

REGULATORY UPDATE:

The Regulatory Relief Act Has Been Signed into Law

On Tuesday, May 22nd 2018, the U.S. House of Representatives passed Senate Bill 2155: *The Economic Growth, Regulatory Relief, and Consumer Protection Act*. The bill, otherwise known as *The Regulatory Relief Act*, was subsequently signed into law by President Trump, establishing a new regulatory framework for banks and other financial institutions that is more closely aligned with their size, level of complexity and structure.

Key Provisions of the Law

While the provisions included within *The Regulatory Relief Act* are extensive, several notable changes include the following.

- Increasing the threshold for systemically important financial institutions (SIFI) from \$50 billion to \$250 billion.
- Ending internal stress tests for banks with less than \$250 billion in assets.
- Simplifying capital calculations, providing Volcker Rule exemption and relief from capital and leverage requirements for qualifying community banks with less than \$10 billion in assets.
- Raising the consolidated asset threshold for the Board of Governors of the Federal Reserve System's Small Bank Holding Company Policy Statement from \$1 billion to \$3 billion in assets.
- Increasing the threshold for mandatory risk committees from \$10 billion in assets to \$50 billion. The Federal Reserve will be permitted to establish a risk committee requirement for publicly traded bank holding companies with less than \$50 billion in total consolidated assets.
- Extending the examination cycle for well capitalized with assets less than \$3 billion community banks to 18 months.
- Providing relief for certain aspects of mortgage lending for community banks and credit unions.

Notable Sections Within the Legislation

Within *The Regulatory Relief Act* there are specific sections that will impact banks to varying degrees, based on their size, business model and complexity.

Section 201: Community Bank Leverage Ratio

Federal banking agencies must develop a specified Community Bank Leverage Ratio for banks with assets of less than \$10 billion. Under the rule, agencies may consider a company's risk profile when evaluating whether it qualifies as a community bank. Banks that exceed this ratio shall be considered in compliance with all other capital and leverage requirements.

The Basel III capital rules were designed to address conditions that contributed to the 2008 financial crisis. However, many have argued that these rules impose onerous and unnecessary burdens on community banks that were not engaged in the risky activities from which Basel III was designed to protect.

This bill will require regulators to create a community bank leverage ratio of tangible equity/averages assets between 8% and 10%. Banks maintaining a higher ratio would automatically comply with capital and leverage requirements.

Section 202: Limited Exception for Reciprocal Deposits

Reciprocal Deposits are deposits received by an agent institution through a deposit placement network with the same maturity (if any) and in the same aggregate amount as covered deposits placed by the agent institution in other network member banks.

Sec. 202 includes provisions that provide a limited exception for Reciprocal Deposits. Under the new rule:

“ [Reciprocal Deposits of an agent institution] shall not be considered to be funds obtained, directly or indirectly, by or through a deposit broker to the extent that the total amount of such reciprocal deposits does not exceed the lesser of: (A) \$5,000,000,000; or (B) An amount equal to 20 percent of the total liabilities of the agent institution.

The goal of the legislation is to provide banks (primarily community and regional banks) with greater flexibility to attract and retain stable local deposits by amending the classification of Reciprocal Deposits under the Federal Deposit Insurance Act.

Section 205: Short Form Call Reports

Section 205 amends Section 7a of the Federal Deposit Insurance Act to allow for a reduced reporting requirement for a covered depository institution when the institution makes the first and third report of condition for a year.

The term ‘covered depository institution’ means an insured depository institution that:

- “ (i) has less than \$5,000,000,000 in total consolidated assets; and
- (ii) Satisfies such other criteria as the appropriate Federal banking agencies determine appropriate.

The primary objective of this section is to remove burdensome reporting requirements on community banks.

Section 214: Revised Capital Standards for HVCRE

The new bill specifies that a federal banking agency may not put a depository institution through higher capital standards regarding a high-volatility commercial real-estate (HVCRE) exposure, unless it is an HVCRE acquisition, development, or construction (HVCRE ADC) loan.

An HVCRE ADC loan is defined as a loan that:

- “ (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;
- (3) is dependent upon future income or sales proceeds from, or refinancing of, the real property for the repayment of the loan.

Under current BASEL III capital rules, these loans are reported separately, and assigned a risk weight of 150%. The change alleviates a banking organizations’ obligation to hold this additional capital for HVCRE loans that are otherwise performing and do not pose a threat to the financial stability of the banking organization.

Section 403: Treatment of Certain Municipal Securities as Level 2B Assets

This bill amends the treatment of certain municipal obligations under the Federal Deposit Insurance Act as level 2B liquid assets if they are investment grade, liquid, and readily marketable when calculating LCR under Basel III. 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 liquid assets, or HQLAs).

The initial LCR did not include US municipal securities as HQLA. However, the Federal Reserve Board issued regulations in April 2016 classifying certain US municipal securities as such. This would codify these regulations in the statute, and therefore make investments in such municipal bonds more attractive to covered banks.

Other sections within the legislation are designed to address the industry as a whole, such as the emerging risk of cyber threats.

Section 216: Treasury Report On Risks of Cyber Threats

Section 216 states:

“ Not later than 1 year after the date of enactment of this Act, the Secretary of the Treasury shall submit to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives a report on the risks of cyber threats to financial institutions and capital markets in the United States, including—

(1) an assessment of the material risks of cyber threats to financial institutions and capital markets in the United States;

(2) the impact and potential effects of material cyberattacks on financial institutions and capital markets in the United States;

(3) an analysis of how the appropriate Federal banking agencies and the Securities and Exchange Commission are addressing the material risks of cyber threats described in paragraph.

The inclusion of this provision highlights the increasing focus on cyber threats in financial services and the potential impact to the nation’s critical infrastructure.

Total Bank Solutions is Prepared to Help

Given the scope of the changes included under *The Regulatory Relief Act* and other recent rule changes, such as the 2017 *Tax Cuts and Job Act*, FDIC’s Recordkeeping for Timely Deposit Insurance Determination, among others, we understand that our clients will need to evaluate the impact of the various new rules and their applicability based on their size, unique business models and firm objectives.

Banks and financial institutions of all sizes should also consider the new rules in the context of larger technology trends, such as digital transformation, that are simultaneously reshaping how the financial industry operates and serves its clients.

We believe that as the industry continues to evolve, the most successful firms will be able to deliver a range of integrated “wealth management” solutions both seamlessly and securely. To do so, firms must balance the changing needs and expectations of their clients and their ability to create and deliver, either themselves or through partnerships, industry leading products and services.

At Total Bank Solutions, our mission is to help our clients achieve success by delivering innovative cash sweep, deposit funding, risk management and securities based lending solutions today and in the future. Since 2004, we have served the needs of the largest global banks and financial institutions as well as regional and community banks, combining deep industry experience with superior business processes and advanced technology to create value for their organizations and clients.

Over the coming months, we will be launching a series of initiatives designed to increase our engagement with clients on these and other topics, share our vision and introduce new capabilities in support of our overall mission.

Some of these initiatives include:

- The extension of our **Deposit Management System (DMS)** to facilitate the placement of Reciprocal Deposits.
- The formal launch of our end-to-end securities based lending platform, the **Loan Management System (LMS)**.
- Enhancing **TBS Bank Monitor** to facilitate the analysis of and compliance with relevant sections of new legislation, including:
 - Updated stress test module
 - Customized enterprise risk and compliance modules
 - Community Bank Leverage Ratio
- Launching a series of quarterly client webcasts designed to address specific regulatory changes, market trends and their implications
- Hosting senior management strategy sessions to facilitate discussions about how digital transformation is re-shaping our industry and a review of practical adoption strategies.
- Continuing our ongoing regulatory outreach programs and expanding the scope to include industry consultants with relevant domain experience.

Finally, we value the collaborative relationships we have built with our clients and are grateful for the opportunity to contribute toward their success. As a trusted partner, we are committed to making the necessary investments in our people and platform as we continue to look for ways to add value and deliver a higher level of service on behalf of our clients.

For additional information please feel free to contact your sales coverage, account management representative or directly: info@totalbanksolutions.com