SPECTRUM
Asset Management

Dodd-Frank Act Changes

A Plus for Smaller Regional and Community Banks

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Yesterday President Trump signed S.2155 "The Economic Growth, Regulatory Relief & Consumer Protection Act" into law. This legislation recalibrates US bank regulation, and is the largest bank regulatory change since the Dodd-Frank Act (DFA) of 2010. That said, not much will change for the largest US bank groups; the brunt of the changes affect regional and community banks – especially the smaller banks in this group.

Key Features:

- Raises the Systemically Important Financial Institution (SIFI) threshold that triggers stricter regulatory oversight to $250 billion in assets, from $50 billion. However, the Federal Reserve can, at its discretion, apply "any prudential standard" to banks with >$100B in assets. It is entirely possible that the Fed will exercise this authority, the precise manner to be determined. In effect, Congress is telling the Fed: "You will not be required to apply enhanced prudential standards to the $100B to $250B asset group, but you can if you want to. It's your call." Therefore, regulatory expenses for the largest banks will not change, and might not change for smaller, albeit still large, banks.
- Banks with assets between $50B and $100B fall in the legislation's sweet spot. Their regulatory burden is reduced, and banks just below the former $50B SIFI cut-off – and hesitant to cross it – are now more likely to engage in M&A to grow. This could be one of the more prominent effects of the legislation.
- Custody banks (Bank of New York Mellon, State Street and Northern Trust) have their leverage rules eased slightly, by exempting certain deposits at central banks from their leverage calculation.
- High quality municipal securities will be counted as liquid assets, thereby easing liquidity rules.
- Banks with less than $10B in assets are exempted from the Volcker Rule, which bans proprietary trading and certain types of investments. In addition, regulators must establish a community bank leverage ratio rule between 8% and 10%. If a community bank exceeds such ratio it would be deemed compliant with capital and leverage requirements. This would eliminate significant regulatory cost.

Spectrum views this legislation as a plus for regional – especially smaller regional – and community banks, the degree of which depending on the Fed's approach to regulating banks between $100B and $250B in assets. The benefit stems from lower regulatory costs. That said, there is no substantive shift in banks' prudential standards, and the protective approaches which have been put in place post-Crisis remain, thereby supporting banks' creditworthiness.

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