provision of payoff statements.

RESPA Servicing Requirements. The Dodd-Frank Act amends the qualified written request provisions of RESPA to reduce the time to acknowledge the receipt of and act on a qualified written request. Additionally, a fee may not be imposed for responding to "valid qualified written requests," to be defined by the CFPB. Upon the payoff of a loan the servicer must within 20 business days return the escrow account balance to the borrower or credit the balance to a similar account for a new mortgage loan with the same lender. The Dodd-Frank Act amends RESPA to impose restrictions on the force-placement of insurance by mortgage servicers.

Fannie Mae and Freddie Mac. The Secretary of the Treasury is required to conduct a study of and develop recommendations regarding the options for ending the conservatorship of Fannie Mae and Freddie Mac while minimizing the cost to taxpayers. Options to be considered are: (1) the gradual wind-down and liquidation of the entities, (2) the privatization of the entities, (3) the incorporation of the functions of the entities into a federal agency, (4) the dissolution of Fannie Mae

and Freddie Mac into smaller companies, and (5) any other measures the Secretary determines to be appropriate.

13. Financial Crisis Assessment Fund

The Dodd-Frank Act creates a financial crisis assessment fund to cover the costs of implementing the legislation. After significant debate, funding for the bill will come from \$19 billion raised by limiting the spending authority under the Troubled Asset Relief Program to \$475 billion, as opposed to the previous limit of \$700 billion, and prohibiting the allocation of TARP funds repaid by TARP participants for further use. As an additional source of revenue, funding for the Dodd-Frank Act will also come from raising the FDIC's reserve ratio from 1.15 percent to 1.35 percent by 2020, with an exemption for banking institutions with less than \$10 billion in deposits.

14. Executive Compensation

The Dodd-Frank Act would establish new rules for (1) shareholder "say-on-pay" votes; (2) compensation committee independence (including compensation consultant independence) and disclosure; (3) expanded proxy disclosure (pay vs. performance); (4) compensation clawbacks; (5) hedging disclosure; and (6) enhanced compensation disclosure for financial institutions.

"Say-on-Pay." At least once every three years, public company proxy solicitations will be required to include a separate non-binding "say-on-pay" resolution that will give shareholders an advisory (non-binding) vote on executive compensation matters. With respect to proxy solicitations in connection with mergers and acquisitions, the "say-on-pay" resolution will require disclosure to shareholders of *all* compensation (whether payable currently, deferred or contingent) that is or may be paid to executive officers in connection with such merger or acquisition (so-called "parachute" payments). The SEC may adopt exemptions for small issuers. Finally, the Dodd-Frank Act requires institutional investment managers to report at least annually how they voted on all "say-on-pay" resolutions.

Compensation Committee Independence and Disclosure. The Dodd-Frank Act directs the SEC to issue rules prohibiting the listing of any security on a national securities exchange or national securities association (Exchanges) of any issuer (other than a controlled company more than 50% owned by another issuer, person or group) that does not comply with the independence requirements for members of the compensation committee. The SEC is directed to adopt rules for cure procedures to permit issuers reasonable opportunity to come into compliance before de-listing.

The Exchanges are required to identify factors impacting independence, such as whether the director derived any income from the issuer through consulting or advisory fees or otherwise, and whether the director is otherwise affiliated with the issuer or one of its subsidiaries or affiliates. The adoption of independence standards should preserve the compensation committee's ability to engage the services of any class of Advisor. The Exchanges could exempt particular relationships between directors and the issuer as appropriate in light of the size of the issuer and other relevant factors. Compensation committees also would be responsible for considering the independence of the Advisors retained by the committee. The Dodd-Frank Act directs the disclosure of an issuer's

receipt of advice from or retention of any compensation consultant and the existence and resolution of any conflicts of interest in the issuer's annual proxy solicitation. The Dodd-Frank Act directs issuers to provide sufficient funding to compensation committees to pay reasonable compensation to compensation consultants and other advisors to the compensation committee.

Pay vs. Performance Disclosure. The Dodd-Frank Act requires the SEC to amend its rules to require further disclosure of how executive compensation relates to actual financial performance, taking into account changes in the value of an issuer's stock and dividend distributions. The new disclosure requirements also include a comparison of how median employee compensation compares to CEO compensation.

Recovery of Erroneously Awarded Compensation (the "Clawback"). The Dodd-Frank Act requires the SEC to issue rules prohibiting the Exchange listing of any security of any issuer that does not adopt and implement a "clawback" policy, as outlined below. Issuers are required to adopt a policy providing (1) for disclosure of any incentive-based compensation that is based on financial information required to be reported under the securities laws; and (2) that in the event of an accounting restatement due to material noncompliance with any financial reporting requirement under the securities laws, the issuer will recover ("clawback") from any current or former executive officer who received incentive-based compensation (including stock options) during the three-year period preceding such restatement, based on erroneous data, any amount in excess of what would have been paid to the executive based on such restatement.

Hedging by Employees/Directors Disclosure. The Dodd-Frank Act directs the SEC to adopt rules requiring public issuers to disclose in their annual proxy statement employee and director purchases of financial instruments (including futures, swaps, collars, etc.) that hedge or offset any decrease in the market value of the issuer's securities granted as compensation by the issuer to the employee or director or held, directly or indirectly, by the employee or director.

Enhanced Compensation Disclosure for Financial Institutions. The Dodd-Frank Act directs Federal bank regulators to jointly adopt guidance requiring covered financial institutions to disclose sufficient information on all incentive-based compensation structures to permit regulators to determine if such compensation structures: (1) provide any executive officer, employee, director or principal shareholder with excessive compensation, fees or benefits or (2) could lead to material financial loss to such financial institution. Federal bank regulators are further directed to jointly adopt guidance to prohibit or restrict any such compensation structures (or elements of such structures) described in (1) and (2) and to apply current FDIC compensation standards. "Covered financial institutions" include banks, bank holding companies, registered broker-dealers, credit unions, investment advisors and such other financial institutions as determined jointly by the Federal bank regulators. An exemption is set forth for financial institutions with assets less than \$1 billion.