Memorandum

Dodd-Frank Reconsidered: The Financial CHOICE Act 2.0

April 26, 2017

On April 26, 2017, the House Financial Services Committee held hearings on the Financial CHOICE Act, a proposal that aims to reverse many features of the landmark Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank"). The bill—sometimes referred to as the "CHOICE Act 2.0"—is the second version of a reform bill that was introduced last summer by Committee Chairman Jeb Hensarling (R-TX).

The CHOICE Act 2.0 would not repeal Dodd-Frank in its entirety, but it would make targeted changes to many of the most controversial aspects of Dodd-Frank. Significantly, it would repeal the Volcker Rule, the Durbin Amendment and the authority of the Financial Stability Oversight Council to designate non-bank firms as systemically important, as well as the "orderly liquidation authority" in Title II of Dodd-Frank (which would be replaced by new Bankruptcy Code provisions). The bill would also retain the signature "off-ramp" concept from the original bill, which would exempt qualifying banking organizations from a number of capital, liquidity and other enhanced prudential supervision requirements.

The CHOICE Act 2.0 would also address a variety of other capital markets and corporate governance matters, repeal the *Chevron* doctrine of judicial deference to agency rule-making and interpretation, and introduce a new procedure requiring affirmative Congressional approval for "major" rule-makings and providing Congress the ability to vote to block other rule-makings.

Passage of the bill is uncertain, and it is likely that significant changes will be made, including during the Committee's markup process, which is expected to commence in early May. The final terms of the bill will likely also be affected by the report regarding possible modifications to financial services regulations that the Treasury Department is required to finish by early June pursuant to President Trump's February 3 executive order.

This memorandum provides a high-level summary of certain key features of the CHOICE Act 2.0.

Volcker Rule

The Volcker Rule, arguably one of the most controversial aspects of Dodd-Frank, would be repealed in its entirety. Under the bill, the rule would be treated "as if . . . [it] had not been enacted."

"Off-Ramp" Relief For Qualifying Banking Organizations

- **Election for "Off-Ramp" Relief**. The bill would allow a qualifying banking organization ("QBO") to elect to be exempt from risk-weighted capital requirements, liquidity requirements and a variety of other regulations if the QBO maintains an average non-risk weighted leverage ratio of at least 10%. For banking organizations other than "traditional banking organizations" (which have no trading assets or liabilities and not more than $8 billion notional amount of interest rate and foreign exchange swaps), this leverage ratio calculation would include off-balance sheet as well as on-balance sheet assets (calculated in the same manner as used by advanced approaches banks to calculate their leverage exposure under the existing Basel III capital rules). For a depository institution holding company making such an election, each of the holding company's depository institution subsidiaries must make the same election. While the CHOICE Act 1.0 would have required a QBO to have a composite CAMELS rating of 1 or 2 at the time of the election, the CHOICE Act 2.0 eliminated this CAMELS rating component for QBOs.
    - If a banking organization that has made a qualifying capital election fails to maintain a 10% leverage ratio for the most recently completed calendar quarter, the banking organization will be: (1) prohibited from making a capital distribution if its primary federal regulator objects to such distribution; (2) required to submit a capital restoration plan to its primary federal regulator within three months; and (3) required to restore its leverage ratio to at least 10% within one year.
    - If a banking organization fails to restore its leverage ratio to at least 10% within one year, then the banking organization will lose all regulatory relief. In addition, if a banking organization that has made a qualifying capital election fails to maintain a 6% leverage ratio, then the banking organization will immediately lose all regulatory relief.

  The term "banking organization" for purposes of the CHOICE Act 2.0 off-ramp would include an insured depository institution, a depository institution holding company, a foreign banking organization that is treated as U.S. bank holding company under the International Banking Act (by virtue of maintaining a U.S. branch or agency or controlling a U.S. commercial lending company) and a U.S. intermediate holding company of a foreign banking organization.

- **Regulatory Relief Following "Off-Ramp" Election**. A banking organization making a qualifying capital election would be exempt from any federal law or regulation:
    - addressing capital or liquidity requirements and standards (including all capital and

liquidity standards developed by the Basel Committee);

- permitting a federal banking agency to block a capital distribution by the banking organization (including rules permitting the Federal Reserve to block a capital distribution if the Federal Reserve objects to an organization's CCAR capital plan);
- permitting a federal banking agency to consider the risk to the stability of the U.S. banking or financial system (a standard added to various federal banking laws by Section 604 of Dodd-Frank) when reviewing an application to consummate an acquisition or commence an activity;
- providing limitations on mergers, consolidations or acquisitions of assets or control, to the extent the limitations relate to capital or liquidity standards or concentrations of deposits or assets; or
- implementing the "enhanced prudential standards" provisions of Dodd-Frank (to the extent not already covered by the above), including the governance and stress testing requirements, resolution planning requirements, single-counterparty credit limits and short-term debt limits.

A QBO would also be exempt from the Federal Reserve's authority under Dodd-Frank to set more stringent prudential standards for bank holding companies. In addition, a QBO would be exempt from any prior notice requirement under Section 163 of Dodd-Frank, which currently requires a bank holding company with assets of $50 billion or more to notify the Federal Reserve prior to acquiring ownership of any voting shares of a company (other than an insured depository institution) that is engaged in financial activities and that has assets of $10 billion or more.

CCAR and Stress Testing

For banking organizations that are not QBOs, the bill would make several changes to the CCAR and stress testing process.

- Only an annual company-run stress test would be required (mid-term stress tests would be eliminated).
- CCAR would change from an annual cycle to a two-year cycle.
- The Federal Reserve would be prohibited from objecting to a capital plan on the basis of qualitative deficiencies in a banking organization's capital planning process.
- The Federal Reserve would be required to have procedures for responding to inquiries from banking organizations subject to CCAR, including procedures for establishing a time frame in which such responses will be made.

Living Wills

Section 165(d) of Dodd-Frank requires certain financial institutions to submit resolution plans, or "living wills," to the Federal Reserve and the FDIC, which have joint authority to review and determine whether such plans are credible. Under the bill, the FDIC's role in evaluating living wills would be eliminated. The bill also makes changes to the submission and review procedures for living wills. Bank holding companies subject to resolution planning requirements would need to submit living wills only once every two years. In addition, the Federal Reserve would be required to review and provide feedback within six months of receiving a living will, and it would also have to disclose the framework used to assess the adequacy of living wills.

"Too Big to Fail" and Bank "Bailout" Related Provisions

- **Repeal of Orderly Liquidation Authority**. Title II of Dodd-Frank, which established a framework for the resolution of systemically important financial companies and gave the FDIC expanded resolution powers, would be repealed in its entirety. In its place, there would be a new subchapter of the Bankruptcy Code specifically designed to address the failure of large, complex financial institutions.

- **Curtailment of Emergency Authorities**. The bill would further curtail the Federal Reserve's emergency lending authority under Section 13(3) of the Federal Reserve Act. In addition, it would eliminate the FDIC's authority to establish a "widely available" guarantee program during times of severe economic distress, prohibit the use of the Exchange Stabilization Fund to establish a guarantee program for any nongovernmental entity, and repeal the "systemic risk" exception to the requirement that the FDIC resolve insured depository institutions on a "least cost" basis.

Financial Stability Oversight Council and Related Changes

- **Non-Bank SIFI Designation Authority Repealed**. The authority of the Financial Stability Oversight Council ("FSOC") to designate non-bank financial companies as systemically important financial institutions ("SIFIs") would be repealed retroactively. The bill also would retroactively repeal all designations of certain payments and clearing organizations as systemically important financial market utilities ("FMU").
    - The bill would also repeal Dodd-Frank's "Hotel California" provision, originally aimed at Goldman Sachs and Morgan Stanley, which provides that any company that was a bank holding company with more than $50 billion of assets as of January 1, 2010 and that received TARP assistance will be treated as a non-bank financial company supervised by the Federal Reserve even if the company subsequently ceases to be a bank holding company.

- **Non-Bank SIFI Supervision Authority Repealed**. In connection with the repeal of the FSOC's authority to make systemic risk designations, the bill would strip the Federal Reserve of its

authority to supervise and set regulations for designated non-bank financial companies. The bill would also repeal the application of several restrictions to such non-bank financial companies, including:

- management interlock restrictions;
- Section 163 of Dodd-Frank, which requires prior notice to the Federal Reserve for the acquisition of shares of any company with assets of $10 billion or more that is engaged in financial activities; and
- Section 14 of the Bank Holding Company Act, which was added by Section 622 of Dodd-Frank and restricts "financial companies" (including non-bank financial companies supervised by the Federal Reserve) from engaging in certain M&A transactions if the total consolidated liabilities of the acquirer would, on a pro forma basis, exceed 10% of the aggregate consolidated financial sector liabilities.

In addition, the bill would repeal the Federal Reserve's authority under Section 121 of Dodd-Frank to limit M&A activity, impose restrictions on product offerings or terminate certain activities of a bank holding company with assets of $50 billion or more, or a non-bank financial company subject to Federal Reserve supervision, on the basis that such institution poses a "grave threat" to U.S. financial stability.

- **Less Authority, More Transparency and Other Changes**. The FSOC itself would not be eliminated, but it would be substantially weakened. In addition to no longer being able to make non-bank SIFI and FMU designations, its authority to recommend enhanced prudential standards and reporting and disclosure requirements for large, interconnected bank holding companies would be repealed. It would also be subject to heightened transparency and open-meeting requirements, as well as limited funding ($4 million for fiscal year 2017, for example) subject to the Congressional appropriations process. Its membership would be broadened to include each member of the Federal Reserve Board, the FDIC, the SEC and the CFTC, among others. The FSOC would no longer benefit from any research or studies of the Office of Financial Research, which would be eliminated.

Consumer Financial Protection Bureau

- **Restructuring**. The Consumer Financial Protection Bureau ("CFPB") would be restructured, from an independent bureau within the Federal Reserve System to an executive agency, and renamed the Consumer Law Enforcement Agency ("CLEA"). The CLEA's Director and Deputy Director would be appointees removable by the President at will. Funding would be subject to the Congressional appropriations process (in contrast, the CFPB is currently funded out of earnings of the Federal Reserve System).

- **A More Limited Mandate**. The CLEA would have significantly less authority than the CFPB has under current law.
  - In a significant break with the CFPB's current mandate, the CLEA would not have supervision authority.
  - Its authority to prescribe rules to implement federal consumer protection laws would be limited in several ways, including by requiring the CLEA to consider the impact of a proposed rule on the financial safety and soundness of an insured depository institution.
  - Before initiating any administrative enforcement actions or civil lawsuits or entering into a consent order, the CLEA would be required to consider a cost-benefit analysis of such actions.
  - The CLEA would have no authority exercise any rulemaking, enforcement or other authority with respect to payday loans, vehicle title loans or other similar small-dollar loans.
  - The CLEA would have no authority to take any action against unfair, deceptive or abusive acts and practices, so-called "UDAAP" authority. Instead, the bill would transfer the authority to prevent unfair or deceptive acts or practices—so-called "UDAP" authority—by depository institutions back to the federal banking regulators.
- **Auto Lending Guidance and Arbitration Matters**. The CFPB's prior indirect auto lending guidance (Bulletin 2013-02) would be nullified. In addition, the CFPB's authority to restrict pre-dispute arbitration would be repealed.
- **Advisory Opinions**. The bill would establish an advisory opinion procedure whereby inquiries could be made concerning the conformance of specific conduct with federal consumer financial laws. The Director would generally be required to respond within 90 days of a request for an opinion.

Securitization Risk Retention Requirements

The bill would remove the risk retention requirement mandated by Section 941 of Dodd-Frank, which generally requires sponsors of asset-backed securities ("ABS") to retain at least 5% of the credit risk relating to the assets that underlie such asset-backed securities, for all ABS securitizations *other than* non-qualified residential mortgage securitizations.

Mortgage and Other Financing Related Reforms

- **Codification of "Valid When Made" Doctrine**. The bill would provide that a loan that complies with applicable usury limits when *made* will remain valid with respect to its interest rate regardless of whether the loan is *subsequently* sold or transferred, and may be enforced by the buyer or transferee notwithstanding any state law to the contrary. This would essentially invalidate

the ruling in *Madden v. Midland Funding, LLC*, which held that a non-bank entity taking assignment of debts originated by a national bank is not entitled to protection under the National Bank Act from usury claims under state law.

- **Mortgage Lending on Manufactured Housing**. The bill would clarify that a retailer of a manufactured home is not a "mortgage originator" for purposes of the Truth in Lending Act ("TILA") unless the retailer receives compensation for engaging in mortgage loan application or negotiation activities. The bill would also amend the definition of a "high-cost mortgage" for purposes of the Home Ownership and Equity Protection Act by modifying the interest rate and points-and-fees thresholds with respect to manufactured housing mortgages. In particular, the bill would increase the maximum loan amount for "high cost" manufactured housing mortgages from $50,000 to $75,000, increase the interest rate threshold for "high cost" manufactured housing mortgages from 8.5% to 10% over the average prime rate, and add a points-and-fees threshold of 5% or $3,000 (whichever is greater) with respect to manufactured housing mortgages of less than $75,000.
- **Points and Fees Included in "High-Cost Mortgage" Calculation**. The bill would modify the calculation of points and fees for purposes of the "high-cost mortgage" rule by excluding escrow charges for insurance and fees retained by a creditor or its affiliate in connection with an affiliated business transaction.
- **More Flexible Lending Standards for Non-Qualified Mortgages**. The bill would create a safe harbor from TILA's "ability to repay" requirements, homeownership counseling requirements and prohibition against prepayment penalties for non-qualified mortgage loans that are kept on a depository institution's balance sheet and that comply with the prepayment penalty limitations applicable to qualified mortgages. The bill would also allow mortgage loan originators to steer customers from a qualified mortgage to a non-qualified mortgage if the lender is a depository institution and has informed the mortgage originator that it intends to hold the loan on its balance sheet for the life of the loan.
- **Small Bank Mortgage Lending Compliance Relief**. For any mortgage lender with $10 billion or less in total assets, the bill would create a safe harbor from TILA's requirement that a mortgage lender establish an escrow account for the payment of taxes and insurance premiums prior to the closing of a mortgage loan, provided that the mortgage lender holds the loan on its balance sheet for a three-year period beginning on the date of the origination of the loan. The bill also would require the CLEA to provide regulatory exemptions from certain escrow requirements under the Real Estate Settlement Procedures Act for mortgage loan services that service 20,000 or fewer mortgage loans annually.
- **Transitional Mortgage Loan Licensing**. For registered loan originators who were employees of a depository institution and transition to a non-bank state-licensed mortgage company, the bill

would provide a 120-day grace period from state licensing requirements applicable to loan originators.

- **Loan and Borrower Reporting Requirements**. The bill would exempt a depository institution from the Home Mortgage Disclosure Act reporting and recordkeeping requirements with respect to closed-end mortgage loans and open-end lines of credit if the depository institution originated less than 100 of such mortgage loans and less than 200 of such lines of credit in each of the two preceding years. The bill would also repeal the recordkeeping requirements under the Equal Credit Opportunity Act with respect to women-owned, minority-owned and small businesses.

Other Key Bank Regulatory Reforms

- **Durbin Amendment**. Dodd-Frank's Durbin Amendment, which set price controls for interchange fees on debit card transactions, would be repealed entirely.
- **Small Bank Holding Company Policy Statement**. The bill would require the Federal Reserve to increase the asset threshold for application of its Small Bank Holding Company Policy Statement from $1 billion to $5 billion, thereby permitting a greater number of community banking institutions to finance the acquisition of banks or other companies with debt levels higher than would be permitted for larger holding companies.
- **Customer Account Closures**. The bill would prohibit a federal banking agency from formally or informally requesting or ordering a depository institution to terminate customer accounts, or otherwise restricting depository institutions from maintaining a banking relationship with a customer, unless the agency has a material reason, based on something other than reputational risk, to do so. This provision is in response to the Department of Justice's "Operation Choke Point," in which the DOJ reportedly applied pressure to financial institutions to restrict financial services to customers in particular industries.
- **Bank Exam Reform**. The bill would reform the examination process for financial institutions by requiring the federal banking agencies to issue timely final examination reports, conduct timely exit interviews following an examination, and provide supporting information for any material supervisory determination upon request. The bill would also create a new "Office of Independent Examination Review" with the authority to conduct independent reviews of the examination practices, reports and supervisory determinations of the federal banking agencies.
- **Federal Savings Association Charter Flexibility**. The bill would allow federal savings associations to elect, upon 60 days' prior notice to the OCC, to be subject to the same rights, privileges, duties and restrictions as a national bank. This would seem to exempt electing federal savings associations from, among other things, certain asset-based limitations such as those

applicable to a federal savings association's holdings of commercial and consumer loans, unsecured construction loans, and non-residential real property loans.

Incentive-Based Compensation Requirements

The bill would repeal Section 956 of Dodd-Frank, which requires the major banking and financial regulators to jointly issue regulations or guidelines that prohibit certain kinds of incentive-based payment arrangements by financial institutions (broadly defined to include banking organizations, broker-dealers and investment advisers) that have $1 billion or more in assets. In April 2016, the banking and financial regulators had re-proposed incentive-based compensation rules to implement Section 956 of Dodd-Frank, more than five years after the rules were initially proposed. Regardless of whether the CHOICE Act 2.0 is ultimately enacted, it seems unlikely that such incentive-based compensation rules will become effective.

Investment Management and Advisory Related Reforms

- **DOL Fiduciary Rule**. The bill would repeal the fiduciary rule finalized by the Department of Labor ("DOL") in April 2016, which expanded the scope of financial service providers treated as fiduciaries under both the Employee Retirement Income Security Act of 1974 and Section 4975 of the Internal Revenue Code by reason of providing investment advice to retirement plans and individual retirement accounts.
    - The bill would further restrict the DOL from issuing any other similar regulations until at least two months after the SEC issues a final rule relating to the standards of conduct for brokers, dealers and investment advisers pursuant to Section 913 of Dodd-Frank. Any DOL rule issued after this two-month period would need to be substantially identical to the SEC's rule regarding what constitutes fiduciary investment advice, and impose standards of care on fiduciaries substantially identical to those imposed by the SEC on brokers, dealers or investment advisers.
    - Before the SEC would be permitted to issue a final rule to implement Section 913 of Dodd-Frank, the bill would require the SEC to report to the House Financial Services Committee and Senate Banking Committee regarding the impact that a uniform fiduciary standard for brokers, dealers and investment advisers would have on retail investors and their access to personalized and cost-effective investment advice.
- **Private Equity Fund Adviser Exemption**. The bill would exempt investment advisers to private equity funds from registration under the Investment Advisers Act of 1940, at least with respect to the provision of advisory services to private equity funds, which registration obligation was largely a result of Dodd-Frank. In connection with that exemption, the SEC would be required to adopt rules that would define the term "private equity fund" for these purposes and require advisers to such funds to adhere to limited recordkeeping and reporting requirements. Given the

expansion of business lines by many private equity firms, among other factors, it is unclear if the exemption from registration would significantly reduce the number of SEC-registered private equity advisory firms.

- **Expansion of BDC Authority**. The bill would amend the Investment Company Act of 1940 (the "1940 Act") to significantly expand the range of eligible investments for business development companies ("BDCs") and allow BDCs to increase leverage beyond current statutory limits if certain conditions are met. The bill would also lift a 1940 Act restriction on investments in registered investment advisers by BDCs. Additionally, BDCs would be allowed to invest up to 50% of their assets in companies relying on certain exemptions from the definition of "investment company" under the 1940 Act, including finance companies, banks and financial intermediaries. The bill includes a variety of other measures that would facilitate offerings including by eliminating the exclusion of BDCs from the definition of "well-known seasoned issuer."

SEC Reporting and Governance Reforms

- **Shareholder Thresholds for Registration and Deregistration**. The bill would promote private company flexibility and growth by amending the shareholder thresholds for registration and deregistration under the Exchange Act.
  - *Section 12(g) of the Exchange Act.* Currently, companies must register under Section 12(g) if they have over $10 million in assets and either at least 2,000 holders of record or 500 holders of record that are not accredited investors. The bill directs the SEC to index the $10 million dollar figure for inflation every 5 years and strikes the 500 holders registration requirement. The bill would also allow deregistration under Section 12(g) if the issuer files a certification that its holders of record are reduced to less than 1,200 persons, as opposed to the current 300 person threshold.
  - *Section 15(d) of the Exchange Act.* Currently, companies are required to file periodic reports with the SEC if they have an effective registration statement pursuant to the Securities Act. The duty to file is automatically suspended if the securities to which the registration statement relates are held of record by fewer than 300 persons. The bill would amend this threshold to 1,200 persons.
- **Shareholder Proposals**. The bill includes a number of provisions related to shareholder proposals, including:
  - *Eligibility to Submit a Shareholder Proposal.* Under Exchange Act Rule 14a-8, a shareholder is eligible to submit a shareholder proposal for inclusion in the company's proxy materials if such shareholder has "continuously held at least $2,000 in market value, or 1%, of the company's securities entitled to be voted on the proposal at the meeting for at

least one year" by the date the shareholder submitted the proposal. The bill would eliminate the option to satisfy the holding requirement by holding a fixed dollar amount and instead require that the shareholder hold at least one percent of the company's securities entitled to be voted on the proposal or such greater percentage as the SEC may determine. The bill would also increase the holding period requirement from one year to three years.

- *Shareholder Proposal Resubmission Thresholds*. Under Rule 14a-8, if a shareholder proposal relates to substantially the same subject matter as a proposal included in the issuer's proxy materials within the previous five calendar years, it may be excluded from the company's proxy materials for any meeting held within three calendar years of the last time it was included, if the proposal received (1) less than 3% of the vote if proposed once within the preceding five calendar years; (2) less than 6% of the vote on its last submission to shareholders if proposed twice previously within the preceding five calendar years; or (3) less than 10% of the vote on its last submission to shareholders if proposed three times or more within the preceding five calendar years. The bill would amend these resubmission thresholds to 6%, 15%, and 30%, respectively.
- *Prohibition of Shareholder Proposals by Proxy*. In addition to modifying eligibility and resubmission thresholds for shareholder proposals, the bill would amend Section 14 of the Exchange Act by providing that "[a]n issuer may not include in its proxy materials a shareholder proposal submitted by a person in such person's capacity as a proxy, representative, agent, or person otherwise acting on behalf of a shareholder."

- **Say-on-Pay Frequency**. Under Section 14A(a) of the Exchange Act, an advisory shareholder vote to approve the compensation of executives is required "not less frequently than once every 3 years." The bill would strike this language and instead make say-on-pay resolutions required "each year in which there has been a material change to the compensation of executives of an issuer from the previous year." The bill would also remove the current provision of Section 14A(a) that requires issuers to present a separate resolution to shareholders at least once every six years to determine whether say-on-pay votes should be held every one, two, or three years.
- **Restriction on Recovery of Erroneously Awarded Compensation**. Section 10D of the Exchange Act, added by Dodd-Frank, requires the national securities exchanges to establish listing standards requiring each issuer to implement a policy that, in the event the issuer is "required to prepare an accounting restatement due to the material noncompliance of the issuer with any financial reporting requirement under the securities laws, the issuer will recover from any current or former executive officer of the issuer who received incentive-based compensation . . . during the 3-year period preceding the date on which the issuer is required to prepare an accounting restatement, based on the erroneous data, in excess of what would have been paid to the executive

officer under the accounting restatement." The bill would amend this provision by restricting it to situations "where such executive officer had control or authority over the financial reporting that resulted in the accounting restatement."

- **Repeal of Various Dodd-Frank Provisions**. The bill would repeal various provisions in Titles IX and XV of Dodd-Frank. The most notable among these are provisions requiring:
  - pay ratio disclosure;
  - the disclosure of employee and director hedging policies;
  - disclosures regarding chairman and CEO structures;
  - conflict minerals disclosure;
  - disclosures regarding coal or other mine safety; and
  - the disclosure of payments by resource extraction issuers.

  The bill also would repeal the Dodd-Frank provision permitting the SEC to require proxy access.

- **Prohibition on Requiring a Universal Ballot**. The bill would modify Section 14 of the Exchange Act by adding that the SEC may not require that a proxy or consent solicitation in an election of directors be made using a single ballot that lists the names of both management and dissident nominees and permits shareholders voting by proxy to select from among individuals in both groups.

- **Internal Control Evaluation**. Under Section 404 of the Sarbanes-Oxley Act, each annual report of a public company must contain an internal control report that, among other things, contains management's assessment of the effectiveness of the internal control structure and procedures of the issuer for financial reporting. The registered public accounting firm that prepares or issues the audit report for the issuer is required to attest to, and report on, this assessment.
  - *Small Issuer Exemption*. The bill would provide an exemption from the auditor attestation requirement for any issuer with a total market capitalization of under $500 million or any issuer that is a depository institution and has less than $1 billion in assets.
  - *Temporary Exemption for Low-Revenue Issuers.* Under current law, an issuer that is an emerging growth company ("EGC") no longer qualifies as an EGC on the last day of its fiscal year following the fifth anniversary of the date of its first public sale of common equity securities. At that time, it would be subject to the auditor attestation requirement. The bill would allow issuers with average annual gross revenues of less than $50 million to continue to take advantage of the EGC exemption from the auditor attestation requirement until the earliest of (1) the tenth anniversary of the first sale of registered common equity securities,

(2) the end of a fiscal year during which the average annual gross revenues of the issuer exceeds $50 million or (3) when the issuer becomes a large accelerated filer.

- **Exemption from XBRL Requirements for Emerging Growth Companies and Other Smaller Companies**. Under the bill, EGCs and issuers with total annual gross revenues of less than $250 million, would be exempt from the requirements to use eXtensible Business Reporting Language ("XBRL") for their financial statements and other periodic reports, though they would still be permitted to voluntarily use XBRL for such reporting. The bill would also require the SEC to:
    - conduct an analysis of the costs and benefits to issuers with total annual gross revenues of less than $250 million of the requirements to use XBRL; and
    - provide a report to Congress on the results of this analysis, as well as the SEC's progress in implementing XBRL reporting and the use of XBRL data by SEC officials and investors.

Proxy Advisory Firms

- **Registration Requirement**. The bill would amend the Exchange Act to require proxy advisory firms to register with the SEC. The bill would require each proxy advisor registrant to include in its application for registration, among other things, "the procedures and methodologies that the applicant uses in developing proxy voting recommendations." The bill would also require all information and documents submitted to the SEC by each proxy advisory firm in its completed application to be made publicly available.
- **Censure of Proxy Advisory Firms**. The bill would empower the SEC to censure, suspend or revoke the registration of any registered proxy advisory firm in specified circumstances.
- **Prohibited Conduct by Proxy Advisory Firms**. The bill would require the SEC to issue rules addressing, among other things, potential conflicts of interest relating to the offering of proxy advisory services, including with respect to offering consulting or other services.
- **Management of Conflicts of Interest**. The bill would require each proxy advisory firm to establish, maintain, and enforce written policies to manage any conflicts of interest arising from its business. The SEC would be required to issue rules addressing, among other things, potential conflicts of interest relating to the offering of proxy advisory services, including with respect to offering consulting or other services.
- **Reliability of Proxy Advisory Firm Services**. The bill would require each proxy advisory firm to have staff sufficient to produce proxy voting recommendations that are based on accurate and current information. Proxy advisory firms would also need to have procedures permitting companies receiving proxy advisory firm recommendations to access the draft recommendations within a reasonable time, and would need to provide such companies an opportunity to comment on

the proxy advisory firm's recommendations. Each proxy advisory firm would also be required to employ an ombudsman to receive complaints about the accuracy of voting information used in making recommendations and to resolve such complaints in a timely fashion.

- **Information to be Reported to the SEC**. The bill would require each proxy advisory firm to file with the SEC:
  - financial statements and any other information concerning its financial condition as required by the SEC, at intervals set by the SEC;
  - an annual report with regard to the prior fiscal year on the number of shareholder proposals its staff reviewed, the number of recommendations made, the number of staff who reviewed and made recommendations on such proposals, and the number of recommendations made where the proponent of such recommendation was a client of or received services from the proxy advisory firm; and
  - the firm's methodology for the formulation of proxy voting policies and voting recommendations, which the proxy advisory firm must also make publicly available.

Capital Markets Related Reforms–Registered Offerings

- **Testing the Waters and Confidential Submissions**. The Jumpstart Our Business Startups Act (the "JOBS Act") included provisions permitting EGCs to "test the waters" (i.e. engage in oral or written communications with potential investors that are qualified institutional buyers or accredited investors) prior to the filing of a registration statement (or at any time thereafter). This allowed EGCs to determine investor interest early in the initial public offering process. The bill would enable all issuers, not just EGCs, to engage in "testing-the-waters" communications.
  - The JOBS Act permitted EGCs to confidentially submit draft registration statements to the SEC for review. The bill would allow all issuers contemplating an initial public offering to take advantage of this confidential nonpublic review process, subject to the requirement that the initial confidential submission and all amendments thereto be publicly filed with the SEC not later than 15 days before the date on which the issuer conducts a road show.
- **S-3 Eligibility**. Consistent with the objective to accelerate access to capital, the bill contains certain provisions to expand eligibility for use of Form S-3. The bill does not address F-3 eligibility for foreign issuers.
  - The bill would expand the eligibility for registering primary offerings for cash on Form S-3 to registrants so that the transactional requirements for use of Form S-3 would be satisfied not only where the aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant is $75 million or more but also where the registrant has at least one class of common equity securities listed and registered on a national

securities exchange.

- The bill would expand the eligibility for registering certain limited primary offerings on Form S-3 to registrants that do not have at least one class of common equity securities listed and registered on a national securities exchange. Currently, non-shell companies that wish to conduct sales of no more than one-third of their aggregate market capitalization may not register such offerings on Form S-3 unless they already have common equity securities listed and registered on a national securities exchange.

- **Elimination of Automatic Disqualification as a WKSI**. Under current rules certain "bad acts" and judicial or administrative decrees or orders arising out of governmental action affecting an issuer or its subsidiaries may result in that issuer becoming an "ineligible issuer" under Rule 405 of the Securities Act. Ineligible issuers automatically lose well-known seasoned issuer ("WKSI") status for three years, and consequently become barred from conducting registered securities offerings using an automatic shelf registration statement even if they would otherwise be eligible. Typically, issuers becoming subject to a government enforcement action of this type also negotiate with the SEC for a waiver of the "ineligible issuer" designation. The bill would provide that SEC or government enforcement actions or settlements would no longer result in individuals and entities, including WKSIs, being subject to automatic disqualification as an ineligible issuer.

Capital Markets Related Reforms—Unregistered Offerings

- **Accredited Investors**. The bill would amend the definition of "accredited investor" under the Securities Act to reflect, among other things, the net worth and income tests currently codified in Regulation D under the Securities Act, with a directive to the SEC to inflation-adjust the net worth threshold every 5 years. The bill would conform the definition of "accredited investor" in Section 2(a)(15) of the Securities Act to components of the definition of "accredited investor" currently set forth in Rule 215 and Rule 501 under the Securities Act.

    - In addition, the bill would expand the "accredited investor" definition to include (i) any natural person who, by reason of their net worth or income, is an accredited investor under Rule 215 under the Securities Act (as in effect on the day before the date of enactment of this provision of the bill), (ii) any natural person who is currently licensed or registered as a broker or investment adviser by the SEC, the Financial Industry Regulatory Authority ("FINRA"), or an equivalent self-regulatory organization, or the securities division of a State or the equivalent State division responsible for licensing or registration of individuals in connection with securities activities and (iii) any natural person the SEC determines, by regulation, to have demonstrable education or job experience to qualify such person as having professional knowledge of a subject related to a particular investment, and whose education or job experience is verified by FINRA or an equivalent self-regulatory

organization. In addition, pursuant to a proposed change to Rule 501(a), a "knowledgeable employee" of a private fund or the fund's investment adviser would also be an "accredited investor" for purposes of a Regulation D offering of a private fund with respect to which the person is a knowledgeable employee.

- **Regulation D Private Placement Improvements**. The bill would allow companies greater flexibility in conducting offerings in reliance on the safe harbor under Rule 506 of Regulation D for the private offering exemption of Section 4(a)(2) of the Securities Act. For example, in offerings solely to accredited investors, issuers would not have to submit written general solicitation materials to the SEC. In addition, issuers would not be required to file Form D notices except for a single notice of sales containing the information required by Form D no earlier than 15 days after the date of the first sale of securities.
- **Increase in Amounts Permitted under Rule 701**. Rule 701 under the Securities Act exempts companies from certain disclosure requirements (including financial statements) in securities offerings to employees pursuant to compensatory benefit plans or compensation-related contracts so long as the aggregate sales price or amount of securities sold during any consecutive 12-month period does not exceed $5 million. The bill would revise Rule 701 to increase the threshold from $5 million to $20 million and index the amount for inflation every 5 years.
- **Regulation A+ Exemption**. Section 3(b) of the Securities Act exempts certain small issues from registration. In particular, if the aggregate offering amount offered and sold within the prior 12-month period does not exceed $50 million, then such securities are covered by the exemption from registration provided by Regulation A promulgated under this section of the Securities Act. Under the JOBS Act, Regulation A was expanded into what has become known as Regulation A+ with a two-tiered approach, but the $50 million threshold remained. The bill would increase the threshold from $50 million to $75 million, adjusted for inflation every 2 years.
- **Crowdfunding, Venture Exchanges, Micro Offerings**. The bill would exempt crowdfunding securities from registration under Section 12(g) of the Exchange Act, among other measures to ease crowdfunding restrictions. In addition, the bill provides for the establishment of venture exchanges to facilitate the sale of the securities of EGCs or "early-stage, growth companies" and would exempt such venture exchanges from compliance with certain national security exchange regulations. The bill would also add a safe harbor under Section 4 of the Securities Act for certain micro offerings in which purchasers have substantive pre-existing relationships with the issuer, there are 35 or fewer purchasers and the offering amount does not exceed $500,000.
- **Swaps Between Affiliates**. The bill would generally exempt swaps between consolidated affiliates from SEC and CFTC regulation, and impose only certain reporting and risk management requirements if at least one counterparty is a swap dealer or major swap participant.

Regulatory Process Reform

- **Congressional Review and Approval of Agency Rulemaking**. Before any rule issued by a federal financial agency may take effect, the agency would need to publish a list of information on which the rule is based (including any studies or cost-benefit analyses), and submit to Congress and the U.S. Comptroller General a complete cost-benefit analysis of the rule (including an analysis of the rule's impact on jobs and small businesses).
    - Any rule that would be likely to result in (1) an annual economic impact of at least $100 million, (2) a major increase in prices for consumers or costs for businesses, government agencies, or geographic regions, or (3) significant adverse effects on competition, employment, investment, productivity, innovation, or international competitiveness would be classified as a "major rule."
    - Any such "major rule" would not be permitted to take effect unless it is approved by a joint resolution of Congress within 70 days of the agency's cost-benefit report. If the rule does not obtain Congressional approval within 70 days, it could not be reconsidered until the next Congress.
    - A "major rule" would be permitted to take effect for one 90-day period, upon written determination by the President, to enforce criminal laws, to implement an international trade agreement, or for reasons of national security and other emergencies.
- **Tailoring Regulatory Actions to Relevant Institutions**. The bill would require the federal banking agencies to appropriately tailor regulatory actions to fit an institution or class of institutions in a manner that limits compliance cost and impact, including by considering the risk profile and business models of the institutions subject to the regulatory action and the necessity of applying the regulatory action to those institutions. The bill would also require the federal banking agencies to report annually to the House Financial Services Committee and Senate Banking Committee regarding the specific actions taken to appropriately tailor regulatory actions, and to conduct a look-back review of all regulations adopted in the last five years to determine whether such regulations are sufficiently tailored.
    - With respect to capital requirements for non-QBOs in particular, the CHOICE Act 2.0 would prohibit the federal banking agencies from establishing any risk capital requirements unless such requirements are appropriately tailored to the risk posed by a bank's current activities and businesses, based on a forward-looking assessment of such risk, and permit capital adjustments based on mitigants to such risk.
- **Agency Appropriations**. The bill would subject funding for several financial agencies to the Congressional appropriations process, including the Federal Housing Finance Agency, the National Credit Union Administration, the FDIC, the OCC, the CLEA (formerly the CFPB), and the functions

of the Federal Reserve not related to monetary policy (including its bank regulatory and supervision functions). These agencies would be directed to collect fees and assessments to offset Congressional appropriations. As noted above, funding for FSOC would also be subject to the Congressional appropriations process.

- **Repeal of *Chevron* Deference**. The *Chevron* doctrine, requiring judicial deference to agency interpretations, would be statutorily repealed by requiring *de novo* judicial review of all relevant legal interpretations and rules made by an agency.
- **Federal Reserve Oversight**. The bill includes several provisions that would increase Congressional and public oversight over the Federal Reserve. The Federal Reserve and each of the Reserve Banks would be subject to an annual audit by the U.S. Comptroller General, and the Chairman of the Federal Reserve would be required to testify before Congress quarterly (as opposed to the current semi-annual requirement). Meetings of the Federal Open Markets Committee would be recorded and full transcripts would be available to the public as a matter of law, not custom. Finally, Federal Reserve staff would be subject to financial disclosure requirements, as well as federal prohibitions related to outside employment and activities to the same extent as such prohibitions apply to employees of the SEC.
- **Oversight of International Accords**. The federal financial agencies and the Treasury Department would be required to provide public notice before participating in international standard-setting processes, and to report on any such international standard-setting processes after participating. The agencies would also need to consult with the House Financial Services and Senate Banking Committees on any agreements that may result from international processes.

Insurance Related Reforms

The bill would establish a new Independent Insurance Advocate within the Treasury Department, which would consolidate and replace FSOC's independent member with insurance expertise and the Federal Insurance Office ("FIO").

- The Insurance Advocate would have the authority to coordinate U.S. federal efforts on prudential aspects of international insurance matters and to participate on the Financial Stability Board and with the G20 on insurance matters.
- The Insurance Advocate would have a duty to "observe" (rather than "monitor") the insurance industry, and would not have FIO's current ability to collect data from insurance firms (instead, it would need to rely on state insurance supervisors and other agencies for its data).

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