

## Financial Regulatory Reform: Coming Soon

In the immortal words of the Johnny Cash in his legendary Folsom Prison Blues, "I hear the train a comin' . . . ." From key players on both sides of the aisle as well as from 1600 Pennsylvania Avenue, a consistent message is being sent – Federal Financial Regulatory Reform is coming and many predict it will come sooner than later.

The financial industry and its institutions have been both hit hard by and blamed frequently for the 2008 financial crisis and the resulting aftershocks. Accordingly, Washington has been working for the last two years to craft a legislative response to one of the greatest economic turmoils of this country's history. While there have been bi-partisan efforts that have appeared very close to producing a proposal with consensus along the way, the progress of Financial Regulatory Reform has suffered from spotlight-stealing topics of bailouts and health care reform as well as the political fallout created by each. In addition to hours of study, hard work and negotiations already logged, it seems that health care reform passage has freed-up policy-makers' attention and provided momentum toward finalizing a Financial Regulatory Reform package that is pass-able.

As such, U.S. Senator Chris Dodd, chairman of the Senate Banking, Housing and Urban Affairs Committee, released the second version of his comprehensive financial regulatory reform bill titled, "Restoring American Financial Stability Act of 2010" (the "Bill"). The Bill has since been voted out of committee, albeit strictly along party lines, and now will be debated by the full Senate.

U.S. Senator Bob Corker, a member of the Senate Banking, Housing, and Urban Affairs Committee, addressed the Bill and overarching Financial Regulatory Reform before a group of financial industry leaders at a session held at Vanderbilt's Owen School on Wednesday, March 31, 2010. He reiterated his belief that reform is coming soon and provided insight on what significant provisions in the legislation to watch during its final negotiations: (1) new Consumer Protection Agency and coordination with existing regulatory authorities; (2) Too-Big-To-Fail vs. Bankruptcy as default mechanism; and (3) Derivative Regulation.

In addition to the issues highlighted by Senator Corker, the Bill contains other sweeping changes to financial institutions, corporate governance, executive compensation and Regulation D. Below are the headline items with respect to each sector:

### I. Financial Institutions:

- Federal Reserve. Under the Bill, the Federal Reserve would become the home agency of a new consumer financial watchdog, gain break-up power over financial firms, and have supervision authority over bank holding companies with over \$50 billion in assets. Additionally, the Federal Reserve would be required to establish standards making it an unsafe and unsound practice for the holding companies of depository institutions to provide an employee, director or principal shareholder with compensation that is excessive or could lead to material financial loss to the bank holding company. It would lose its supervision, however, of state-chartered banks with less than \$50 billion in assets with all but the largest state-chartered banks being transferred to the Federal Deposit Insurance Corporation's oversight.
- Too Big to Fail. The Bill would heighten capital, leverage and liquidity requirements

for large financial institutions and require such financial institutions to prepare and submit contingency plans for an orderly shutdown.

- Consumer Financial Protection Bureau. The Bill would create a Consumer Financial Protection Bureau with a mandate to protect consumers from harmful lending practices.
- Credit Ratings. The Bill would create an agency to regulate rating agencies.

## II. Corporate Governance:

- Proxy Access. The Bill would grant, under Section 14(a) of the Exchange Act, the SEC power to adopt rules and regulations relating to proxy access. Additionally, the SEC would be granted authority to determine the procedure an issuer must follow when responding to shareholder director nominations.
- Majority Voting. The Bill would add a Section 14B to the Exchange Act, which would require, as a listing requirement on the national exchanges, that a director must receive a majority of the votes cast in an uncontested election to be elected director.
- Whistleblower. Section 922 of the Bill would allow the SEC to award whistleblowers between 10 and 30 percent of any monetary sanctions imposed and collected on any successful action whereby such whistleblower provided the SEC with original information leading to such action.

## III. Executive Compensation:

- Say-On-Pay. As proposed, the Bill would require public companies to give shareholders a separate non-binding vote on all executive compensation disclosed in the company's proxy statement.
- Executive Pay in Relation to Company Performance. Section 953 of the Bill would require the SEC to adopt rules that require a public company to disclose in its annual proxy statement the relationship between the compensation actually paid to an executive and the company's financial performance. The company's financial performance should include any change in the value of the company's stock, dividends and other distributions.
- Compensation Committee Independence. Under the Bill, it would become a listing requirement that all members of a company's compensation committee and their consultants be independent.
- Clawback Policies. Section 954 of the Bill would require the SEC to adopt rules prohibiting the listing on a national securities exchange of companies that do not adopt a clawback policy with respect to incentive-based compensation (including stock options) paid to executives. Such policies would require the company to recover incentive-based compensation received by an executive during the three-year period preceding an accounting restatement in excess of the incentive-based compensation that would have been paid to such executive under the accounting restatement. These clawback policies will apply to all incentive-based compensation received by all company executives.
- Disclosure of Hedging Activities. The Bill would required companies to disclose in their proxy statements whether any employee or director is permitted to purchase financial instruments that are designed to hedge or offset any decrease in the market value of equity securities that are granted to such person by the company as part of compensation or held, directly or indirectly, by such person.

## IV. Regulation D:

- Accredited Investors. The Bill would raise the threshold for individuals to be considered an "accredited investor." Specifically, an individual must have a net worth of at least \$2.3 million or an annual income at least \$450,000 to be deemed an accredited investor. It should be noted that U.S. Senator Herb Kohl is proposing

an amendment to the Bill which would reduce the threshold.

- Covered Securities. Section 926 of the Bill would require the SEC to review and presumably approve any filing made with regard to a Rule 506 offering within 120 days of such filing. In the event the SEC fails to review such filing within 120 days, the securities will not be considered “covered securities” exempt from state regulation unless the SEC separately finds that the issuer made a good-faith and reasonable attempt to comply with applicable rules and regulations, and any failure to comply therewith is immaterial to the offering as a whole.
- Disqualification. The Bill would authorize the SEC to designate a class of securities as not covered by registration exemptions because the offering is not sufficient in size or scope.

If you have any questions relating to this alert or any other matter related to Financial Regulation, please feel free to contact any member of the [Financial Institutions Practice Group](#) or Corporate Department at Miller & Martin, PLLC.

*The opinions expressed in this bulletin are intended for general guidance only. They are not intended as recommendations for specific situations. As always, readers should consult a qualified attorney for specific legal guidance. Should you need assistance from a Miller & Martin attorney, please call 1-800-275-7303.*

Atlanta | Chattanooga | Nashville  
[www.millermartin.com](http://www.millermartin.com)

**ATLANTA**

1170 Peachtree Street,  
N.E., Suite 800  
Atlanta, GA 30309-7706

**CHATTANOOGA**

832 Georgia Avenue,  
Suite 1000,  
Volunteer Building  
Chattanooga, TN 37402-2289

**NASHVILLE**

150 Fourth Avenue North,  
Suite 1200, One Nashville Place  
Nashville, TN 37219