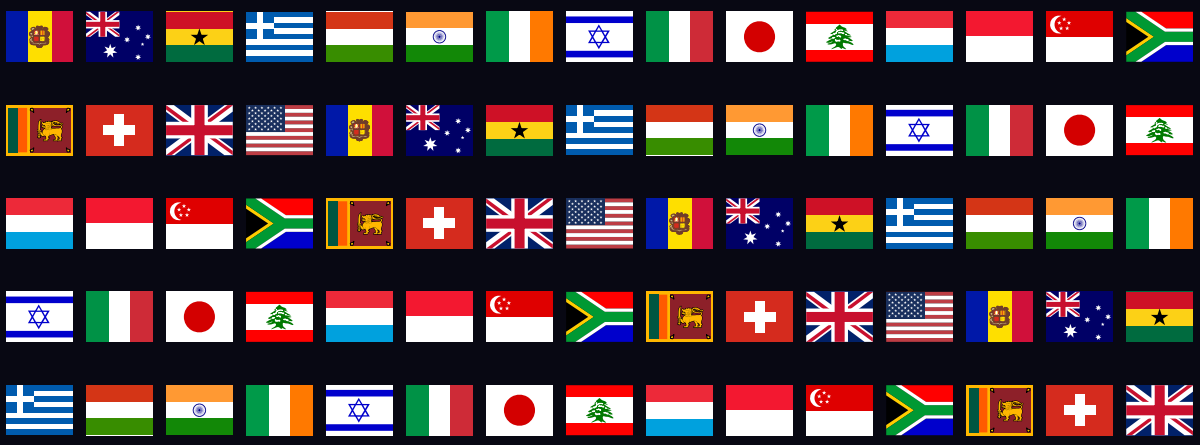
BANKING REGULATION

USA



LEXOLOGY
Getting The Deal Through

Consulting editor

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Banking Regulation

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Quick reference guide enabling side-by-side comparison of local insights, including into the legal and regulatory framework; supervision and enforcement; resolution; capital requirements; ownership restrictions and implications; changes in control; and recent trends.

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UPDATE AND TRENDS

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REGULATORY FRAMEWORK

Key policies

What are the principal governmental and regulatory policies that govern the banking sector?

Given their importance to the US economy, banking organisations are among the most highly regulated institutions in the United States. Broadly speaking, governmental and regulatory policies have two areas of focus:

- the safety and soundness of the banking organisations themselves; and
- promoting economic and social objectives, including the separation of banking and commerce.

As to the first area, banking organisations are subject to a wide range of laws, regulations and policies that limit their activities. While a typical US corporation can engage in any activity that is not prohibited by law, a banking organisation may only engage in activities permitted by the banking laws. In addition, banking organisations must maintain minimum capital and liquidity levels.

As to the second area, banking organisations are, among other things, subject to:

- activities restrictions intended to distinguish between permissible banking activities and impermissible commercial ones;
- a wide range of consumer protection laws designed to ensure non-discriminatory access to banking services; and
- stringent anti-money laundering requirements to facilitate government identification of illegal financial activity.

Moreover, given their unique role as a financial bridge between the government and customers, banking organisations also facilitate the government’s transmission of monetary policy.

Because the application and interpretation of banking law in the United States is largely delegated to administrative agencies through regulation, guidance and policies, bank regulators have a significant impact on the bank regulatory landscape, leading to the common saying 'personnel is policy'. The shift away from a deregulatory approach under the Trump administration could have a significant impact on the direction of bank regulation and oversight in the coming years.

Law stated - 24 January 2022

Regulated institutions

What are the defining characteristics of a bank to be caught by the banking laws and regulations? Is non-bank fintech regulated differently?

For the purposes of the current US bank regulatory regime, a bank is generally defined using a hybrid approach that includes any entity that functions as a bank by making commercial loans and taking demand deposits or that engages in specialised banking activity, such as taking deposits insured by the Federal Deposit Insurance Corporation (FDIC). Entities that have a banking charter (entities engaged in such activities are required to obtain a banking charter) are also covered under the definition of a bank. This approach is often referred to as an entity-based regulatory approach. However, in recent years, fintech (non-bank) companies have encroached on many services that traditionally were the exclusive domain of banks, such as lending. Such companies generally would not be subject to banking laws unless they engage in activities that require a banking charter.

The extent to which the range of banking laws applies to a particular banking organisation depends in part on the nature of its charter. For example, limited purpose state trust companies without FDIC insurance are typically subject to a relatively limited number of banking laws in their chartering state. On the other hand, FDIC-insured, full-service state or federally chartered banks are subject to a wide array of federal (and potentially state) regulations.

Fintech companies currently engage in a wide array of activities that were formerly exclusively performed by banks, such as retail and commercial lending and payment services. Because they often do not have bank charters, they are not subject to the typical range of banking laws. However, they may be subject to the relevant laws and licensing requirements of the states in which they have customers, which can impose significant burdens on their operations.

Law stated - 24 January 2022

Do the rules vary depending on the size or complexity of the banking institution?

Yes. The 2008 financial crisis resulted in the Dodd–Frank Wall Street Reform and Consumer Protection Act (the Dodd–Frank Act), which sought to create meaningful differences in the capital, liquidity and oversight expectations of banking organisations depending on their size and complexity. While imposing the most stringent requirements on the largest US banking organisations, the Dodd–Frank Act generally imposed significantly enhanced burdens on banking organisations with over US$50 billion in assets (deemed to be systemically important).

In 2018, the Federal Reserve Board (FRB) led an effort to further tailor these enhanced burdens to more accurately reflect the size and complexity of banking organisations. This tailoring framework was developed in response to the Economic Growth, Regulatory Relief and Consumer Protection Act of 2018, which mandated certain prudential standards for banking organisations with US$250 billion or more in assets and allowed the tailored application of these prudential standards for banking organisations with US$100 billion or more in assets. The FRB's revised rules, which became effective at the end of 2019, divided banking organisations with US$100 billion or more in assets into four categories, with Category 1 firms being subject to the most stringent requirements and uncategorised firms the least stringent, as laid out below.

- Category 1: US global systemically important banks (G-SIBs).
- Category 2: firms that are not US G-SIBs that have greater than or equal to US$700 billion in total consolidated assets, or greater than or equal to US$100 billion in total consolidated assets and US$75 billion or more in cross-jurisdictional activity.
- Category 3: firms not in Category 1 or 2 that have greater than or equal to US$250 billion in total consolidated assets, or greater than or equal to US$100 billion in total consolidated assets and US$75 billion or more in any of the three following risk-based indicators:
  - weighted short-term wholesale funding;
  - non-bank assets; or
  - off-balance sheet exposure.
- Category 4: firms not in Category 1, 2 or 3 that have greater than or equal to US$100 billion in total consolidated assets.

Law stated - 24 January 2022

Primary and secondary legislation

Summarise the primary statutes and regulations that govern the banking industry.

The specific laws and regulations applicable to a particular banking organisation will depend principally on its charter, activities and size. Among the most significant federal statutes that govern the banking industry are the following.

- The Federal Reserve Act (FRA) establishes the Federal Reserve System as the central banking system of the United States responsible for managing the supply of money and providing oversight to its member banks.
- The Federal Deposit Insurance Act establishes the basic authority for the operation of the FDIC, including the Deposit Insurance Fund as well as the oversight and regulation of insured depository institutions.
- The Home Owners' Loan Act sets out requirements for federal savings associations (thrifts), and savings and loan holding companies (SLHCs).
- The Bank Holding Company Act of 1956 grants the FRB regulation and supervision over companies that control a bank (bank holding companies (BHCs)).
- The National Bank Act establishes the national banking system and the chartering and regulation of national banks by the Office of the Comptroller of the Currency (OCC).
- The International Banking Act of 1978 establishes that foreign banking organisations (FBOs) with operations in the United States are subject to regulation by US banking regulators.
- The Dodd–Frank Act significantly reformed the financial regulatory system after the Great Recession. The Dodd–Frank Act establishes the Consumer Financial Protection Bureau (CFPB) to focus on consumer and investor protections.
- The Community Reinvestment Act of 1977 requires banks to lend to the moderate and low-income residents of their service area.
- The banking laws of each of the 50 states.

Certain key FRB regulations promulgated under these acts include the following.

- Regulation Q sets minimum capital requirements and capital adequacy standards for state-chartered banks that are members of the Federal Reserve System (member banks and BHCs).
- Regulation K governs the international banking operations of US banking organisations and US operations of FBOs.
- Regulation Y and Regulation LL describe various requirements for BHCs and SLHCs, including transactions for which BHCs and SLHCs must seek and receive FRB approval.
- Regulation W provides rules for the types of transactions that can occur between a member bank (or a US branch or agency of an FBO) and its affiliates.
- Regulation YY establishes enhanced prudential standards for certain large BHCs and FBOs.
- Regulation VV restricts proprietary trading and investments or certain other relationships with hedge funds and private equity funds.
- Regulation O regulates the credit extensions that a member bank can offer its executive officers, principal shareholders and directors.

In many cases, the OCC and the FDIC have published parallel regulations that cover the entities that they regulate.

Law stated - 24 January 2022

Regulatory authorities

Which regulatory authorities are primarily responsible for overseeing banks?

Unlike many other countries, the United States has several types of banking organisations, and several federal and state bank regulatory agencies that oversee them.

National banks and federal savings associations are subject to primary supervision by the OCC. State banks and trust companies are subject to the supervision and regulation of their chartering state, and often are subject to oversight at the federal level by either the FRB (if they are member banks) or the FDIC (if they are not). The FRB is the primary regulator for BHCs and SLHCs. Federally insured credit unions are supervised by the National Credit Union Administration. The CFPB, which has a primary focus on the protection of consumers and enforcement of consumer protection laws, also has examination authority over banks with assets of US$10 billion or more.

Law stated - 24 January 2022

Government deposit insurance

Describe the extent to which deposits are insured by the government. Describe the extent to which the government has taken an ownership interest in the banking sector and intends to maintain, increase or decrease that interest.

FDIC deposit insurance, which is backed by the full faith and credit of the US government, insures up to US$250,000 per depositor, per FDIC-insured bank, per ownership category.

As a general matter, the US government does not seek to maintain ownership interests in the banking sector. Nonetheless, the US government has taken an ownership interest in the banking sector through various programmes during periods of financial difficulty. Most notably, in 2008, the Treasury established the Capital Purchase Program under the Troubled Asset Relief Program, which purchased over US$200 billion in shares in over 700 financial institutions to recapitalise the banking system. These programmes subsequently wound down and the US government exited its investments.

Law stated - 24 January 2022

Transactions between affiliates

Which legal and regulatory limitations apply to transactions between a bank and its affiliates? What constitutes an ‘affiliate’ for this purpose? Briefly describe the range of permissible and prohibited activities for financial institutions and whether there have been any changes to how those activities are classified.

Sections 23A and 23B of the FRA and FRB Regulation W promulgated thereunder are designed to ensure that banks are protected in their dealings with affiliates. The types of transactions covered include:

- extensions of credit by the member bank (or US branch or agency of an FBO) to its affiliates;
- purchases of affiliate assets by the bank; and
- certain other credit transactions.

Unless an exemption applies, banks may engage in these types of covered transactions with their affiliates only if:

- the aggregate amount of the covered transactions of the bank or branch with any one affiliate does not exceed 10 per cent of the capital stock and surplus of the bank or branch; and
- the aggregate amount of covered transactions of the bank or branch with all affiliates does not exceed 20 per cent of the capital stock and surplus of the bank or branch.

In addition, credit transactions are subject to collateral requirements and virtually all transactions with affiliates – including service contracts – must be on arm's-length terms to the bank. An affiliate for these purposes includes, among others, any company:

- that controls the bank or thrift;
- that is under common control with the bank or thrift;
- with a majority of interlocking directors with a bank or thrift; or
- that is sponsored or advised by a bank or thrift.

Law stated - 24 January 2022

Regulatory challenges

What are the principal regulatory challenges facing the banking industry?

Historically, the banking industry has faced regulatory pressures from outside the regulatory perimeter as firms with a commercial presence enter into more direct competition with regulated banking organisations. Pressures also arise from the inside as banking organisations innovate and evolve in ways that may not be suited for existing regulatory frameworks. In recent years, fintech companies have struggled with significant compliance burdens as they try to situate themselves in the regulatory spectrum. Because these businesses are not subject to fintech-specific rules, licensing, registration and other regulatory requirements may apply to fintech companies at both the federal and state levels. The number and complexity of regulations that may apply have drawn criticism as having a potential chilling effect on innovation and growth.

Some regulators have sought to address these burdens. For example, the OCC created and defended in court a special purpose national bank charter for fintech companies that offer bank products and services. In 2020, the CFPB issued an advanced notice of proposed rule-making regarding the implementation of section 1033 of the Dodd–Frank Act, which provides for consumer access to financial records. In 2021, President Biden issued an executive order encouraging the CFPB to facilitate, in its rule-making, the portability of consumer financial transaction data so that consumers can more easily switch financial institutions and use new, innovative financial products.

Regulators have also been active in policing innovation. California's Department of Financial Protection and Innovation entered into a settlement agreement with Chime Financial, Inc for the fintech company's failure to comply with banking regulations. Cryptocurrency companies especially have faced regulatory and enforcement scrutiny from the Commodity Futures Trading Commission, the Securities and Exchange Commission (SEC), the Internal Revenue Service, the OCC, the Financial Crimes Enforcement Network and others as the growth of blockchain and digital asset technologies accelerate. In addition, in January 2021, Congress enacted the Anti-Money Laundering Act of 2020 that, among other measures, amended Bank Secrecy Act definitions and money transmitter registration requirements to expressly encompass 'value that substitutes for currency'.

In addition, the shifting political landscape can also have a significant impact on the state and direction of bank

regulation. For example, Biden administration appointees and nominees have indicated a desire for more expansive regulation around regulatory capital, climate change, cryptoassets, and bank mergers and acquisitions (M&A).

Law stated - 24 January 2022

Consumer protection

Are banks subject to consumer protection rules?

US banking organisations are subject to extensive consumer protection rules at both the federal and state levels, regardless of their chartering authority. At the federal level, banking organisations with assets in excess of US$10 billion, as well as their affiliates, are generally subject to examination by the CFPB (with authority for certain regulatory frameworks retained by the primary federal bank regulators, including the OCC, the FRB or the FDIC), while those with assets of US$10 billion or less are subject to examination by their respective primary federal bank, with respect to the following consumer protection rules:

- fair lending (Equal Credit Opportunity Act, Fair Housing Act);
- consumer credit (Truth in Lending Act, Fair Credit Reporting Act, Military Lending Act, Servicemembers' Civil Relief Act);
- payday lending, vehicle title loans and high-cost instalment loans fall under the Dodd–Frank Act's authority to regulate unfair, deceptive or abusive acts or practices (UDAAP);
- mortgage disclosures (Home Mortgage Disclosure Act, Real Estate Settlement Procedures Act);
- deposits, checks, and collections (Truth in Savings Act);
- electronic fund transfers and prepaid cards (Electronic Fund Transfers Act, CARD Act);
- data privacy falls under the privacy provisions of the Gramm–Leach–Bliley Act;
- debt collection (Fair Debt Collection Practices Act); and
- any other act or practice that may be deemed to be 'unfair', 'deceptive', or 'abusive' in accordance with the Dodd–Frank Act's UDAAP requirements.

As noted above, states may also impose their own consumer protection laws – including for those topics outlined above – although they are subject to federal pre-emption unless state requirements provide more protection to consumers. Additionally, banking organisations are generally subject to the usury laws of their respective home states, although interstate banks may be permitted to utilise the usury laws of host states under certain circumstances.

Law stated - 24 January 2022

Future changes

In what ways do you anticipate the legal and regulatory policy changing over the next few years?

In 2021, the Biden administration made a number of significant appointments to the banking agencies, including Rohit Chopra as CFPB director and Gary Gensler as chair of the SEC. However, several key positions – including Comptroller of the Currency and FRB Vice Chair for Supervision – remain to be filled. In addition, at the end of 2021, FDIC chair Jelena McWilliams announced her resignation, creating another significant vacancy to be filled by President Biden and likely leaving the FDIC in the control of Democratic appointees.

This new leadership will drive the priorities for legal and regulatory policy over the next few years. The agencies have already indicated key areas of focus, including climate, cryptoassets, cybersecurity, national security, money laundering, consumer protection and bank M&A (including the impact that such activities have on low- and moderate-income

communities). These leaders have also indicated their intention to review existing capital and liquidity requirements, risk management procedures, disclosure requirements, and other areas. With respect to enforcement, the regulators are expected to take a tougher stance on the regulation of the largest banks. Particularly after FDIC chair McWilliams' departure, it will be much easier for the Biden administration's appointees to advance the administration's interagency regulatory and enforcement agenda around these key areas of focus.

This shift in leadership and priorities is expected to have a significant impact on the regulatory challenges facing banks, and their ability to expand and engage in new activities. For example, prior to the 2020 election, many regional banks announced fintech acquisitions to compete with larger firms. The Biden administration's focus on bank M&A may have the effect of slowing this trend.

Law stated - 24 January 2022

SUPERVISION

Extent of oversight

How are banks supervised by their regulatory authorities? How often do these examinations occur and how extensive are they?

Bank supervision is used to ensure that banks comply with applicable rules and regulations by allowing regulators to identify and mitigate specific risks within a banking organisation, as well as evaluate the banking system as a whole. Banks are supervised by their primary regulator, which is determined based on the bank's charter type. Bank holding companies as well as savings and loan holding companies are supervised by the Federal Reserve Board (FRB). Furthermore, larger banks are also subject to supervision for compliance with consumer protection laws and regulations by the Consumer Financial Protection Bureau (CFPB).

Regulators have two primary methods to supervise banks: reporting requirements for continuous monitoring and periodic examinations. Full-scope, on-site examinations must be conducted at least once every 12 months, except for smaller banks with less than US$3 billion in assets, which are examined once every 18 months. Bank examiners will rate a bank based on components of capital adequacy, asset quality, management earnings, liquidity and sensitivity to market risk. Banks will also receive a composite rating based on these components. Any issues may require more frequent or detailed exams as well as corrective action.

Law stated - 24 January 2022

Enforcement

How do the regulatory authorities enforce banking laws and regulations?

The primary federal banking regulators with authority to enforce banking laws and regulations are the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), the FRB and, for banking organisations with over US$10 billion of assets with respect to consumer financial matters, the CFPB. These agencies have a variety of enforcement mechanisms, which range from less severe informal actions to more severe formal actions. Informal actions are ordinarily not enforceable in court.

Informal actions include supervisory criticisms ('matters requiring attention' and 'matters requiring immediate attention') in exam reports, bank board resolutions and memoranda of understanding. These are not public actions and are generally used for less severe situations where regulators believe the bank is able to, and will, correct the issue in a reasonably prompt fashion.

Formal actions include written agreements, cease and desist orders, civil money penalties, and removal orders. Formal

actions also often result in downgraded examination ratings for banks, which in turn can limit their ability to complete acquisitions or engage in new activities, and often involve costly compliance efforts to remediate. Provisions contained in these types of actions can generally be enforced in federal court.

Law stated - 24 January 2022

What are the most common enforcement issues and how have they been addressed by the regulators and the banks?

US authorities have dedicated increasing resources to combat illicit financial activity, with a focus on Bank Secrecy Act (BSA) and anti-money laundering (AML) compliance programmes, cases involving economic sanctions violations, and regulation of cryptocurrencies.

For example, in October 2021, the Department of Justice announced the creation of a National Cryptocurrency Enforcement Team to tackle complex investigations and prosecutions of criminal misuses of cryptocurrency, particularly for crimes involving money laundering. The federal banking regulators and the Financial Crimes Enforcement Network (FinCEN) also have indicated that BSA/AML enforcement is a priority. These authorities issued statements in August 2020 explaining their approach to BSA/AML enforcement and outlining scenarios under which formal actions may be taken against institutions under their jurisdiction. In June 2021, FinCEN issued the first government-wide priorities for AML and countering the financing of terrorism policies, which include a focus on the use of virtual currencies to facilitate illicit activities. Rohit Chopra and Gary Gensler were confirmed as CFPB director and Securities and Exchange Commission (SEC) chair respectively in 2021, signalling a potential increase in regulatory enforcement actions in the coming years based on their prior track records at the CFPB and Commodity Futures Trading Commission, respectively.

Another area of significant focus by the bank regulators is on cybersecurity. For example, on 6 December 2021, the National Risk Committee of the OCC issued its Semiannual Risk Perspective for Fall 2021, which highlighted the 'evolving and increasingly complex' danger to the financial system from cyber threats, and encouraged banks and financial institutions to adopt robust cyber controls to minimise operational risk. Collectively, the New York Department of Financial Services, the SEC and the OCC have brought over a dozen enforcement actions related to cyber events over the past two years, which is a trend that is likely to continue under the Biden administration given its stated focus on cybersecurity issues.

Law stated - 24 January 2022

RESOLUTION

Government takeovers

In what circumstances may banks be taken over by the government or regulatory authorities? How frequent is this in practice? How are the interests of the various stakeholders treated?

If a bank has become – or is at risk of becoming – insolvent, there are two means by which the government can step in to resolve the failed institution.

The first method of resolution is solely for insured depository institutions (IDIs) and is governed by sections 11 and 13 of the Federal Deposit Insurance Act (the FDI Act). If an IDI fails, it will be placed into receivership with the Federal Deposit Insurance Corporation (FDIC) as its receiver. The FDIC will succeed by operation of law to all rights, powers and privileges of the failed bank, and its stockholders, directors and officers. The FDIC is obligated to minimise costs to the Deposit Insurance Fund. The FDIC will seek to resolve the bank in a manner that is least disruptive to depositors and the local community, and that will maintain public confidence in the US financial system. Insured deposits will be paid

and the remaining proceeds will be paid to creditors, whereas shareholders may not receive any payments.

The second method of resolution was enacted in 2010 under Title II of the Dodd–Frank Wall Street Reform and Consumer Protection Act (the Dodd–Frank Act). The Dodd–Frank Act created the orderly liquidation authority for a financial company (a broadly defined term that could include a bank holding company (BHC) or other bank affiliates) to be placed into an FDIC receivership process if resolution through bankruptcy would have serious adverse effects on financial stability. The orderly liquidation authority must be invoked by the Treasury upon the recommendation of certain regulatory agencies and in consultation with the President. If invoked, the FDIC would have broad authority to resolve the financial company using powers similar to those that it uses to resolve IDIs under the FDI Act.

The FDIC has frequently used the FDI Act to place IDIs into receivership, especially during periods of bank failures, such as during the savings and loan crisis from 1986 to 1994 and during the 2008 financial crisis. The orderly liquidation authority under Title II of the Dodd–Frank Act, by contrast, has yet to be invoked.

Law stated - 24 January 2022

Bank failure

What is the role of the bank's management and directors in the case of a bank failure? Must banks have a resolution plan or similar document?

Bank management and directors have a limited role in the resolution process. When the FDIC is appointed as receiver for a bank under the FDI Act, the FDIC succeeds to all the rights, powers and privileges of the directors and officers of the institution. In the case of an orderly liquidation under Title II of the Dodd–Frank Act, the FDIC is required to ensure that management and directors responsible for the failed condition of the financial company are removed.

Large banks and BHCs are required to periodically file resolution plans or living wills.

Law stated - 24 January 2022

Are managers or directors personally liable in the case of a bank failure?

After the FDIC is appointed receiver over a bank, the agency may conduct investigations and bring suits against former directors or officers. Most cases result from demonstrated failures to satisfy the duties of loyalty and care. Examples include cases where a director or officer engaged in dishonest conduct, was responsible for the failure of the bank to adhere to applicable laws and regulations, or participated in a safety or soundness violation.

Law stated - 24 January 2022

Planning exercises

Describe any resolution planning or similar exercises that banks are required to conduct.

The Dodd–Frank Act requires large BHCs and non-bank systemically important financial institutions to submit resolution plans to the FDIC and the Federal Reserve Board (FRB) to prepare for a rapid and orderly resolution under the Bankruptcy Code. The plans require the submission of a resolution strategy for how the financial institution can be resolved without serious adverse effects on US financial stability, as well as information regarding the financial institution's material legal entities, core business lines, operations that are critical to the US financial system, and its financial, operational and external dependencies and interconnections, among other information relevant to the resolution.

The resolution plan used to be required for financial institutions with US$50 billion or more in assets. In 2018, the Economic Growth, Regulatory Relief and Consumer Protection Act of 2018 raised the threshold to US$250 billion, and gave the FRB discretion to apply the requirement to firms with total consolidated assets of between US$100 billion and US$250 billion. In 2019, the FRB and the FDIC revised the implementing regulations to state that financial institutions with total consolidated assets of less than US$100 billion do not have to file resolution plans, and only certain firms (based on tailoring factors) with total assets between US$100 and US$250 billion are required to file plans. In addition, the resolution plan filing requirement moved from an annual to a two- or three-year submission cycle, depending on the firm's category under the FRB's tailoring rules, with the largest firms being required to alternate between filing a full and a targeted resolution plan. The first targeted plans were filed by the US global systemically important banks on 1 July 2021 and were required to address, among other things, the firm's response to the events surrounding the covid-19 pandemic.

The FDIC has issued a separate rule (the IDI Rule) that requires IDIs with more than US$50 billion in assets to submit resolution plans to the FDIC. The resolution plan must show that the FDIC, as receiver, could resolve the IDI under the FDI Act in a manner that protects insured depositors, maximises return from the sale of the IDI's assets and minimises the amount of any loss realised by creditors.

In 2019, the FDIC issued an advance notice of proposed rule-making (ANPR) seeking comment on potential changes to the IDI Rule and indicated that the submission of IDI resolution plans would not be required until the rule-making process was completed. In January 2021, however, the FDIC said that it would require IDIs with US$100 billion or more in assets to resume resolution plan submissions. Further, the FDIC explained that it planned to carry out targeted engagement and capabilities testing, which is an approach to IDI resolution planning contemplated in the ANPR, with select financial institutions on an as-needed basis.

In June 2021, the FDIC issued a statement modifying its approach to implementation of the IDI Rule. The statement confirmed that it resumed the requirement of resolution plan submissions under the IDI Rule from IDIs with US$100 billion or more in assets and extended the resolution plan submission frequency for these institutions to a three-year cycle. It also laid out the FDIC's modifications to the process for IDI resolution planning, the expectations for the contents of IDI resolution plans and exemptions to content requirements for IDI resolution plans. Thus, the statement appears to be in lieu of any proposed revisions to the text of the IDI Rule contemplated by the ANPR.

Law stated - 24 January 2022

CAPITAL REQUIREMENTS

Capital adequacy

Describe the legal and regulatory capital adequacy requirements for banks. Must banks make contingent capital arrangements?

Capital adequacy regulations in the form of minimum ratio requirements are a core aspect of the supervision of banking organisations. Risk-based capital ratios measure the ratio of a banking organisation's eligible capital to its risk-weighted assets (balance sheet assets adjusted based on their deemed riskiness). Leverage capital ratios serve as a backstop to risk-based capital measures by measuring the ratio of a banking organisation's eligible capital to its total assets (unadjusted for risk). These capital requirements generally apply both to banks themselves, as well as to their parent bank holding companies (BHCs) or savings and loan holding companies (SLHCs), on a consolidated basis.

Except in certain limited resolution contexts, US banking organisations generally need not make contingent capital arrangements.

Law stated - 24 January 2022

How are the capital adequacy guidelines enforced?

Bank regulators have at their disposal a number of statutory tools to enforce capital adequacy requirements. Most notable are:

- bank regulators' expansive powers under the Prompt Corrective Action (PCA) framework under the Federal Deposit Insurance Act (the FDI Act);
- the International Lending Supervision Act of 1983 with respect to insured depository institutions (IDIs); and
- Federal Reserve Board (FRB) powers regarding BHCs and SLHCs under the Bank Holding Company Act of 1956 and the Home Owners' Loan Act, respectively.

The PCA regulations establish five PCA categories based on an IDI's capital position and mandate certain specified regulatory responses in each category, including potential restrictions on capital distributions and management fees, requiring regulatory monitoring, requiring submission of a capital restoration plan, restrictions on growth, and prior approval of certain expansion proposals.

The ratios associated with the various categories are summarised below.

Category	Total risk-based capital ratio (%)	Tier 1 risk-based capital ratio (%)	Common equity Tier 1 capital ratio (%)	Tier 1 leverage capital ratio (%)
Well capitalised	≥10	≥8	≥6.5	≥5
Adequately capitalised	≥8	≥6	≥4.5	≥4
Undercapitalised	<8	<6	<4.5	<4
Significantly undercapitalised	<6	<4	<3	<3
Critically undercapitalised	Ratio of tangible equity to total assets ≤2%			

The FRB has adopted a framework for BHCs and SLHCs that impose similar limitations – including activities limitations – on BHCs and SLHCs that are not deemed to be well capitalised, as well as those that do not pass its periodic stress test requirements. A BHC will be deemed to be well capitalised if it maintains a total capital ratio of 10 per cent or greater and a Tier 1 capital ratio of 6 per cent or greater.

Law stated - 24 January 2022

Undercapitalisation

What happens in the event that a bank becomes undercapitalised?

When an IDI becomes undercapitalised (either by failing to meet capital ratios or by regulatory determination) under the PCA framework, the relevant bank regulator must issue a warning to the bank and order the bank to take certain corrective actions to restore the bank to acceptable capital levels. The further undercapitalised an IDI becomes, the more significant the potential limitations.

All undercapitalised IDIs must submit an acceptable capital restoration plan and may not acquire any interests in any companies, establish branches or engage in new lines of business until the capital restoration plan has been accepted by its primary federal banking regulator. Before a plan can be accepted, its parent company must guarantee that the institution will comply until the bank is adequately capitalised during four consecutive quarters.

Law stated - 24 January 2022

Insolvency

What are the legal and regulatory processes in the event that a bank becomes insolvent?

If an IDI fails, it will be placed into receivership with the Federal Deposit Insurance Corporation (FDIC) as its receiver. The FDIC will succeed by operation of law to all rights, powers and privileges of the failed bank and its stockholders, directors and officers. The FDIC is obligated to minimise costs to the Deposit Insurance Fund. The FDIC will seek to resolve the bank in a manner that is least disruptive to depositors and the local community, and that will maintain public confidence in the US financial system. Insured deposits will be paid and the remaining proceeds will be paid to creditors, whereas shareholders may not receive any payments.

A second method of resolution was enacted in 2010 under Title II of the Dodd–Frank Wall Street Reform and Consumer Protection Act (the Dodd–Frank Act). The Dodd–Frank Act created the orderly liquidation authority for a financial company (a broadly defined term that could include a BHC or other bank affiliates) to be placed into an FDIC receivership process if resolution through bankruptcy would have serious adverse effects on financial stability. The orderly liquidation authority must be invoked by the Treasury upon the recommendation of certain regulatory agencies and in consultation with the President. If invoked, the FDIC would have broad authority to resolve the financial company using powers similar to those that it uses to resolve IDIs under the FDI Act.

Law stated - 24 January 2022

Recent and future changes

Have capital adequacy guidelines changed, or are they expected to change in the near future?

The federal banking agencies adopted rules implementing the Basel III framework in late 2013 and have adopted several revisions to that framework, including following the enactment of the Economic Growth, Regulatory Relief and Consumer Protection Act of 2018. In December 2017, the Basel Committee on Banking Supervision adopted revisions to the Basel III framework, which it expects member countries (including the United States) to adopt at a national level by 1 January 2023. The federal banking agencies are expected to propose revisions to their capital requirements to implement these changes in the near future. Under the Biden administration, the federal banking agencies are less likely to deviate from the international Basel III framework in any way that would reduce capital requirements for banks.

Law stated - 24 January 2022

OWNERSHIP RESTRICTIONS AND IMPLICATIONS

Controlling interest

Describe the legal and regulatory limitations regarding the types of entities and individuals that may own a controlling interest in a bank (or non-bank). What constitutes ‘control’ for this purpose?

Both individuals and entities may own a controlling interest in a bank. An individual or group of individuals seeking to acquire a bank will need to comply with the requirements of the Change in Bank Control Act (CIBCA). Under the CIBCA,

approval may be required before acquiring 10 per cent or more of the voting stock of a bank or company that controls a bank.

In general, a company that controls a bank or a bank holding company (BHC) will be regulated by the Federal Reserve Board (FRB). For this purpose, 'control' means having the power to vote 25 per cent or more of any class of voting securities, controlling the election of a majority of the directors or trustees, or exercising a controlling influence over the management or policies of the bank or holding company.

In 2020, the FRB finalised regulations putting in place a tiered framework for determining controlling influence, under which the FRB presumes that a company exercises a controlling influence over a bank if the company owns or controls a specified percentage of the bank's voting securities and other indicia of control are present. Voting securities are defined as securities that entitle the holder to vote for or select directors, trustees or partners, or entitle the holder to vote on or to direct the conduct of the operations or significant policies of the issuer. There are four tiers of the control analysis based on the ownership of voting securities of the bank or company:

- less than 5 per cent;
- 5 per cent to less than 10 per cent;
- 10 per cent to less than 15 per cent; and
- 15 per cent to less than 25 per cent.

Each higher ownership tier is accompanied by greater restrictions on various control factors.

Law stated - 24 January 2022

Foreign ownership

Are there any restrictions on foreign ownership of banks (or non-banks)?

Foreign banking organisations (FBOs) are generally subject to the same limitations and processes as US owners of banks pursuant to the general principle of national treatment. The federal banking laws do not prohibit foreign ownership or control of US depository institutions and the laws of states also permit foreign ownership of banks or thrifts chartered by the state. There are certain restrictions on citizenship, however, of directors of national banks and some state-chartered banks. An acquisition of a US bank or thrift by a foreign acquirer could be subject to a national security review by the Committee on Foreign Investment in the United States if the transaction could result in foreign control of any critical infrastructure. The FRB requires certain FBOs with a large US presence to form a US intermediate holding company to hold US subsidiaries, including bank subsidiaries.

Law stated - 24 January 2022

Implications and responsibilities

What are the legal and regulatory implications for entities that control banks?

A company that controls (within the meaning of the Bank Holding Company Act of 1956 (the BHC Act)) a bank and its affiliates are subject to banking laws, regulations, guidance and limitations on activities and operations. In particular, a BHC may not engage in any activity not explicitly authorised under the BHC Act, which generally requires that companies that control banks limit their activities to financial activities. Notable supervisory and regulatory implications include that the BHC will be subject to examinations, reporting requirements and capital requirements. The BHC would be subject to periodic on- and off-site examinations to assess the risk management and financial condition of the BHC and its subsidiaries. The BHC must submit periodic reports to the FRB, including financial

statements for the BHC and its subsidiaries as well as reports on company ownership and organisational structure. The BHC must also comply with minimum capital requirements and overall capital adequacy standards.

Law stated - 24 January 2022

What are the legal and regulatory duties and responsibilities of an entity or individual that controls a bank?

The Dodd–Frank Wall Street Reform and Consumer Protection Act imposes a 'source of financial strength' requirement on any company that directly or indirectly controls an insured depository institution. This requirement mandates that the controlling company of a bank must be able to provide financial and managerial assistance to the bank in the event of its financial distress. Under this doctrine, any company that controls a bank – regardless of whether it is a BHC under the BHC Act – must serve as a source of strength. Individuals, however, are not subject to this requirement.

Law stated - 24 January 2022

What are the implications for a controlling entity or individual in the event that a bank becomes insolvent?

If a bank becomes insolvent, it may be placed into receivership with the Federal Deposit Insurance Corporation (FDIC) as receiver. The FDIC will then have broad authority to resolve the bank. The FDIC may conduct investigations and bring suits against former directors or officers.

Law stated - 24 January 2022

CHANGES IN CONTROL

Required approvals

Describe the regulatory approvals needed to acquire control of a bank (or non-bank). How is 'control' defined for this purpose?

Transactions to acquire control of a bank are governed by the Change in Bank Control Act (CIBCA), the Bank Holding Company Act of 1956 (the BHC Act), the Home Owners' Loan Act (HOLA) and the Bank Merger Act.

The CIBCA mandates that any individual or company that acquires control of a bank must provide prior notice to the appropriate federal banking agency of the target bank. It requires regulators to approve or disapprove an acquisition within a specified time period. If the time period has expired without agency disapproval, the transaction can go forward. The CIBCA does not apply to transactions that require approval separately under the BHC Act, HOLA or the Bank Merger Act.

Under the BHC Act, if a company seeks to acquire control (the definition of which differs slightly from the CIBCA) of a bank or a bank holding company (BHC), it will require prior approval by the Federal Reserve Board (FRB). FRB approval is also required under HOLA for the acquisition of control of a savings association.

The Bank Merger Act requires that mergers between depository institutions receive prior approval from the primary federal regulatory of the resulting institution.

Law stated - 24 January 2022

Foreign acquirers

Are the regulatory authorities receptive to foreign acquirers? How is the regulatory process different for a foreign acquirer?

Under the International Banking Act of 1978, a foreign bank with a US commercial banking presence and any of its parent companies are subject to many of the same laws that regulate the activities of US BHCs.

Beginning in July 2016, the FRB has required certain foreign banking organisations (FBOs) to hold US-based subsidiaries – including depository institutions subsidiaries and broker-dealer subsidiaries – in an intermediate holding company to act as the parent company of all of the FBO's US subsidiaries. The rule applied to FBOs with US$50 billion or more in US non-branch assets and was an effort to consolidate supervision. The FRB could then require the intermediate holding company to comply with capital, stress testing, liquidity, risk management and other regulatory requirements in the same manner as applicable to a domestic BHC.

Law stated - 24 January 2022

Under what circumstances can a foreign bank (or non-bank) establish an office and engage in business? For example, can it establish a branch or must it form or acquire a locally chartered bank?

An FBO generally will be treated as a BHC under the BHC Act. FBOs that wish to establish a US banking presence or otherwise take part in deposit-taking activities in the United States may not do so through a branch office insured by the Federal Deposit Insurance Corporation (FDIC) but, instead, must establish or acquire an insured US bank subsidiary. All foreign banks must limit their US activities to those not requiring FDIC insurance. Foreign reserve services and privileges are open to foreign bank branches, but they are also subject to all supervision and enforcement requirements of US banking agencies.

State law determines whether a foreign bank with a branch in a given state may establish additional branches in that state. For this reason, an FBO that is establishing additional branches may prefer a federal licence in many states.

Law stated - 24 January 2022

Factors considered by authorities

What factors are considered by the relevant regulatory authorities in an acquisition of control of a bank (or non-bank)?

In reviewing an application for control of a bank, the BHC Act and the Bank Merger Act require federal regulators to consider various enumerated factors with respect to both the applicant and the bank. These factors include:

- the effect on competition;
- the financial and managerial resources and future prospects of the two entities;
- the competence, experience and integrity of the officers, directors and principal shareholders;
- the convenience and needs of the communities to be served; and
- any impact that the transaction will have on the banking or financial system.

Similarly, under the CIBCA, a notice of change in control can be disapproved if:

- the proposed acquisition of control would result in a monopoly;
- the proposed acquisition of control might substantially lessen competition;
- the financial condition of any acquiring person or the future prospects of the bank might jeopardise the financial stability of the bank;
- the competence, experience or integrity of any acquiring person or the proposed management personnel indicates that it would not be in the interest of depositors or the public to permit that person to control the bank; or
- the proposed acquisition would result in an adverse effect on the Deposit Insurance Fund.

Law stated - 24 January 2022

Filing requirements

Describe the required filings for an acquisition of control of a bank.

The filings that are required for the acquisition of control of a bank depend on what type of transaction is contemplated, and what statute and regulations govern the transaction. Examples of filings include:

- a Bank Merger Act Application;
- a Notice of Change in Bank Control;
- an Application to Become a Bank Holding Company and/or Acquire an Additional Bank or Bank Holding Company; and
- an Application for a Foreign Organization to Acquire a US Bank or Bank Holding Company.

All of these filings require a detailed description of the transaction as well as detailed financial and management information of the applicant and potential subsidiary or target company.

Law stated - 24 January 2022

Time frame for approval

What is the typical time frame for regulatory approval for both a domestic and a foreign acquirer?

In 2020, the average number of days for the FRB to approve mergers and acquisitions (M&A) proposals was 69 days. However, the FRB may receive adverse public comments with respect to an M&A proposal. This would likely increase the length of time that it takes to approve the merger as the FRB will allow the applicant the opportunity to respond to the comment, and then the FRB will evaluate both the comment and the applicant's response. In 2020, four proposals subject to adverse public comments were approved. The average processing time for proposals that received adverse public comments was 232 days versus an average of 64 days for proposals that did not receive adverse public comments.

Law stated - 24 January 2022

UPDATE AND TRENDS

Key developments of the past year

Are there any emerging trends or hot topics in banking regulation in your jurisdiction?

US financial regulators have devoted significant attention in recent years to fintech, including cryptoassets. For example, at the federal level, the Office of the Comptroller of the Currency (OCC) confirmed in November 2021 that national banks may provide cryptocurrency custody services and hold cryptographic keys on behalf of customers if they have adequate controls in place. In November 2021, the federal banking agencies issued a joint statement regarding a 'policy sprint' initiative focused on cryptoassets, in which they signalled future regulation or guidance focused on developing a commonly understood vocabulary that uses consistent terms regarding the use of cryptoassets by US banking organisations. The initiative also aimed at identifying and assessing key risks, analysing the applicability of existing regulations and guidance, and identifying areas that may benefit from additional clarification.

At the state level, in September 2020, the state of Wyoming issued its first special purpose depository institution charter to Kraken, the cryptocurrency exchange, allowing it to take deposits and provide custody for digital assets. Similarly, in May 2021, Nebraska passed a law that permits the grant of bank charters to digital asset depository institutions.

Under the Biden administration, there is expected to be greater consideration as to whether fintech should be subject to similar federal regulation as banks (for example, whether fintech companies engaged in substantial lending should be subject to regulation similar to the Community Reinvestment Act). The Biden administration may also bring notable changes to federal regulation and policy, especially with respect to:

- payment systems and their anti-money laundering obligations;
- third-party and customer access to financial records;
- cryptoassets; and
- bank mergers and acquisitions.

These changes have the potential to make it more difficult for larger banks to engage in the above activities.

At the state level, various states will likely continue to grapple with issues surrounding money transmission, data privacy and security, and universal cryptocurrency regulations.

The banking regulators also devoted significant attention in 2021 to the climate, which is widely anticipated to continue to be an area of focus going forward.

For example, the Financial Stability Oversight Council (FSOC) released its Report on Climate-Related Financial Risk, which assessed climate-related risks to US financial stability and proposed non-binding recommendations to FSOC member agencies to address climate-related financial risk. In December 2021, the OCC released draft principles to support the identification and management of climate-related financial risks by OCC-supervised large banks, which align closely with a similar set of principles released by the Basel Committee on Banking Supervision one month earlier. The OCC also announced the appointment of its first-ever Climate Change Risk Officer, who will chair the newly established Climate Risk Implementation Committee that is part of the OCC's National Risk Committee. The Federal Reserve Board announced that it is actively developing scenario analyses to model potential financial risks associated with climate change, and assess the resilience of individual financial institutions and the financial system to these risks. Finally, the Securities and Exchange Commission requested public input on climate change disclosures and is expected to issue a formal notice of proposed rule-making on such disclosures in 2022.

Law stated - 24 January 2022

Jurisdictions

Andorra	Cases & Lacambra
Australia	Piper Alderman
Ghana	Nobisfields
Greece	Zepos & Yannopoulos
Hungary	Nagy és Trócsányi
India	Shardul Amarchand Mangaldas & Co
Ireland	Dillon Eustace LLP
Israel	Tadmor Levy & Co
Italy	Ughi e Nunziante
Japan	TMI Associates
Lebanon	Abou Jaoude & Associates Law Firm
Luxembourg	Loyens & Loeff
Monaco	CMS Pasquier Ciulla Marquet Pastor Svara & Gazo
Singapore	WongPartnership LLP
South Africa	White & Case LLP
Sri Lanka	Tiruchelvam Associates
Switzerland	Lenz & Staehelin
United Kingdom	1 Crown Office Row
USA	Debevoise & Plimpton LLP