

Federal Agencies Clarify Method of Determining Institutions Subject to CFPB's Supervision and Enforcement Jurisdiction

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On November 17, 2011, the Federal Deposit Insurance Corporation ("FDIC"), Federal Reserve Board ("FRB"), Office of the Comptroller of the Currency ("OCC"), and National Credit Union Administration ("NCUA") (collectively, the federal banking agencies), along with the Bureau of Consumer Financial Protection ("CFPB") (collectively, the "Agencies"), issued a Supervisory Statement regarding how the Agencies will calculate the total assets of an insured depository institution or an insured credit union for determining which institutions will be subject to their supervision and enforcement authority with respect to Federal consumer financial law.¹ The statement is primarily intended to eliminate uncertainty for institutions regarding the identity of their primary supervisor under Sections 1025 and 1026 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("DFA").

Background

DFA Sections 1025 and 1026 divide the supervisory and enforcement responsibilities among the Agencies with respect to insured depository institutions and insured credit unions that are engaged in offering or providing a consumer financial product or service for purposes of Federal consumer financial law.² Under DFA Section 1025, the CFPB has exclusive supervisory authority and primary supervisory authority over insured depository institutions and insured credit unions with total assets of more than \$10 billion and their affiliates.³ DFA Section 1026 provides that the federal banking agencies retain supervisory and enforcement authority for purposes of Federal consumer financial law with respect to insured institutions and insured credit unions below the \$10 billion threshold. The Dodd-Frank Act does not, however, specify the method or the appropriate time frame for determining an institution's total asset size for purposes of these provisions. Accordingly, the Agencies have issued a supervisory statement "to provide clarity and transparency" on how and when the Agencies will determine the total assets of an insured institution or insured credit union for purposes of their supervisory and enforcement responsibilities under the DFA.

In issuing the guidance, the Agencies recognized that a common measure for determining asset size is necessary to establish clear expectations for both the Agencies and the institutions they regulate so as to reduce uncertainty regarding the primary regulator or supervisor. In addition, the Agencies acknowledged that for institutions with assets close to the \$10 billion threshold, their asset size may fluctuate over time, and that frequent periodic assessments or measures of an institution's asset size

would impose increased regulatory burden on these institutions from shifts in the principal supervisor as well as potential issues regarding coordination of supervisory and enforcement responsibilities between the Agencies.

Overview of guidance

Method of Calculating Total Asset Size

In identifying possible measures for determining asset size, the Agencies focused on existing measures used for other purposes. The most common metric used for determining asset size today is the total assets reported by institutions in their quarterly reports of condition, or Call Reports, which are required to be filed pursuant to Section 7(a)(3) of the Federal Deposit Insurance Act for insured depository institutions, and pursuant to 12 CFR 641.6(a)(2) for insured credit unions. Thus, the Agencies concluded that it is appropriate to use Call Report data in determining an institution's asset size for purposes of determining Agency supervisory and enforcement responsibilities under DFA Sections 1025 and 1026.

Time Period for Determining Asset Size

To limit the potential for uncertainty or short-term volatility regarding the identity of an institution's primary supervisor with respect to Federal consumer financial law, the Agencies determined that the current method used by the FDIC for deposit insurance assessments would be similarly appropriate for purposes of DFA Sections 1025 and 1026. Accordingly, in adapting the FDIC's methodology for deposit insurance assessments for use in the asset size determination, the Agencies will reclassify for the following quarter, an insured institution or credit union as a large institution subject to the CFPB's supervisory and enforcement authority if the institution reports assets exceeding \$10 billion in its quarterly Call Report for four consecutive quarters. Thus, beginning with the June 30, 2011 Call Report data (representing the reporting date closest to the designated transfer date for the CFPB of July 21, 2011), the Agencies will look to that Call Report data for determining the appropriate initial regulator for purposes of DFA Sections 1025 and 1026. As a result:

- Institutions or credit unions that have total assets of less than \$10 billion as of June 30, 2011 will not become large institutions subject to the CFPB's supervisory and enforcement jurisdiction under DFA Section 1025 until they report total assets exceeding \$10 billion in their quarterly Call Report for four consecutive quarters; and
- Similarly, an institution or credit union determined to be a large institution as of June 30, 2011, will not cease to be a large institution for purposes of the CFPB's jurisdiction under DFA Section 1025 until it reports total assets of \$10 billion or less in its quarterly Call Report for four consecutive quarters.
- In the case of an acquisition, merger, or combination occurring after June 30, 2011, where each of the entities to be combined has total assets of \$10 billion or less before the transaction, the Agencies will look to the combined assets of each of the constituent entities prior to the transaction to determine if the resulting institution is a large institution.

Illustrative Examples

To illustrate the Agencies' methodology, the Supervisory Statement includes several examples:

- An institution with total assets exceeding \$10 billion as of June 30, 2011 that subsequently reports total assets below \$10 billion in four consecutive quarterly Call

reports (September 30, 2011, December 31, 2011, March 31, 2012, and June 30, 2012), would no longer be deemed a large institution subject to the CFPB's supervisory and enforcement authority with respect to Federal consumer financial law after July 1, 2012 (and thereafter would have the benefit of four consecutive quarters in such status).

- An institution with total assets of \$10 billion or less as of June 30, 2011 that subsequently reports total assets exceeding \$10 billion in four consecutive quarters would become subject to the CFPB's supervisory and enforcement authority as a large institution with respect to Federal consumer financial law beginning July 1, 2012 (and thereafter be deemed a large institution for at least the next four quarters).
- In the case of two institutions merging where neither constituent institution has total assets of greater than \$10 billion, the resulting institution generally would be subject to the CFPB's supervisory and enforcement authority with respect to Federal consumer financial law beginning in the first full quarter after the merger is consummated if the combined total assets reported by the two institutions is more than \$10 billion in each of the four consecutive quarterly Call Reports prior to the merger. However, if the combined total assets reported by the two institutions is not more than \$10 billion in each of the four consecutive quarterly Call Reports prior to the merger, the resulting institution would not be subject to the CFPB's supervisory and enforcement authority as a large institution with respect to Federal consumer financial law, unless and until the resulting institution reports total assets of greater than \$10 billion in its quarterly Call Report for four consecutive quarters.

Conclusion

While the CFPB has already deployed examiners to the largest institutions with total asset sizes that are well in excess of \$10 billion for the first round of on-site examinations, the Agencies' Supervisory Statement should assist those institutions with asset sizes close to the \$10 billion threshold in determining the circumstances under which they will become subject to the CFPB's supervisory and examination authority with respect to Federal consumer financial law.⁴ The guidance should significantly reduce the difficulty that such institutions might otherwise have in identifying their appropriate regulator as a result of fluctuating changes in their assets. From a prudential regulatory perspective, application of a common asset size measure based on existing agency precedents allows the Agencies to more clearly demarcate their supervisory and enforcement responsibilities with respect to regulated institutions and effectively communicate their supervisory expectations to the institutions under their jurisdiction, while reducing the potential for supervisory arbitrage.



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¹ The Supervisory Statement can be found at:

<http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20111117a1.pdf>.

² "Federal consumer financial law" is defined under DFA Section 1002(14), and includes the enumerated consumer laws in DFA Section 1002(12), consumer financial protection laws transferred to the CFPB from other federal agencies, and new rulewriting authorities granted to the CFPB under the DFA, such as its authority to issue rules addressing unfair, deceptive, or abusive acts or practices. Federal consumer financial law excludes the Federal Trade Commission Act. On July 21, 2011, the CFPB published in the Federal Register a list of rules and orders that transferred to the CFPB from the federal banking agencies, the Federal Trade Commission, and the Department of Housing and Urban Development on that date. See 76 Fed. Reg. 43569 (July 21, 2011).

³ For a general overview of the CFPB's large bank supervision program, please see our article "CFPB Initiates Large Bank Supervision Program," Stay Current alert (July 2011), available at <http://www.paulhastings.com/publicationDetail.aspx?PublicationId=1962>. On October 13, 2011, the CFPB released version 1.0 of its Supervision and Examination Manual which will guide its examiners in their oversight of the institutions that will be subject to its jurisdiction. The manual contains more than 500 pages of policies, procedures, and protocol for examining and assessing risks posed by, and compliance of consumer financial products and services with, federal consumer protection laws. In large measure, the manual incorporates examination procedures used by other federal regulators to assess compliance with existing federal consumer protection law. The manual also includes a risk assessment module to help examiners identify the risks posed to consumers arising from the activities or business of the regulated entity. A copy of the manual can be found at: http://www.consumerfinance.gov/wp-content/themes/cfpb_theme/images/supervision_examination_manual_11211.pdf.

⁴ The CFPB has announced that it intends to examine the largest of the large banks on a continuing basis, and other large banks periodically. See "A Guide to the CFPB's Supervision," CFPB press release (October 13, 2011), available at www.consumerfinance.gov/guide/cfpb-supervision/.