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AUTHORS

Jonathan L. Pompan

William J. Donovan

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The Dodd-Frank Act and Implications for Nonprofit Organizations

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In the midst of the worst U.S. financial crisis since the Great Depression that has captured the attention of lawmakers and the public over the last several years, Congress passed the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (the "Act" or the "Dodd-Frank Act"), which was signed into law on July 21, 2010. The law has set in motion a new era of regulation over financial products and services that will have a broad impact for years to come.

While many of the provisions of the Dodd-Frank Act apply specifically to financial services firms and their related activities, the Act does include a handful of key provisions that may impact generally the nonprofit community. In addition, the Dodd-Frank Act makes sweeping changes in how financial products and services are regulated that will impact a number of nonprofit organizations directly due to new regulations and compliance requirements.

Nonprofit leaders should look carefully at the provisions of the Dodd-Frank Act and determine whether their organization's fall under any of its provisions and, to the extent that they do not, how they may address practices required under the Act, even if not mandated by law. In addition, there are a number of opportunities for nonprofits in the areas of financial literacy and consumer education. Of course, there also will be no shortage of opportunities for financial services industry trade associations to weigh-in on issues of importance to their memberships.

This article will provide some general background and review the main provisions most likely relevant to nonprofit organizations.

The Dodd-Frank Act Basics

In a nutshell, the Dodd-Frank Act imposes new restrictions on risky financial investments, creates new consumer protections, including a new regulator of financial products and services (the Bureau of Consumer Financial Protection) and makes significant changes to the existing regulatory structures for financial institutions. As a practical matter, the Dodd-Frank Act is over 2,000 pages and has been estimated to require federal agencies to conduct over 250 rulemakings and to make dozens of studies and periodic reports.

Executive Compensation and Corporate Governance Reforms

The Dodd-Frank Act includes strict new requirements on publicly traded companies to provide shareholders with a say on pay and corporate affairs with a non-binding vote on executive compensation and golden parachutes. The effect of these provisions is to vastly increase the role of shareholders in areas that had previously been the sole domain of corporate boards of directors.

Under the Dodd-Frank Act, at least once every three years, public company shareholders will be able to cast a non-binding vote to approve executive compensation and where applicable, executive golden parachutes, known generally as "say on pay." Notably, however, the Securities and Exchange Commission ("SEC") will be permitted to adopt exemptions for small public companies.

In addition, the Dodd-Frank Act authorizes the SEC to promulgate rules that would allow shareholders to nominate candidates for a public company's board through the company's proxy materials, a process called proxy access. Again, the SEC may exempt small companies from these provisions.

The Dodd-Frank Act also requires the SEC to amend its rules to require additional disclosure on the relationship between executive compensation and corporate financial performance with respect to such metrics as changes in the value of an issuer's stock and dividend distributions.

The Act also requires the SEC to issue rules prohibiting stock exchanges from listing the stock of any company that does not adopt an executive incentive pay "clawback" policy. With broad applicability to current or former executives, if there is an accounting restatement due to material noncompliance with financial disclosure laws, a company is to recover – *i.e.*, clawback – incentive compensation that was awarded on the erroneous disclosures during three years preceding the restatement.

The Dodd-Frank Act also directs federal financial regulators to jointly adopt guidance requiring applicable financial institutions, including nonprofit credit unions, with more than $1 billion in assets to prohibit incentive-based pay arrangements for executives, employees, directors, or principal shareholders deemed to be excessive, or that could lead to material financial loss at the financial institution.

In addition, there are new independence requirements for compensation committee members of publicly traded companies. In short, there are now requirements that compensation committees be composed exclusively of independent directors and that the committees consider the independence of consultants and advisers (*e.g.*, legal advisers and compensation consultants).

As with most major aspects of the Sarbanes-Oxley Act of 2002 ("SOX") (with the exception of provisions concerning whistleblowers and document destruction), the Dodd-Frank Act executive compensation and governance provisions will not directly apply to nonprofit organizations. Moreover, for many nonprofit organizations the march towards executive compensation and corporate governance reforms may seem to be like old news considering all of the reforms that the nonprofit community has already undertaken, including as a result of the Internal Revenue Service's revisions to the Form 990. Nevertheless, the changes to executive compensation and corporate governance may take on increasing importance as federal and state officials and others seek out elements of the Dodd-Frank Act's reforms to apply to nonprofit organizations.

Enhanced Whistleblower Protections

The Dodd-Frank Act includes significant provisions to incentivize whistleblowers and to provide protection from retaliation. In particular, the Dodd-Frank Act includes provisions that:

- Provide a bounty for all tips resulting in securities law enforcement actions with monetary sanctions that are greater than $1,000,000.
- Protect whistleblowers from retaliation under 18 U.S.C. § 1513(e), which prohibits retaliation, including in connection with employment, against individuals for providing information to a law enforcement officer about the possible commission of a federal offense.
- Protect employees of all subsidiaries and affiliates of public companies and any individual performing tasks related to the offering or provision of a consumer financial product or service.
- Provide a private right of action in federal court for whistleblowers regardless of administrative delay.
- Increase the statute of limitations for whistleblower protection actions to 6 years following the alleged violation.

The scope and depth of the protections provided to whistleblowers under the Dodd-Frank is broader than those that were created under SOX in 2002. The Dodd-Frank Act's expansion of protections may impact nonprofit organizations by providing in some instances employees with new protections and a longer period in which to invoke those protections than they presently have under SOX.

These changes to whistleblower laws are likely to have a cascading affect in related areas of the law and compliance. Indeed, in the wake of the SOX, several states enacted new laws containing elements of the then new law to be applied to nonprofit organizations.

Accordingly, nonprofit organizations – especially those involved in providing financial products or services – will want to carefully review their business practices and policies against the new Dodd-Frank Act provisions to help avoid whistleblower related liability.

Consumer Financial Protection Act

Title X of the Dodd-Frank Act (entitled the "Consumer Financial Protection Act") establishes a Bureau of Consumer Financial Protection (the "CFPB") within the Federal Reserve System to have authority over an array of consumer financial products and services (including nonprofit credit counseling and foreclosure assistance providers).

The CFPB will serve as the primary federal consumer financial protection supervisor and enforcer of federal consumer protection laws over many of the institutions that offer these products and services.

Notably, the Dodd-Frank Act explicitly exempts a number of entities and activities from the CFPB's jurisdictional reach, including most merchants and activities related to the solicitation or making of voluntary contributions to tax-exempt charities.

In addition, a significant part of the Bureau's consumer protection mission will focus on financial literacy and educational activities, which should provide a number of opportunities for nonprofit organizations.

The Bureau is to be up and running as of July 21, 2011.

Miscellaneous Provisions that May Affect Nonprofits

The Dodd-Frank Act contains many additional provisions that may be relevant to nonprofit organizations, including the following:

- Small dollar lending to low-to-moderate-income Americans, provided that the lender also promotes financial literacy and credit counseling that is supported by the Department of Treasury.
- Nonprofit housing counseling requirements for certain first time homebuyers and "high cost loans."
- Additional funds for the neighborhood stabilization program, which allows states and localities to combat the impact on neighborhoods of the foreclosure crisis by rehabilitating, redeveloping, and reusing abandoned and foreclosed properties.
- Funding for loans to qualified unemployed homeowners with reasonable prospects for re-employment to help them cover mortgage payments until they are re-employed.
- A foreclosure legal assistance grant program to provide foreclosure legal assistance to low- and moderate-income homeowners and tenants related to homeownership preservation, home foreclosure prevention, and tenancy associated with home foreclosure.

Embedded within the text of the Dodd-Frank Act are several other financial reforms that may related to investments, mortgage lending, insurance and other areas that may impact a nonprofit organization's day-to-day business.

Implementation of the Dodd-Frank Act

The Dodd-Frank Act imposes extensive new responsibilities on numerous federal agencies. While some of those agencies (most notably the CFPB) do not rely on Congress for funding, many others do, and their resources will be stretched as a result of the Republican majority in the House of Representatives underlying opposition to passage of the Dodd-Frank Act (only three Republicans voted for the bill and only one of them is returning to the 112th Congress) coupled with their interest in shrinking the size of government. Additionally, Congressional opponents of the Dodd-Frank Act have introduced legislation (H.R. 87) to repeal it in its entirety; the new Chairman of the House Financial Servicers Committee has reportedly pledged to review the new law "provision by provision"; and, some have advocated pushing back all regulatory deadlines in the Dodd-Frank Act by one year. Finally, as of this writing, the President has yet to nominate, and, the Senate will need to confirm, a first director of the CFPB. Nevertheless, several federal agency rulemakings to implement the Dodd-Frank Act are underway or are expected within the next few months and a CFPB implementation team has been laboring out of the Department of Treasury since September 2010.

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Many nonprofits will be affected, directly and indirectly, by provisions in the Dodd-Frank Act. Nonprofits that are directly engaged in providing financial products or services will generally need to comply and operate within a new regulatory regime. In addition, many nonprofit organizations will be impacted by the changes that the Dodd-Frank Act makes that may eventually become benchmarks for all companies and organizations, including nonprofits. Accordingly, nonprofit organizations should take into account the changes to the law under the Dodd-Frank Act and the rulemakings that will follow in the coming months and years.

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Jonathan Pompan *is Of Counsel at Venable LLP in the Washington, D.C. office. He represents nonprofit and for-profit companies, including non-banking providers of financial services. Mr. Pompan's practice focuses on regulatory law compliance and advocacy, as well as in connection with government investigations and enforcement actions. Prior to joining Venable, Mr. Pompan was an in-house counsel at a trade association.*

William Donovan *is a partner at Venable LLP in the Washington, D.C. office. He represents a variety of nonprofit and for-profit providers of financial services as well as companies that support providers of financial services. Mr. Donovan's practice predominantly has a legislative focus; he was intimately involved in representing client interests as the Dodd-Frank Act worked its way through the*

legislative process to the President's desk. Prior to joining Venable, Mr. Donovan was in-house general counsel for an association of nonprofit financial services providers.

*For more information, please contact Jonathan Pompan at 202.344.4383 / **jlpompan@venable.com** or William Donovan at 202.344.4939 / **wjdonovan@venable.com**.*