An Annotated Agenda for Reform of the Federal Regulation of Financial Institutions

Understanding the Policies Embedded in the President's Executive Orders, the Treasury Report and the Financial CHOICE Act

July 2017

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Executive Summary

We have developed this White Paper to assist regulated financial institutions to foresee future regulatory trends and be better armed to develop their strategic business plans. In that regard, the formal and informal statements by the Administration, the Treasury and the Congress indicate a direction that will be marked by the following characteristics:

- Regulation of financial institutions should be less burdensome, clearer and directly tethered to a realistic comparison of the costs and the benefits of such regulation.
- The Office of Management and Budget's Office of Information and Regulatory Affairs will become a choke point that monitors and enforces these goals.
- Regulation should become more customized and principles-based, taking into account size, balance sheet risk, markets and management expertise.
- Efforts should be made to limit the extent of redundant federal and state regulation, as well as the tendency for agencies to "pile on" in significant enforcement cases.
- Stress testing, capital requirements and liquidity rules will be tailored to reflect the size of the institution and will be based on more reasonable time periods (e.g., two-year cycles) to flatten out wide variances in the requirements, while making them more transparent, consistent and less redundant.
- The Volcker Rule is likely to be amended, if not by Congress, by the agencies to reduce artificial market and liquid impacts, reduce its compliance burdens, shrink its product and geographic reach, limit its applicability to smaller financial companies, soften the terms of its Super 23A provisions and simplify its terms and definitions.
- The tools and authorities provided by Title I of Dodd-Frank with regard to systemic stability are likely to be reevaluated and refocused on broad economic red flags and corresponding tools that can be implemented to avoid future financial crises before they become imminent.
- The Financial Stability Oversight Council is likely to remain in place, but act more akin to the coordinating committee after which it was patterned to provide the Administration with a vehicle for direct communication to the agencies that are represented in FSOC. Designations of systemically important financial institutions are likely to proceed at a very slow pace, if at all.
- Global capital and regulatory standards will likely be viewed from the perspective of what makes sense in America, and adoption should be contingent on how and if they will be uniformly adopted by foreign countries.
- Title II of Dodd-Frank and its orderly liquidation authority provisions will be reevaluated and possibly repealed, but the need for some facility to resolve and finance large failures will remain a goal.
- While resolution planning will continue to be an important goal, the utility, the applicability requirements, the frequency and the benefits of living wills will be reconsidered relative to the cost of their production.
- Efforts will be made to move toward a more streamlined regulatory structure, which may include the consolidation or elimination of agencies or offices.
- Cybersecurity risks will continue to increase and become the predominant operational risk. The associated regulatory preparation and response will continue to create significant compliance challenges that will need to be properly focused by Cybersecurity experts on the real and most pressing risks.

Introduction: A Question of Timing and Balance

On June 12, 2017, the U.S. Department of the Treasury released a report entitled: *A Financial System That Creates Economic Opportunities: Banks and Credit Unions* (the "Treasury Report" or "Report").[1] The Report was directed by President Trump's Executive Order No. 13772, which established the Trump Administration's Core Principles for financial regulation:

– Empower Americans to save for retirement, build wealth, and make informed choices in the marketplace.

– Prevent taxpayer-funded bailouts.

– Foster economic growth and vibrant financial markets through more rigorous regulatory impact analysis.

– Advance American interests in international financial regulatory negotiations.

At the same time, Congress continues to evaluate sweeping alterations of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act" or "Dodd-Frank"), most notably through adoption of the Financial CHOICE Act.[2] Twenty-four of the world's largest commercial banks, via The Clearing House, have offered their own submission to the Treasury Department with recommendations for aligning bank regulation with the Core Principles.[3]

Unified Republican control over Congress and the Executive branch has created a rare window of opportunity to overhaul the U.S.'s redundant, complex and aging bank regulatory system.[4] We endeavor here to evaluate and analyze these proposals in light of our own experience and the nature of the markets to intuit the direction and form that future regulation of financial institutions may take.

1 A Financial System That Creates Economic Opportunities: Banks and Credit Unions, U.S. Department of the Treasury, (June 12, 2017).

2 Executive Order on Core Principles for Regulating the United States Financial System, Dechert Financial Regulatory Reform Tracker (Feb. 3, 2017).

3 See generally, The Clearing House, *Submission to the U.S. Treasury Department: Aligning the U.S. Bank Regulatory Framework with the Core Principles of Financial Regulation*, (May 2, 2016).

Dodd-Frank Act

849 pages	nearly 400 new regulations	2 new federal agencies

Over the last 50 years, prudential regulation in America has seen a slow but steady evolution from a principles-based system reliant on give-and-take between regulators and financial executives toward a more adversarial, rules-based system marked by complexity and high costs of compliance. Although much of what occurred in the financial crisis could have been addressed by financial regulators under then-existing laws and enforcement authorities, Dodd-Frank added 800 new single-spaced pages of federal laws that resulted in nearly 400 new regulations. Dodd-Frank also launched two very active new agencies, the Financial Stability Oversight Council ("FSOC") and the Consumer Financial Protection Bureau ("CFPB"). Together, those agencies have significantly broadened the range of companies that are subject to federal regulation.

This expansion of federal regulation contradicts an unwritten but long-standing understanding that the highest levels of regulation are reserved for financial

4 The Office of the Comptroller of the Currency ("OCC") was the first federal banking agency established in 1864, followed by the Federal Reserve ("FRB") in 1913, the Federal Home Loan Bank Board in 1933, and the Federal Deposit Insurance Corporation ("FDIC") in 1934.

institutions that enjoy federal deposit insurance. The extension of vigorous prudential regulation under Dodd-Frank increasingly appears to be based on the government's desire to prudentially regulate financial companies that have the capacity to adversely impact economic stability. This may be an appropriate premise on which to craft regulation in a 21st century in which banks no longer hold the percentage of consumer funds that they once did. However, there has been little to no discussion, debate, or study of that principle, its intended and unintended consequences, or its qualitative and quantitative economic costs and benefits. History suggests that attempts to affect the operation of companies and markets that are not part of a well-considered overall plan can result in devastating financial repercussions.[5] While it is undisputed that federally insured institutions should be closely regulated, since the enactment of the thousands of pages of new rules under the Dodd-Frank Act, the resulting cost of regulatory compliance has increased exponentially.[6]

Community banks, which were largely uninvolved in the causes of the last crisis, are laboring under a compliance cost structure that often creates a complex set of operational choices for them. Increasing costs threaten their ability to comprehensively serve local communities, a bedrock of the American financial services and products delivery system, while competition continues to increase.[7] The Financial CHOICE Act offers relief to community banks by incorporating the elements of the Taking Account of Institutions with Low Operational Risk (TAILOR) Act,[8] the Financial Institution Customer Protection Act,[9] the Portfolio Lending and Mortgage Access Act,[10] the Financial Institutions Examination Fairness and Reform Act,[11] and the Community Bank Reporting Relief Act.[12]

The Treasury Report calls for a "sensible rebalancing of regulatory principles" in light of the post-recession health of the financial system and the economy.[13]

5 The S&L crisis and the conservatorships of Fannie Mae and Freddie Mac are two illustrations of this phenomenon.

6 In 2015, the American Action Forum estimated the cost of Dodd-Frank to be roughly $895 billion in reduced gross domestic product (or $3,346 per working-age person) between 2016 and 2025. Such costs may be warranted and appropriate, but neither Congress nor the federal government assessed the cost of the Dodd-Frank Act either before or since its enactment. For more detail on the cost and inefficiency of the current regulatory system, see Thomas Vartanian, "*The Good, Bad or Ugly of the Dodd-Frank Act, Part 1 and 2*", BNAInsights, Vol.106, No. 16, 04/18/2016.

7 Community banks are particularly concerned with the increasing competition from credit unions, which have recently been given authority to expand their fields of membership and make commercial loans. See Chartering and Field of Membership Manual, 81 Fed. Reg. 88,412 (Dec. 7, 2016). Both the Independent Community Bankers of America and the American Bankers Association have sued to block those authorizations by the NCUA. See *Independent Community Bankers of America v. National Credit Union Administration*, No. 16 Civ. 01141 (E.D. Va. Jan. 24, 2017); see also *Complaint, American Bankers Ass'n v. Nat'l Credit Union Admin.*, No. 16 Civ. 02394 (D.D.C Dec. 17, 2016).

8 H.R. 1116, 115th Cong. (2017), available at https://www.congress.gov/bill/115th-congress/house-bill/1116/text. The TAILOR Act would require financial regulators to consider the risk profile, size, and business model of each institution and tailor any rule or regulation thereto. It also requires greater consideration of the necessity and impact of rules as well as requires reports by the regulators regarding its implementation.

9 H.R. 766, 114th Cong. (2015), available at https://www.congress.gov/bill/114th-congress/house-bill/766/text. The Financial Institution Customer Protection Act limits' regulators ability to order a depository institution to terminate a customer account.

10 H.R. 1210, 114th Cong. (2015). The Portfolio Lending and Mortgage Access Act creates a safe harbor from lawsuit under the Truth in Lending Act for depository institutions who hold onto residential mortgage loans.

11 S. 774, 114th Cong. (2015). The Financial Institutions Examination Fairness and Reform Act amends the examination process by federal financial regulators to, among other things, shorten the timeline for a response, establish a right of appeal, and creates an Office of Independent Examination Review.

12 H.R. 4500, 114th Cong. (2016). The Community Bank Reporting Relief Act amends the Federal Deposit Insurance Act to direct federal banking agencies to issue regulations reducing reporting requirements for highly rated and well-capitalized depository institutions.

13 Treasury Report, p. 6.

> Most critically, regulatory burdens must be appropriately tailored based on the size and complexity of a financial organization's business model and take into account risk and impact. In particular, the use of arbitrary asset thresholds to apply regulation has resulted in a "one-size-fits-all" approach that has prevented regulators from focusing on a banking organization's most serious risks.
> Treasury Report, p. 9.

The fact that the regulatory system missed the signs of the last crisis and was not agile enough to resolve it quickly or efficiently is also offered as evidence that the current regulatory system may need to be recalibrated. The overlapping system of U.S. domestic regulation appears to allow multiple supervisory authorities to regulate toward different views of safety and soundness while, at the same time, competing for jurisdiction, civil penalties and headlines. Banks that find themselves on the business end of the enforcement mechanisms of federal and state agencies experience the redundancy in the system most acutely.[14] The same set of facts often provides concurrent enforcement jurisdiction to the Federal Reserve,[15] the OCC,[16] the FDIC,[17] fifty state bank regulators,[18] and the Department of Justice.[19] In the case of mortgage, automobile and other consumer law violations, state attorneys general and state consumer protection authorities have shown their interest in joining such actions. Furthermore, the Department of Justice has also become a serious bank enforcement authority, extracting some of the largest penalties ever assessed based on the conduct of institutions related to the issuance, packaging and sale of mortgage-backed securities.[20] Treasury's Financial Crimes Enforcement Network has concurrent enforcement and civil money penalty authority over banks in the case of money laundering and Bank Secrecy Act violations. The SEC has jurisdiction to enforce various corporate governance, securities and disclosure laws with regard to publicly-traded bank holding companies. Finally, given the continuing criminalization of banking, it is increasingly likely that federal and state criminal authorities may also be involved in any enforcement matter. If these trends continue, the financial vibrancy of the banking sector may be permanently affected, which will inevitably impact the vibrancy of the U.S. economy.

The following will address various solutions being proposed to address these issues and recalibrate the delicate balance between markets and financial regulation.

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14 The vast administrative enforcement authorities given to the federal banking agencies make them the prosecutor, judge, jury, and appellate court, leaving even a completely innocent target bank left to choose between a rapid financial settlement, or two to three years of administrative litigation before it is able to get to a federal court where the judge is not loosely affiliated to the agency that it is deciding the actions. See 12 U.S.C §1818.

15 The FRB regulates bank and financial holding companies and is the principal federal regulator for state-chartered Fed-member banks.

16 The OCC regulates national banks and federally-chartered thrift institutions.

17 As the provider of federal deposit insurance, the FDIC is the back-up regulator for national and state banks, the primary regulatory for a state-chartered, non-Fed-member banks, and acts as receiver or conservator for federal and state charted banks.

18 The states charter and regulate state-chartered banks, which are insured by the FDIC.

19 The DOJ has become a familiar bank regulator with its concurrent civil authority with regard to a wide array of federal laws and regulations. While it has asserted itself for many years in fair lending, money laundering, and False Claims Act cases, it has led the charge in a variety of new bank enforcement cases, including mortgage origination, servicing and securitization, third party processing, and payday lending. In DOJs' mortgage origination, servicing and securitizing cases, the DOJ relied on a little known authority provided to it in 1989 in the aftermath of the S&L crisis when Congress enacted 12 U.S.C. § 1833a as a part of Financial Institutions Reform Recovery and Enforcement Act (FIRREA). Section 1833a authorizes the DOJ to use civil investigation and enforcement powers to "recover a *civil* penalty" from "whoever violates" certain *criminal* statutes through activities that harm insured banks. It has used this provision by asserting that banks in these cases have essentially defrauded themselves.

20 See DOJ Press Release, (Feb. 11, 2016); see also DOJ Press Release (Apr. 8, 2016).

Reaction to a Rules-Based System of Regulation

The Trump Administration's Executive Orders and Core Principles suggest the need for a more thoughtful regulatory impact analysis before rules are adopted. In that regard, they generally require (i) a more rigorous set of hurdles to legitimize the issuance of rules, (ii) the elimination of two rules for every new one that is promulgated, and (iii) the adoption of more substantial cost benefit analyses before the need for new rules can be authorized.[21]

To further avoid the annual compounding of rules, we would also expect that new regulations should also include sunset dates by which they would be automatically reevaluated or allowed to expire. Sunset provisions would create a regulatory culture where the constant rigorous reevaluation of the costs and benefits of rules becomes normalized.

At the same time, Congress is also taking steps to ensure that the effort to reduce redundant and unnecessary regulations is not undercut by agency efforts to regulate through directives, bulletins and the informal but effective mechanisms that the regulatory system provides.[22] The Financial CHOICE Act would change the rulemaking process entirely by subjecting all financial federal regulatory agencies to the Congressional approval of rules contained in the proposed REINS Act[23] and to the Congressional appropriations process for their funding. The CHOICE Act would also require each financial regulator to conduct a detailed economic cost-benefit analysis of all proposed and final regulations. Safety, soundness, transparency, efficiency and cost-effectiveness will be the ultimate goals.

21 While Executive orders generally apply only to Executive Agencies, which would not include the independent bank regulatory agencies, and there is already litigation against some of these Executive Orders, the message being sent by the Administration is that the policies of newly appointed regulators are likely to ensure that the trend will move toward the imposition of less unnecessary rules and regulations.

22 Recently, efforts have been made to ensure that agency directives, bulletins and guidance which are functionally equivalent to regulations are also subject to rescission by Congress under the Congressional Review Act. See 5 U.S.C. § 801 et seq. Ian McKendry, *Toomey Seeks GAO's Help in Reviewing Agency Guidance, American Banker* (Mar. 31, 2017).

23 Regulations from the Executive in Need of Scrutiny Act of 2017, H.R. 26 (115th Congress), available at https://www.congress.gov/bill/115th-congress/house-bill/26/text. The REINS Act, among other things, would subject every major rule to Congressional approval before effectiveness. A "major rule" is any rule that the Office of Information and Regulatory Affairs of the Office of Management and Budget finds has resulted in or is likely to result in: (1) an annual cost on the economy of $100 million or more (adjusted annually for inflation); (2) a major increase in costs or prices for consumers, individual industries, federal, state or local government agencies, or geographic regions; or (3) significant adverse effects on competition, employment, investment, productivity, innovation or the ability of U.S.-based enterprises to compete with foreign-based enterprises.

Efforts to Consolidate, Simplify and Make Capital, Stress Testing and Liquidity Requirements Transparent

Attempts are being made to ensure that financial regulators' reliance on regulatory capital requirements coming out of the financial crisis are rational, practical and transparent. Banks, particularly larger banks, are subject under Dodd-Frank to a library of overlapping quantitative and qualitative U.S. and international financial regulatory standards measuring capital adequacy in ways that are not always transparent. They include:

- Basel III (IV)
- DFAST (Dodd-Frank Act Stress Test)
- CCAR (Comprehensive Capital Analysis and Review)
  - Counterparty Default Components
  - Global Market Shock
- TLAC (Total Loss-Absorbing Capacity) and U.S. Long Term Debt
- Counter-cyclical Capital Buffers
- Global Systemically Important Bank (G-SIB) Capital Surcharges
- Stress Capital Buffers (*under consideration*)
- Capital Conservation Buffers
- Tier 1 Leverage
  - Supplemental Leverage Ratio (SLR)
- Standard and Advance Risk-Weighting
- Operational Risk
- Resolution and Recovery Planning

An array of liquidity measurements are similarly approaching the same complex status as regulatory capital. The liquidity measurements include:

- Liquidity Coverage Ratios (LCR)
- Net Stable Funding Ratio (*not finalized yet but built into Basel III*)
- CLAR (Comprehensive Liquidity Analysis and Review)
- Resolution and Recovery Planning

Compliance with the capital requirements testing regime is costly in terms of the resources required and the opportunity cost of maintaining the capital. Even before the appointment of any new Governors at the Federal Reserve Board, since the election, departed Governor Tarullo and Governors Fischer and Powell have been backtracking in speeches that give some credence to the industry's concerns by suggesting the rollback of certain elements and increasing the transparency of current capital requirements, particularly the CCAR stress test, which had drawn most of the criticism from the industry.[24] Federal Reserve Chair Janet Yellen has even suggested exempting community banks from the Volcker Rule, simplifying the capital regime for community institutions and the Fed returning to a more traditional supply of reserve balances while praising the Treasury Report for its many useful positions on tailoring regulations.[25]

Large banks need an army of experts to address domestic and international regulatory capital requirements. The Treasury Report pointed to the requirement for large banks to calculate their capital requirements under both "advanced approaches" generated internally, and regulator-generated "standardized approaches" as evidence of redundancies that require attention. The Report calls the current design and implementation of CCAR stress testing opaque, complex and excessively

24 Departing Thoughts: Remarks by Daniel K. Tarullo Member Board of Governors of the Federal Reserve System at The Woodrow Wilson School (Apr. 4, 2017), pp. 20-21; Supervisory Stress Testing of Large Systemic Financial Institutions (June 24, 2015).

25 Statement by Janet L. Yellen, Chair, Board of Governors of the Federal Reserve System before the Committee on Financial Services, U.S. House of Representatives (July 12, 2017).

conservative. The Report singled out the qualitative aspects of CCAR as the cause of inefficiencies in capital allocation that allow regulators to steer lending toward preferred asset classes. It recommends, among other things, that the Federal Reserve subject its stress-testing and capital planning review frameworks to public notice and comment and convert the stress-testing process to a two-year CCAR cycle, which would still allow results to be forecast over a nine-quarter cycle.[26]

The CHOICE Act would also limit testing to every two years to reduce compliance costs and also attempt to increase transparency, ending mid-year Dodd-Frank Act Stress Tests ("DFAST") entirely, limit DFAST to only bank holding companies, and broaden the exemptions from qualitative aspects of CCAR so that the Federal Reserve could assess a bank organization's qualitative strength but could not object to its capital plan based on that assessment.[27]

History suggests that over-reliance on arbitrary financial formulas and capital and liquidity measurements as arithmetical proxies for financial reality can lead to unintended consequences. The Treasury Report acknowledges the cost of current capital requirements, which are naturally passed on to borrowing households and businesses.[28] The industry finds that CCAR is imposing dramatically higher capital requirements on small business loans and residential mortgages than either bank internal modeling or Basel-based models.[29]

The Report recommends that the threshold for application of CCAR should match the threshold for enhanced prudential standards.[30] The Report not only recommends eliminating year-to-year uncertainties in the development of CCAR and risk capital standards, but reformatting U.S. and international capital, liquidity and risk requirements to make them work more efficiently and fairly.[31] Capital and liquidity regulations that are actually in direct conflict (e.g., LCR requires banks to hold high quality assets, including cash and Treasuries, but Tier 1 Leverage, SLR[32] and G-SIB Surcharges tax them on the capital side) would be prioritized to ensure that they work in a rational and harmonized way.[33] Parenthetically, these rules would benefit from one standard definition of "financial institution" for the purposes of measuring capital, leverage and liquidity requirements.

Finally, the application of standardized risk-weighting should not encourage low-risk companies to take on more risk because they are already being surcharged for risk that exceeds their profile. In that regard, additional recommendations for tailoring capital requirements in the Treasury Report include narrowing the LCR to only internationally active banks, applying the single-counterparty credit limit to only banks subject to the enhanced prudential standards threshold, and factoring a banking organization's historical experience into its LCR process.[34]

26 Treasury Report, p. 12.

27 H.R. 10, 115th Cong. § 151 (2017).

28 Treasury Report, p. 49.

29 See also The Clearing House, *The Capital Allocation Inherent in the Federal Reserve's Capital Stress Tests* (January 2017), p. 4.

30 Treasury Report, p. 12.

31 Treasury Report, p. 12.

32 The Treasury Report already recommends adjustments to the SLR and the enhanced SLR (through the calibration of the eSLR buffer and the leverage exposure calculation) to increase liquidity and avoid penalizing low-risk assets. See Treasury Report at 14.

33 Treasury Report, p. 53.

34 Treasury Report, p. 12.

The Volcker Rule and Other Impacts on Market Liquidity

The Volcker Rule, Liquidity Coverage Ratios and Risk Retention requirements should be re-evaluated now that they have had some time to take effect so that observers can determine how they interact and whether they are creating unfavorable dislocations in market liquidity and investment patterns. These and other regulations bestow favored investment status on government securities, which, among other things, necessarily impacts market liquidity, whether intended or not. At some point, the economic consequences should be evaluated and the cost should be relative to the real benefits that are measurable.

Federal regulators under the Trump Administration are already reviewing the Volcker Rule to identify its unintended consequences. In part based on this review, the regulators recently announced their intent to suspend enforcement of the Volcker Rule until July 21, 2018 against certain foreign banks and their affiliated foreign investment funds that might otherwise be deemed to be banking entities. While this action only covers a narrow issue under the Volcker Rule, the regulatory initiative and flexibility indicates broader reforms may be forthcoming.

While simply stated in the law, the application of the Volcker Rule adopted by federal regulators is extraordinarily complex. Perhaps no one provision of Dodd-Frank has more potential to have as wide and significant a financial impact on banks, non-bank financial companies, and the U.S. economy and foreign affiliates than the Volcker Rule.[35] Yet, surprisingly, perhaps no provision of Dodd-Frank had less to do with the direct causes of the last financial crisis or less analysis about its effects. The CHOICE Act would repeal the Volcker rule.[36] The Treasury Report is direct in its evaluation of it:

> The Volcker Rule requires substantial amendment. Its implementation has hindered market-making functions necessary to ensure a healthy level of market liquidity. Combined with high liquid asset buffers, and limited to restore buffers during periods of stress, the Volcker Rule could result in pro-cyclical behavior and reinforce market volatility during periods of stress.
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> Treasury Report, p.8.

Commenters have noted the Volcker Rule's deficiencies. It is "fundamentally flawed" and will do considerably "more harm than good" for the economy.[37] Brookings Institute Fellow, Douglas J. Elliot concludes that the Volcker Rule tries "to eliminate excessive investment risk at our core financial institutions without measuring either the level of investment risk or the capacity of the institutions to handle the risk, which would tell us whether the risk was excessive. Instead, the rule focuses on the intent of the investment rather than its risk characteristics."[38]

Elliot's rationale turns on (i) the imprecision of regulators measuring investment intent; (ii) the arbitrary definition of "proprietary investments;" (iii) the creation of an overly complex set of regulations that micromanage banks; and (iv) the likelihood that arbitrary regulatory definitions will miss some of the more excessive risks that banks may actually take.[39] Industry criticism, among

35 In December 2013, five U.S. regulatory agencies — the FRB, the FDIC, the OCC the SEC and the Commodity Futures Trading Commission ("CFTC") (collectively, Volcker Agencies) — approved a final, rule (Final Rule or Regulations) implementing the so-called "Volcker Rule" enacted in the Dodd-Frank Act. While the Volcker Rule itself comprised a mere 11 pages in the Dodd-Frank Act, the Final Rule and preamble adopted by the Agencies take up 270 pages of the Federal Register. 79 Fed. Reg. No. 21, pgs. 5535–6076, Friday, January 31, 2014.

36 H.R. 10, 115th Cong. § 901 (2017).

37 Douglas J. Elliot, *The Volcker Rule and its Impact on the U.S. Economy* Hearing Before the U.S. House Fin.Servs. Comm.l (Jan. 18, 2012).

38 Id.

39 Id.

other things, argues that the Volcker Rule arbitrarily singles out U.S. financial companies for a form of regulation that will adversely impact market liquidity and job creation.[40]

> [R]egulators should give banks additional flexibility to adjust their determinations of the reasonable amount of inventory. In particular, for illiquid securities, banks should be permitted to focus less on predicting with precision the future demands of clients based on past patterns and should have greater leeway to anticipate changes in markets that could increase demand for such securities.
> Treasury Report, p. 75.

The Volcker Rule is intended to limit risks to the financial system that Congress believes may be created by: (i) proprietary trading operations of insured depository institutions, foreign banking entities with certain U.S. operations, and the affiliates of the foregoing entities (collectively, "banking entities") through a set of "proprietary trading restrictions"; and (ii) investments and certain relationships between banking entities and private equity and hedge funds (referred to as "covered funds") through a set of "covered fund restrictions."[41] Nevertheless, the lack of clarity in the definition of proprietary trading is an issue.

> The Volcker Rule's definition of proprietary trading turns on three tests — two of which are relatively straightforward, and one of which has generated undue complexity.... The "purpose test," by contrast, turns on a fact-intensive, subjective inquiry. To evaluate a trade under the purpose test, a banking entity is required to determine whether a trade was made principally for the purpose of short-term resale, benefitting from actual or expected short-term price movements, realizing short-term arbitrage profits, or hedging such a position.... The proprietary trading prohibition should be revised by eliminating the regulations' rebuttable presumption that financial positions held for fewer than 60 days constitute proprietary trading. In addition, policymakers should assess whether the purpose test should be eliminated altogether, to avoid requiring banks to dissect the intent of a trade.
> Treasury Report, p. 75.

Entities that fall within the definition of a "banking entity" are covered, and that definition is quite broad. Indeed, it extends far beyond any insured depository institution to include: (i) any company that controls an insured depository institution (which could be as little as 10% of a company's voting securities); (ii) any foreign bank that maintains a branch or agency in a State; (iii) any company that *controls* such a foreign bank, as well as any commercial lending company organized under State law that is a subsidiary of a foreign bank or its controlling company under Section 8 of the International Banking Act of 1978 (FBO); and (iv) any "affiliate" or "subsidiary" of any of these foregoing entities.[42] Even where the Volcker Rule permits a banking entity to retain sponsorship of or investment in a covered fund, pursuant to the exemptions discussed above, the banking entity and its affiliates are nevertheless prohibited from entering into certain "covered transactions" with those funds.

> If a foreign bank owns 26% of the "voting securities" or contributes a similar amount of the total capital of a company in the asset management, insurance, FinTech, or securities business, that company is a banking entity covered by the Volcker Rule. If an asset manager invests money for an unaffiliated entity that is subject to the Volcker Rule, that

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40 Trey Garrison, 5 Ways the Volcker Rule Will Destroy Job Creation, (Jan. 15, 2014).

41 Ledig, Robert H., et. al, *The Volcker Rule; Commentary and Analysis*, (2014), ThomsonReuters/Westlaw.

42 Entities that are designated as SIFIs by FSOC but are not banking entities are also subject to additional capital charges or other restrictions related to the risks and conflicts of interest that the Volcker Rule is intended to address. SIFIs, however, are not subject to the proprietary trading or covered fund restrictions that apply to banking entities.

asset manager may be made subject to the Volcker Rule. Moreover, the reach of Volcker goes beyond U.S. borders to capture foreign affiliates and subsidiaries.

The Treasury Report is also critical of the Volcker Rules' impact on capital formation:

> [T]he covered funds provisions of the Volcker Rule are not well-tailored to these objectives. Treasury believes that changes to the covered fund provisions can greatly assist in the formation of venture and other capital that is critical to fund economic growth opportunities. First, the covered funds definition is overly broad, including types of entities beyond private equity and hedge funds. The current approach of defining covered funds by reference to whether they would be deemed investment companies under the Investment Company Act but for certain specific exemptions requires banks to go through a highly technical, fact-specific legal analysis. Instead, regulators should adopt a simple definition that focuses on the characteristics of hedge funds and private equity funds with appropriate additional exemptions as needed.
> Treasury Report, p. 77.

The Volcker Rule's regulations also draw on the bank affiliate restrictions found in sections 23A and 23B of the Federal Reserve Act.[43] However, whereas section 23A merely places limits on covered transactions between affiliated entities, the Volcker Rule's so-called "Super 23A provision" prohibits such transactions altogether. The regulations' Section 23B provisions require that certain other transactions between a banking entity and a covered fund be substantially the same or at least as favorable to the banking entity as those prevailing at the time for comparable transactions with or involving unaffiliated companies, or in the absence of comparable transactions, on terms and under circumstances that in good faith would be offered to an unaffiliated party.

The U.S. Chamber of Commerce's Center for Capital Markets Competitiveness released a study in 2012 on the economic consequences of the Volcker Rule. It concluded that it would: (i) have a negative effect on market-making and liquidity; (ii) reduce network benefits of market-making for financial institutions; (iii) lead to higher costs of capital; (iv) make bank risk management less efficient; and (v) harm the ability of businesses to raise capital.[44] In 2014, the Office of the Comptroller of the Currency ("OCC") estimated that implementation of the Volcker Rule would cost the banks that it supervises between $413 million and $4.3 billion.[45] Most of the potential costs could come from the rule's limits on some collateralized loan obligations, with the largest impact being on banks with more than $10 billion in assets. "The range of [their] cost estimate primarily reflects the uncertainty of the final rule's impact on the market value of banks' investments," according to the OCC's report. After Volcker, the market value "could drop by up to 5.5 percent." There has indeed been a growing recognition of the need to reduce the cost of compliance with the Volcker Rule at the Federal Reserve Board.[46]

Understanding the costs, complexity and market impact that the Volcker Rule can have, Treasury proposes to limit the reach of its long arms:

> The agencies provided for progressively more stringent requirements based on a banking entity's size and involvement in covered activities but further tailoring would reduce burdens without significantly increasing risks at banking entities…[B]anks with less than $10 billion in assets should be exempted from the rule entirely and banking organizations not subject to the market risk capital rules should be exempt from the proprietary trading restrictions. Further, the existing "enhanced" compliance program under the regulations

43 12 U.S.C. § 371c (2010).

44 Anjan V. Thakor & John E. Simon, *The Economic Consequences of the Volcker Rule* Center for Capital Markets Competitiveness, U.S. Chamber of Commerce (2012).

45 OCC, Analysis of 12 CFR Part 44, Jesse Hamilton, *Volcker Rule Will Cost Banks Up to $4.3 Billion, OCC Says* (Mar. 21, 2014) (subscription required).

46 *Fed's Powell Suggests Tweaks to Volcker Rule to Reduce Cost*, June 22, 2017, MNI News.

should be focused in application so that it applies only to those banking entities with at least $10 billion in trading assets and liabilities on a consolidated basis, rather than the current application to all banking entities with over $50 billion in total consolidated assets.

Treasury Report, pp. 76-77

The absence of an economic cost-benefit analysis should be troubling to policy makers. Moreover, to the extent that the Volcker Rule engineers financial markets without full recognition of the financial consequences, the impact on U.S. liquidity could be significant. Indeed, the broad definition of "banking entities" that are covered by the rule include a vast array of direct and indirect domestic and global affiliates that gives the Volcker Rule a pervasive global impact. The Rule may overreach to the extent that its efforts to curtail risky proprietary and fund investment activities by banking organizations effectively channels bank investments into government securities, a trend that requires much more analysis before the full consequences can be understood.

Approaching Real Cost-Benefit Analyses

The Trump Administration proposes to make agency rulemaking subject to standardized cost-benefit analysis so that the costs of proposed rules can be empirically demonstrated to be reasonable when compared to their overall impact on safety, soundness and any corresponding benefits to the financial system.[47] This is a critical element in reforming the rulemaking process. Experts argue that deficient regulations can have a "multiplier effect on the regulated sector and are thus a potential source of systemic risk."[48] The Treasury echoes those sentiments:

> Federal financial regulatory agencies should follow the principles of transparency and public accountability by conducting rigorous cost-benefit analyses and making greater use of notices of proposed rulemakings to solicit public comment.
> Treasury Report, p. 17.

The President's executive orders make clear that the administration disfavors rules that will have a net negative economic effect, which suggests a reevaluation of the periodic reviews that are currently required under applicable law.[49] Moreover, the courts seem to be moving toward the conclusion that an agency cannot reasonably determine under the Administrative Procedure Act that its action is not arbitrary and capricious unless it has measured or projected the direct and indirect economic costs or benefits of its actions.[50]

As a partial remedy, the Treasury Report favors expanding Executive Order 12866's cost-benefit analysis requirements to independent financial regulatory agencies including the CFTC, SEC, FDIC, Federal Reserve, OCC and CFPB.

> Treasury recommends that financial regulatory agencies perform and make available for

47 Presidential Executive Order on Enforcing the Regulatory Reform Agenda (Feb. 24, 2017).

48 Rolf Nebel, *Regulations as a Source of Systemic Risk: The Need for Economic Impact Analysis.* The Geneva Paper on Risk and Insurance, Vol. 29 No. 2, 281 (April 2004) (subscription required).

49 The Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), Pub. L 104–208 (1996), codified at 12 U.S.C. 3311, requires that regulations prescribed by the Federal Financial Institutions Examination Council, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, and Board of Governors of the Federal Reserve System be reviewed by the agencies at least once every 10 years. The purpose of this review is to identify outdated, unnecessary or unduly burdensome regulations and consider how to reduce regulatory burden on insured depository institutions while, at the same time, ensuring their safety and soundness and the safety and soundness of the financial system. The second EGRPRA review is underway. This review provides an opportunity for the public to consider and comment on these regulations, individually and as a whole. The final report from the first EGRPRA review was submitted to the Congress in 2007.

50 Recent case law has begun to recognize this theory, even where the enabling statute does not explicitly require a cost benefit analysis. *MetLife, Inc. v. Financial Stability Oversight Council*, Civil Action # 15-0045 (RMC), March 30, 2016, *citing Michigan v. Environmental Protection Agency*, 135 S. Ct. 2699 (2015). The explanation that it is difficult to quantify the benefits of a rule to the extent that it may avert a financial loss or systemic crisis in the future that never occurs may in part be true. But that argument would support the adoption of almost any rule at any time. Surely, sophisticated economic models can be deployed to more scientifically calculate costs and benefits, as well as the likelihood that a range of risks may or may not arise and/or be averted by a particular rule or set of rules.
Rolf Nebel, *Regulations as a Source of Systemic Risk: The Need for Economic Impact Analysis.* The Geneva Paper on Risk and Insurance, Vol. 29 No. 2, 273 (April 2004) (subscription required).

> public comment a cost-benefit analysis with respect to all "economically significant" proposed regulations, as such term is used in Executive Order 12866.
>
> Treasury Report, p. 17.

The absence of any cost benefit analysis by the government with regard to the Dodd-Frank Act before it was adopted or since is remarkable. If a private company took such a corporate action in the same way, the board of directors would be criticized as imprudent.

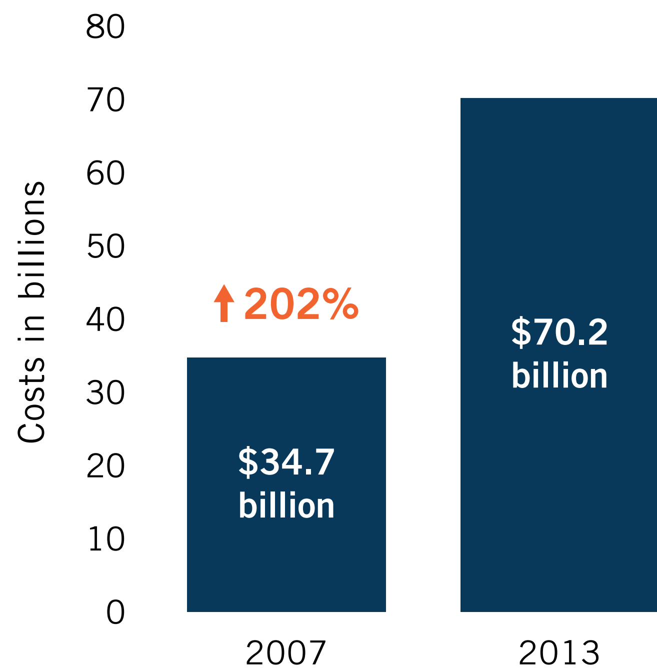
Financial services regulations aim to overcome or to mitigate market imperfections. However, regulatory actions sometimes cause their own distortions of market structures and market behavior that could even aggravate existing market deficiencies. Well-intentioned regulations could be counterproductive and undermine the very objective they were supposed to attain. Measuring the cost of macroeconomic distortions is difficult (at least in monetary terms). The essential issue is for policymakers to be conscious of the macroeconomic effects that regulatory action could have.[51]

While no governmental entity has ever comprehensively attempted to quantify the economic impact of Dodd-Frank, the Government Accountability Office ("GAO") has tinkered around with the subject at the margins. In 2013, it stated that while regulators have collected *some* data on these costs, no comprehensive data or analysis exists. Studies have estimated the economic impact of certain of the act's reforms, but their results vary widely and depend on key assumptions.[52] Similarly, in 2014, the GAO noted that although in certain circumstances financial regulators must consider costs and benefits of their rulemakings, they are *not* required to make a formal analysis of them.[53]

The Federal Reserve Bank of Minneapolis illustrated the financial impact of Dodd-Frank on community banks. It found that increased staffing needs at community banks could result in a reduction of 14 to 45 basis points in the median profitability among banks with less than $50 million in assets. The study projected that the reduction would result in between 6% and 33% of those banks becoming unprofitable.[54] A 2014 survey of 200 community banks by the Mercatus Center at George Mason University revealed that customers are seeing the effects of the increased regulatory burden through reduced product and service offerings, particularly mortgage credit availability.[55]

At the other end of the size spectrum, a study by Federal Financial Analytics in 2014 concluded that "quantifiable" regulatory costs faced by the six largest banks have doubled since the financial crisis, rising from $34.7 billion in 2007 to $70.2 billion in 2013.[56] The American Action Forum pegged the burden of compliance with Dodd-Frank at roughly $895 billion in reduced Gross Domestic Product, or $3,346 per working-age person

Quantifiable Regulatory Costs for the Six Largest Banks[56]



51 Nebel, at 276.

52 U.S. Gov't Accountability Off., GAO 13-180, Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act (2013).

53 U.S. Gov't Accountability Off., GAO 15-81, Regulators' Analytical and Coordination Efforts (2014).

54 Ron J. Feldman, et al., *Quantifying the Costs of Additional Regulation on Community Banks*, Fed. Res. Bank Minneapolis 13-3 (May 30, 2013).

55 Hester Pierce, et. al., How Are Small Banks Faring under Dodd-Frank? (Mercatus Center, George Mason Univ. Feb. 2014).

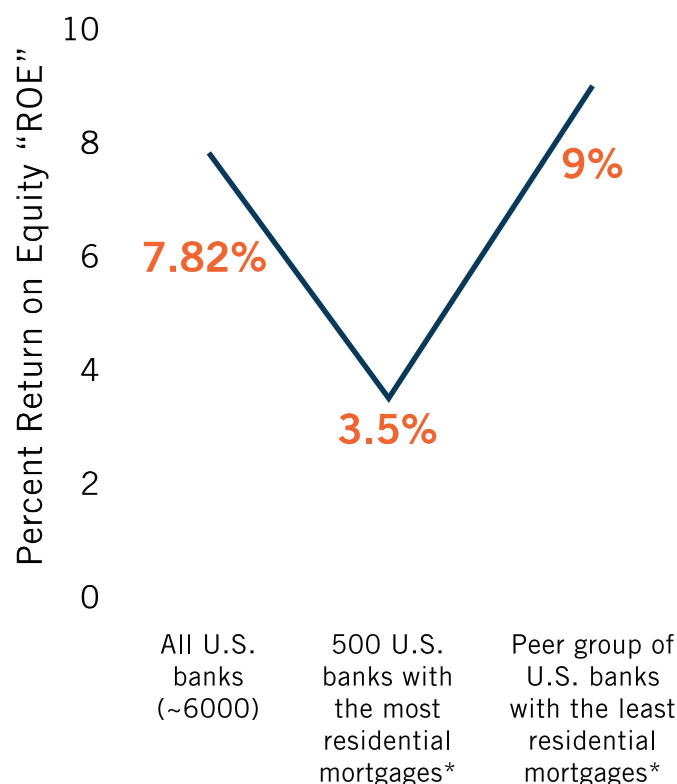
56 Saabira Chaudhuri, *The Cost of New Banking Regulation: $70.2 Billion*, *Wall St. J. Moneybeat*, (July 30, 2014).

between 2016 and 2025.[57] Similarly, Merrill Lynch recently released a report on the volatility in the stock market, noting that "[s]tricter financial regulation has caused banks to slash holdings in financial assets (dealer inventories currently total 2% of corporate bond fund assets, versus 20% 10 years ago)" and is "exacerbating the volatility that normally occurs when the Fed signals its intent to begin raising rates."[58] JPMorgan Chase's Chief of Regulatory Affairs underscored in a recent speech that banks and regulators are in unchartered waters with regard to market liquidity and a number of structural, economic and participant changes in the market.[59]

While these may all be somewhat anecdotal and may not accurately reflect the actual benefits and costs of Dodd-Frank, the point is that Dodd-Frank's costs and benefits must be measured. Richard J. Parsons, the author of "*Broke: America's Banking System*," contends that, as to the impact on the mortgage business, the impact is not just anecdotal. He notes that residential mortgage loans are the largest asset sitting on the balance sheets of U.S. banks — comprising 22% of all loans — but are the least profitable product. Mr. Parsons grouped together the 500 U.S. banks with the most residential mortgages relative to their total loans and compared those institutions to other peer groups and to the industry as a whole. While the nation's roughly 6,000 banks had a median return on equity ("ROE") of 7.82% through the third quarter of 2015, his peer group's median ROE was only 3.5%.

Meanwhile, the peer group of banks with the *lowest* ratio of residential loans to total loans had a median ROE of 9%. He ascribes that result, in part, to the fact that the 500 banks with the most mortgage loans on their books also are burdened with the highest capital ratios in the country. Moreover, the billions that the nation's biggest banks paid in legal settlements and fines associated with home mortgages are required to be input as operational losses into their regulatory capital calculations. Thus, large banks must show sufficient capital going forward, based on past experience, to cover 99.9% of potential losses.[60]

Median ROE of U.S. Banks[60]



57 Douglas Holtz-Eakin, *The Growth Consequences of Dodd-Frank, American Action Forum* (May. 6, 2015).

58 CIO Reports Investment Insights, "A Market Under Stress – We Believe This, Too, Will Pass", Merrill Lynch Bank of America, Chief Investment Officer, January 19, 2016.

59 Ian McKendry, *Regulation Only One Factor Hurting Market Liquidity: JPM Exec, American Banker*, March 7, 2016 (subscription required).

60 Parsons, Richard, "*Do Mortgages Still Have Earnings Potential*," *American Banker*, February 2, 2016.

Refocusing the Regulation of Systemic Stability

The purpose and goals of the FSOC will be re-evaluated by this Administration. Systemic regulation is indeed an important goal, but implementation has presented significant challenges. To date, FSOC's purpose and goals have been vaguely defined and difficult to understand. Like all regulation, it requires sound data, followed by a practical set of executable goals that will be implemented by experienced people. In short, policy makers should be able to say that if everything they have laid out as a plan works perfectly, the risk of systemic instability will be reduced and regulators will have a better opportunity to see those risks coming and mitigate their impact. FSOC has not achieved those goals to date.

Title I of Dodd-Frank requires the members of FSOC, who are the very regulators who manufacture the underlying regulations, to weigh the aggregate impact of their individual actions on national and global systemic stability. That is a difficult task for the most objective and confident policy makers. In nearly seven years, FSOC has designated four nonbank financial companies as "systemically important financial institutions" ("SIFIs") to be prudentially regulated by the FRB. However, only two remain as such. GE Capital decided to sell a substantial portion of its banking and financial businesses in order to scale down and, among other things, avoid the more restrictive regulation[61] that accompanies that status,[62] and a federal district court invalidated FSOC's designation of MetLife.[63]

It is difficult to argue — seven years after enactment of the Dodd-Frank Act — that the designation of two non-bank financial companies is the solution to the systemic concerns that erupted in the financial crisis. Since anticipating and avoiding systemic financial duress is a primary goal, if FSOC is to continue in some form,[64] its time would be better spent focusing less on SIFI designations of individual companies and more on developing comprehensive, technologically empowered data and effective early warning mechanisms that can provide regulators with the opportunity to take remedial actions to avert the next crisis. The CHOICE Act would eliminate the FSOC's ability to designate SIFIs and "financial market utilities" (FMUs) with discount window access altogether.

The CHOICE Act, while ending the SIFI designation regime overall, also states as its first key principle ending "too big to fail." The Treasury Report is somewhat coy on FSOC.

> Treasury recommends that Congress expand FSOC's authority to play a larger role in the coordination and direction of regulatory and supervisory policies. This can include giving [FSOC] the authority to appoint a lead regulator on any issue on which multiple agencies may have conflicting or overlapping regulatory jurisdiction.
>
> Treasury Report, p. 11.

While it seeks to broaden the scope of FSOC's powers, the example provided is very practical: use FSOC to monitor regulatory piling on so that one agency is designated to lead the change on matters that previously would include multiple federal agencies, in addition to numerous state authorities and attorneys general. The Report seems instructive, however, in what it does not say about the intended use of FSOC by the Administration.

61 Ian Katz and Katherine Chiglinsky, *MetLife CEO Raised Possibility of Breakup in 2014*, *Insurance Journal* (Jan. 28, 2016).

62 Matt Levine, GE Doesn't Want to Be a Big Bank Anymore (Apr. 10, 2015).

63 *Metlife, Inc v. Financial Stability Council*, D. D.C., Civil Action No. 15-cv-00045 (RMC) (2015).

64 The constituency of FSOC should be also reevaluated. Having the regulators who prescribe the rules for their segment of the financial services world come together to measure the effectiveness of those rules from a holistic perspective may not be the most objective way to oversee systemic stability.

As a result of Dodd-Frank's prudential and resolution provisions, the FRB and FDIC are reengineering the vertical regulation of large financial companies through macro-prudential tools, including: new capital standards, risk management requirements, liquidity and activities limitations, and single point of entry resolution plans. The theory appears to be that, if governments supervise large companies more closely, restrictively, and require greater capital and liquidity reserves, markets will be safer and the likelihood of financial collapse reduced. Substantial new costs are projected to accompany these new rules and SIFI designations.[65] Those costs will inevitably impact the array and pricing of financial services products available to consumers on Main Street. Yet, the benefits are not certain.

In August 2010, just one month after Dodd-Frank was enacted, the Basel Committee published an analysis of the regulation of systemic risk and its attendant benefits and costs.[66] It is a complex and somewhat opaque analysis which concludes that — assuming institutions pass on to borrowers the added costs arising from strengthened regulations — the net benefits from the reduction of the probability of a banking crisis through higher capital and liquidity standards could be measured in terms of "the long-run change in the yearly level of output from its pre-reform path."[67]

> Admittedly, the precise mapping between higher capital levels and stricter liquidity standards, on the one hand, and the reduction in the probability of crises, on the other, is quite uncertain. With this caveat, the sizeable gap between benefits and costs for a broad range of assumptions still suggests that in terms of the impact on output there is considerable room to tighten capital and liquidity requirements while still achieving positive net benefits.[68]

No less of an expert than William Dudley, President of the Federal Reserve Bank of New York, in an October 2015 conference at the Federal Reserve Bank of Boston, said that while "the use of macro-prudential tools holds promise, we are a long way from being able to successfully use such tools in the United States."[69] At the same conference, Adam Posen, President of the Peterson Institute for International Economics in Washington, D.C. said that the U.S. institutional framework for preventing crises was "likely to fail" and that FSOC was a "mess."[70]

Admittedly, there are many within and outside of government who would consider GE Capital's divestiture and downsizing to be a great success because it is a step in the direction of safer, smaller and more supervised financial markets. On the other hand, for those who measure the delicate balance between regulation and

65 Costs will be incurred as a result of the elimination of profitable activities deemed too risky (such as the indirect application of the Volcker Rule which prohibits proprietary trading and investments in covered funds), or the application of increased capital and compliance responsibilities.

66 See Basel Comm. On Banking Supervision, An Assessment of the Long-Term Economic Impact of Stronger Capital and Liquidity Requirements 2 (Aug. 2010).

67 See id.

68 Id. at 2-3. The study notes that the net benefits of the regulatory reforms are based on the expected yearly output/gain associated with the reduction in the frequency and severity of banking crises. "*Using the median estimate of the cumulative discounted costs of crises across all comparable studies, which is around 60%, each 1 percentage point reduction in the annual probability of a crisis yields an expected benefit per year equal to 0.6% of output when banking crises are allowed to have a permanent effect on real activity. Using the median estimate of losses when crises are seen to have only a temporary effect, which is around 20%, each 1 percentage point reduction in the annual probability of a crisis yields an expected benefit per year equal to 0.2% of output. …. each 1 percentage point increase in the capital ratio raises loan spreads by 13 basis points. Second, the additional cost of meeting the liquidity standard amounts to around 25 basis points in lending spreads when risk-weighted assets (RWA) are left unchanged; however, it drops to 14 basis points or less after taking account of the fall in RWA and the corresponding lower regulatory capital needs associated with the higher holdings of low-risk assets.*" This calculation relies on realistically estimating the expected discounted cost of a crisis because of stronger capital and liquidity requirements. The analysis does not, however, reflect the fact that Dodd-Frank repealed many of the authorities that the Federal Reserve and the FDIC used to control the collateral damage to the economy in the last crisis.

69 See also Craig Torres, *Dudley Says Work Needed on Tools to Avert Financial Crisis* (Oct. 3, 2015) (subscription required).

70 See supra note 68 (Torres).

free markets, this trend is the proverbial canary in the coal mine.

There are fundamental concerns with how the FSOC and the FSB have proceeded that raise serious questions regarding the efficacy of the process and measurability of the benefits that can offset the related costs. Indeed, as the District Court's opinion in the *MetLife* case may indicate, the hypothecation by FSOC of unsubstantiated risks — to which it then tethers a designation — effectively requires companies to shadowbox with fictional risks, is unfair, and arbitrary and capricious.[71]

Interestingly, FSOC's and FSB's analyses have not yet clearly distinguished between large companies that are the creators of market risk, and those that either invest in, absorb or manage that risk. Moreover, if FSOC is successful in lessening systemic risk creation in the U.S economy through designations of non-bank financial companies, its analysis will necessarily have to continuously be a dynamic process that factors the improvements into future analyses. Thus, the need to impose enhanced prudential regulation on additional companies should logically be commensurately lessened over time. As the Treasury Report indicates, U.S. engagement with the FSB must "prevent unnecessary regulatory standard-setting that could stifle financial information" and "assure the competitiveness of U.S. companies and markets."[72] Thus, the number and profile of companies needing to be designated should necessarily be under constant evaluation if and as each new designation occurs.

Disagreements among FSOC members are also a red flag. When some of the more knowledgeable members of FSOC from the insurance industry, for example, dissent on insurance company designations, one wonders what it all means.[73] Similarly, it is not clear how FSOC's voting members, who are the heads of the constituent agencies, not the agencies themselves, should be and are interacting with their fellow commissioners, board members and staffs.[74]

Finally, FSOC has been designating companies for enhanced regulation without clearly identifying a path out of that regulatory status, even though Dodd-Frank requires an annual review of the designation status of each company.

The future of FSOC in this Administration is unclear. At the very least, we expect that designations of new SIFIs will be the exception and that it will be used by Treasury as a means of coordinating its message and policies throughout the federal financial regulators that sit on it.

71 See, e.g., Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) §§153- 154, 12 U.S.C. §§5343- 5344 (2010). See also *MetLife Inc. v. Financial Stability Oversight Council*, No. 15 Civ. 00045 (D.D.C Mar. 30, 2016).

72 Treasury Report, p. 55.

73 See, e.g., Edward J. DeMarco, *Views of the Acting Director of the Federal Housing Finance Agency* (Sept. 19, 2013) (dissenting from the majority in voting against a final determination to designate Prudential Financial) by Edward J. DeMarco.

74 Section 120 authorizes FSOC to recommend heightened regulatory standards to a primary financial regulator, but it is required to consult with that agency (not just the agency head) and conduct a cost/benefit analysis. There are several consultation requirements in Title I the DFA, but it appears that differences among commissioners and other principals of various federal and state agencies are not being reflected in the deliberations of FSOC. See Konstantine Kastens, New SEC Commissioner Takes Aim at FSOC on MMF Regulation (2014).

A Shift to Principles-Based Regulation

In 1864, the National Bank Act needed just 18 pages of text to establish the national banking system. The Dodd-Frank Act used 800 pages in 2010 to reconfigure banking and securities regulation and reinforce the transition to a rules-based approach to financial regulation. Hundreds of new rules have followed.

1864
National Bank Act
18 pages

2010
Dodd-Frank Act
849 pages

Both rules-based and principle-based systems of regulation have merit, but the balance between them must be carefully calibrated to the reality of the marketplace. Rules-based systems cannot substitute for situational analysis based on sound judgment and experience and may camouflage some critical problems. Still, the regulatory pendulum seems to have swung too far in the direction of a rules-based system given the relative ease of throwing new rules at a problem and the apparent sense of confidence that the imposition of such rules can suggest.

As more detailed laws are enacted that rely less on regulatory discretion, the degree of compliance difficulty rises, as well as the costs of that regulation. Rules-based regulation tends to foster a more adversarial cat-and-mouse game. In such situations, the search for loopholes by a regulated entity is a common exercise, using time and resources that might be better deployed to maximize safety and soundness. Perhaps more pernicious, however, is the extent to which the plethora of rules creates a false sense of security.[75]

A principles-based regulatory system requires sound regulatory judgment, deep expertise and the authority and willingness of regulators to make judgments that will help a bank and the system steer a path toward safety and soundness under a variety of financial circumstances. It underscores the joint effort by regulator and bank to point the bank in the direction of safe and sound operation. Recalibrating this balance of regulation is not a simple matter, but at this point, it is critical.

We would expect to see this Administration devote significant administrative time and energy to the creation of extensive real-time data bases upon which regulators can make judgments. We would also hope that the Administration devote additional resources to the hiring and retention of talent with the requisite expertise.

75 Additionally, the propensity to regulate through “guidance” that is not subject to notice and comment rulemaking procedures often becomes a way of doing an end-around what should be a formal promulgation of rules, and permits agencies to effectively issue pronouncements that for all intents and purposes are enforced as a regulations.

Reevaluation of Efforts to Harmonize Global Regulation

For the last 30 years, there has been an effort to harmonize global financial regulation. We would expect to see a major reevaluation of that effort with an eye on rationalizing regulatory decisions with the economic conditions on the ground and ensuring consistent implementation around the globe. The Treasury report notes this incongruity:

> International regulatory standards should only be implemented through consideration of their alignment with domestic objectives and should be carefully and appropriately tailored to meet the needs of the U.S. financial services industry and the American people.
> Treasury Report, p. 16.

As competition has become global in nature, the value of international standards has become obvious. However, questions have been raised as to whether the implementation and enforcement of those standards is occurring in foreign countries as robustly and consistently as they are in the U.S. At the same time, there is reason to question whether some of the international standards that were adopted should have been adopted given the problematic impact that full implementation of such standards would have in many European countries. Consider a simple fact: in the last crisis, the U.S. closed some 450 banks due to their failing financial condition and provided strings-attached financial assistance to hundreds more. Despite being no healthier, we can count on one — maybe two — hands all of the banks that were seized and/or closed in Europe and Asia.[76]

The European Union indicated that it will *not* follow the Basel Committee's recommendation on standardized credit or operational market risk rules for fear of stifling economic growth. The *American Banker* characterized it as a "stunning move."[77] Similarly, the use of the FSB as a stalking horse in the U.S. to legitimize the need for tougher standards should be closely reevaluated. It has not gone unnoticed that the FSB's efforts at tightening the regulation of asset management firms and funds, for example, focuses on U.S.-based companies that are already subject to extensive regulation in the U.S. Moreover, such U.S. regulation, unlike FSB rules, are the result of congressionally enacted statutes and formal rulemakings subject to legal challenge in a court of law.

The Treasury Report is somewhat vague when it comes to international standards. It generally supports efforts to finalize remaining Basel reforms including establishing a global risk-based capital floor because it believes that will promote "a more level playing field for U.S. firms" and strengthen the capital adequacy of global banks. That begs the question whether implementation can be consistent from country to country.

For example, foreign jurisdictions have shown an inclination to use forbearance where warranted by economic conditions. After the savings and loan crisis of the 1980s and 1990s, when the application of regulatory forbearance and discretion became unforgiveable

76 There is no doubt that many banking systems outside the United States are more concentrated. Some countries may have less than a dozen significant banks, so that closing one of them becomes a more difficult matter than closing a community bank in Arkansas, for example. But that does not eliminate the fact that if banks in foreign countries operate in an economic environment where their failures may not necessarily lead to an enhanced regulatory reaction, that difference in market discipline will influence their assumption of risk. Any time that there is a "heads I win, tails you lose scenario," the risk-reward model is impacted.

77 See *The American Banker*.

regulatory sins in the U.S., the regulatory system lost a large part of its ability to customize the response to the actual economic factors. At the same time, efforts by the U.S. to adopt and implement international standards that may cause economic pain in other countries nearly assures that their implementation will likely be delayed by those countries.[78] In those cases, the harmonization that is sought may not be achieved, and certainly not synchronously.

> The banking agencies should carefully consider the implications on U.S. credit intermediation and systemic risk from the implementation in the United States of a revised standardized approach for credit risk under the Basel III capital framework. U.S. regulators should provide clarity on how the U.S.-specific adoption of any new Basel standards will affect capital requirements and risk-weighted asset calculations for U.S. firms.
> Treasury Report, p. 56.

Finally, despite the defects in the adoption and implementation of international standards, the propensity of U.S. regulators to "gold-plate" those standards and make them even more rigorous only adds to the competitive equality and jurisdictional confusion that U.S financial institutions believe favorably impact international competitors. The Treasury Report notes that "U.S. firms currently operate with high levels of capital compared to their international counterparts" and are "subject to a risk-based capital floor, while many foreign competitors do not adhere to such a standard."[79] As a result of such imbalances, the CHOICE Act offers an off-ramp from Basel III capital and liquidity standards for banking organizations that make a qualifying capital election.[80]

78 Silla Brush, Alexander Weber, and Boris Groendahl, Global Bank Capital-Rule Revamp Postponed as Europe Digs In (Jan. 3, 2017).

79 Treasury Report, p. 56.

80 H.R. 10, 115th Cong. § 601 (2017).

Reevaluation of Title II of Dodd-Frank and the Extraordinary Powers Needed by Regulators to Resolve Financial Crises

During the financial crisis, the FRB and FDIC used an array of extraordinary emergency powers in the Federal Reserve Act and the Federal Deposit Insurance Act to blunt the impact of the growing liquidity crisis. The Federal Reserve used section 13(3) of the Federal Reserve Act to institute broad-based emergency lending programs for participants who were otherwise unable to obtain credit due to "unusual or exigent circumstances." Because Congress perceived the use of these powers as an affirmation of the "Too-Big-To-Fail" ("TBTF") doctrine, and thereby favoritism of large banks, it repealed or limited the FRB's and FDIC's extraordinary powers in the Dodd-Frank Act. Dodd-Frank amended 13(3) to require prior approval of the treasury authority and emphasized that any programs be "broad-based" and not tailored as needed to one or few institutions. So, the next time that large financial institutions begin to melt down, the FRB and FDIC may not be able to take the same kinds of actions nor make the same kinds of capital and liquidity injections to stabilize them and the financial markets without going through some mental gymnastics under the current state of the law. Congress' action in Dodd-Frank seems to have been impacted by a dislike for how the TBTF doctrine has been perceived politically, but our financial system should not be left dangling because regulators are prohibited from taking action because it may be perceived as favoring TBTF institutions. Frankly, TBTF has always been a part of the financial system, so it may make more sense to regulate with that as a given fact, rather than imagining that in the next crisis, the largest financial companies in the world will be seized and liquidated by a regulatory structure that has never done it before.

Additionally, although the FDIC has never acted as receiver for any entity other than a federally insured bank — and never where a bank did significantly more than take deposits, make loans, and issue mortgage-backed securities — Congress authorized the Treasury in Dodd-Frank to appoint the FDIC as receiver for the largest, non-bank financial companies in the country and, by extension, the world. Whether the FDIC has the ability and resources to undertake such a task is open to debate. More significantly, the capital markets have not fully appreciated or anticipated such a receivership action in their pricing of non-bank financial stocks. The first time that this authority is used, markets may immediately reprice the securities of such large companies based on revised expectations in an FDIC receivership, which will typically look nothing like a traditional bankruptcy.

The Financial CHOICE Act, in the first section of its first title, repeals all of Title II of the Dodd-Frank Act and its Orderly Liquidation Authority ("OLA"). The CHOICE Act would add a new chapter to the Bankruptcy code designed to accommodate the resolution of a large, complex financial institution.[81] The CHOICE Act's preference for bankruptcy over OLA is based on three principles: the competence and impartiality of bankruptcy judges, the certainty and predictability of bankruptcy for affected parties, and the impossibility of a Bear Stearns-AIG-style taxpayer-funded bailout, liquidation or reorganization.

81 H.R. 10, 115th Cong. §§ 121-23 (2017).

Moving Toward a Clearer Coherent Financial Services Strategy and Regulatory Structure

Financial executives need certainty as they blend applicable market and regulatory factors to define a path to profitability and safe and sound operation. That certainty has not existed for some time. For example, Dodd-Frank increased regulation on the premise that it would necessarily lead to a safer and sounder financial system yet it created a regulatory bias against large institutions, an operational obstacle course for community-based institutions, and a regulatory tax on the growth of all banks.[82] Dodd-Frank failed to provide banks with a clear vision of how financial services will be permitted to be delivered in this country long-term. Do policy makers believe that the community bank, large bank or some different model of financial product and service delivery is favored? Financial executives deserve a clear and consistent picture of government policies so they can steer a course to profitability. The Trump Administration is likely to attempt to provide a clearer picture than we have had in many years.

In this regard, the regulatory burden on community banks is likely to be recalibrated in light of the fact that: (i) the failure of community banks do not cause market disruption or impact systemic stability; (ii) community banks had little or no role in the last financial crisis; and (iii) community banks are the backbone of Main Street America and local economies will suffer economic deprivation without vibrant community banking. More focused supervision of the simpler business model of community banks (e.g., interest rate risk, a fundamental risk in community banking) could potentially produce the same benefits as the current system but at a much lower cost. Empirical evidence since the enactment of Dodd-Frank suggests that arbitrary asset thresholds for increased regulation should be significantly increased.

The CHOICE Act attempts to resolve uncertainty be reducing complexity. It removes the sheer weight, volume and complexity of regulation for community financial institutions to encourage them to provide credit to small businesses and consumers. Its drafters sought to eliminate the “regulatory taxes” imposed by Dodd-Frank that have been passed through to small businesses and reject its creation of a “too small to succeed” class of community banks.[83]

The Treasury Report indicates that the uncertainty resulting from the post-Dodd-Frank regulatory approaches has fostered risk-aversion among lenders, particularly residential mortgage lending and leveraged lending.[84] In leveraged lending, 2013 guidance left the definition of leveraged lending and penalties for noncompliance unclear, which ultimately resulted in fewer leveraged loans.[85]

The Administration appears to be coalescing on the belief that there are too many banking agencies involved in the regulatory process. While strong regulation of financial institutions is necessary, regulatory redundancy and piling-on is wasteful and counterproductive.

Conventional wisdom suggests that several approaches be considered. Until statutory solutions can be enacted, such as the expansion of FSOC jurisdiction to mediate actions involving multiple regulatory agencies, the banking agencies, DOJ, SEC, Treasury and each of the state banking, securities and consumer protection agencies should consider entering into regulatory treaties

82 See David L Ansell, Thomas P. Vartanian, *“To Grow Or Not to Grow: Regulatory Burdens Increase as Banks Get Bigger,” NY Law Journal*, December 13, 2013.

83 CHOICE Act Comprehensive Summary, p. 6.

84 Treasury Report, pp. 93, 104.

85 Treasury Report, p. 104.

or memoranda of understanding allocating and assigning jurisdiction so that one agency takes the lead on behalf of others to resolve an enforcement or regulatory matter where there may be concurrent jurisdiction. These agreements should also cover how concurrent civil and criminal enforcement proceedings should maintain ultimate efficiency while not sacrificing the various governmental agencies' interests in remediating an issue and maintaining a safe and sound banking system.

The Treasury Report suggests that coordination of the different regulators should be FSOC's role. Similarly, the CHOICE Act instructs FSOC to conduct overarching monitoring of market developments, facilitate information sharing and regulatory coordination among regulators, coordinate with regulators to identify systemic risks, and report to Congress on behalf of the bank regulators. Either or both of those approaches would reduce the number of different agencies pursuing actions against banks regarding the same facts.

Finally, it might be time to unpack the overlapping federal regulatory structure to make it more efficient and less redundant. The Treasury Report recommends that Congress "take action to reduce fragmentation, overlap, and duplication in the U.S. regulatory structure. This could include consolidating regulators with similar missions and more clearly defining regulatory mandates."

> There are numerous examples of overlap in the depository regulatory framework. For example, state and federal regulators (including the FDIC and the Federal Reserve) share oversight of the safety and soundness of state-chartered banks. As another example, as administrator of the Deposit Insurance Fund, the FDIC has backup supervisory authorities over all banks and thrifts that are federally insured. Thus, there is overlap between the FDIC, the Federal Reserve, the OCC, and state banking regulators regarding supervisory responsibilities. For credit unions, there are elements of overlap between the NCUA, as consolidated regulator, and the CFPB and state regulators. These areas of overlap can create confusion and increased costs for supervised entities, as well as increased burdens for the regulatory agencies themselves. Although Dodd-Frank created the CFPB in part to rectify the fragmentation of authority among regulators with respect to consumer financial protection, its authority on such matters is not unique and is duplicative with the supervisory activities of the Federal Reserve, OCC, FDIC, NCUA, and state regulators.
>
> Treasury Report, p. 30.

A more streamlined regulatory authority will enhance the government's ability to react and remediate future financial crises. Perhaps all supervision, regulation and examination of financial institutions and their holding companies will be moved to the OCC, which would then be reestablished as a multi-member commission. Management of the Deposit Insurance Fund and receivership and conservatorship functions for insured depository institutions could remain with the FDIC, while monetary policy remains with the FRB. The FDIC and the FRB could fill in the information deficiencies they may have by serving as members of the new combined banking commission.

The Future of Living Wills

Section 165(d) of the Dodd-Frank Act requires the largest banks and designated SIFIs, among others, to construct resolution plans — or living wills. The stated purpose of the living will is to plan for the rapid and orderly resolution of the company in the event of material financial distress or failure. The plan is required to inventory the company's affiliates and subsidiaries and its contractual obligations, counterparty exposures and other information required by the FDIC and FRB.

Since 2010, large banks have been devoting enormous resources to the development of these documents, which generally fill tens of thousands of pages. This exercise of developing these documents over the last five years has been instructive to the banks in terms of forcing them to understand and inventory their company and the related risks inherent in their balance sheet and market contracts. However, there appears to be a significant gap between the resources required to complete satisfactory living wills, a target that has proven to be quite illusive, and the benefits of the final plan.

The Treasury Report favors a biannual living will process over the current annual process. The Report also recommends limiting its application only to those banking organizations subject to enhanced prudential standards and which are sufficiently complex.[86] The current $50 billion asset threshold can be preserved, but the Report recommends tailoring.

> Treasury recommends that the living will process be made a two year cycle rather than the current annual process, which is not required by Dodd-Frank. Treasury also recommends that the threshold for participation in the living will process be revised to match the revised threshold for application of the enhanced prudential standards. This change would only include those banks that have a sufficient level of complexity as to justify the living will requirement. Other changes Treasury recommends include improving the quality and transparency of guidance and promoting better regulatory harmonization and timely response following submission of living wills.
> Treasury Report, p. 13.

As beneficial as living wills may be to their creators and the regulators, there are still significant unresolved issues with regard to the practical utility that they can have in an actual crisis.

First, most of the institutions that are required to prepare and file satisfactory living wills have global operations whose failures would be international events that would trigger conflicting claims by multiple governments, legal jurisdictions and private claimants around the world. Until the FDIC and FRB can be confident that those entities will agree on the receivership and disposition of the assets of global organizations in operating within their borders, there can be little confidence that the full spectrum of expectations and orderly disposition can be achieved in the event of the failure of one of those organizations.

Second, overlapping rules over and above the living wills process can impose redundant costs. Most GSIBs plan to be resolved under the single-point-of-entry ("SPOE") resolution strategy where the losses across a U.S. GSIB are borne by shareholders and long-term debtholders of the GSIB's now-failed and bankrupt holding company. SPOE resolution confines the potential for loss at the holding company level and lessens systemic consequences of a bank's failure by allowing the operating subsidiaries to remain open. The Clearing House Association recommends that any firm using the SPOE strategy and is in compliance with Total Loss-Absorbing Capital ("TLAC") requirements should not then also be subject to an additional incremental liquidity requirement at the operating subsidiary level. The rules-based approach to resolution built the TLAC rule, the qualified financial contract recordkeeping rule and deposit recordkeeping rules on top of the living wills process.

86 Treasury Report, p. 13.

Lastly, the Federal Reserve closely guards the scenarios against which the living wills are tested. Under the current system, the banks are notified annually about the scenarios so that they cannot arrange assets in a way designed merely to pass the test. The CHOICE Act, the Treasury Report and the Clearing House Association all suggest an opportunity for notice and comment. Notice and comment will provide advanced warning to the banks, would allow them to address whether the scenarios being tested are possible or even conceivable, and facilitate feedback to indicate perceived weaknesses that could be most usefully tested. The CHOICE Act would also require the Federal Reserve to opine on the resolution plans within six months of submission.

Without reforms that recognize the reality of internationally disputed assets, the redundancy of a liquidity requirement on a subsidiary of an SPOE-resolving holding company, and the efficiencies created by transparency, a living will serves a limited purpose other than as a hope certificate that will provide the regulators a road map to at least locate the assets and identify the jurisdictional issues.

Clarify FDIC Policy Regarding Suits Against Failed Bank Directors and Officers

The Treasury Report underscores that boards of directors play a critical role in oversight and recommends the rules for their accountability must be appropriately defined after an inter-agency review of the aggregate requirements in order to balance discipline with attracting and retaining high-quality talent.[87] It is time that the government considered a range of issues with regard to this topic.

For example, over time, FDIC receivership practices appear to have been unduly influenced by the FDIC receiver's quest for dollars — often represented by insurance coverage — to offset its losses, as opposed to holding people responsible for the decisions they actually made and the acts they actually took. While the program's focus was originally on finding and punishing wrongdoers, it has devolved into a process where the facts don't matter if there is insurance coverage or personal assets for the FDIC to take to offset the loss it incurred in resolving the failed bank. That has completely changed the risk reward ratio that was originally intended.[88] To the extent that D&Os believe that they will be sued no matter what they do if their bank fails, which seems to be their belief today, the intent of the policy is diluted and the incentive not to throw a financial Hail Mary in the closing days of the institution's life is actually undercut. That is completely contrary to the market discipline that the FDIC's D&O policy is meant to affirm. The program should be reevaluated and amended to ensure that it is not simply a tax collection exercise, but the execution of justice based on actual facts. That will build back in the original program incentives to encourage directors to act prudently and not take imprudent risks.

87 Treasury Report, pp. 16-17.

88 While General Counsel of the FSLIC and FHLBB in 1982, Mr. Vartanian authored the original policy requiring the FSLIC to investigate the actions of individuals that may have caused the losses that lead to the failure of an insured institutions. See, "*Uncle sam is set to sue officers of failed thrifts*," *Business Week*, November 15, 1982, p. 43.

Modernization of Bank Control Rules

Nothing was more important in the last crisis than the need for and availability of new capital. Nothing proved to be more problematic — both in drafting and interpretation — than the antiquated control rules that the FRB and FDIC implemented. If regulators actually want to encourage capital investments in regulated financial institutions, the door needs to be propped open a little wider. The Treasury Report is silent on this issue.

The Bank Holding Company Act and the Federal Change in Bank Control Act set forth the standards for investment in and "control" of a federally insured bank by shareholders. The standards established in those laws, which have applied for at least four decades, are based on, among other things, the understanding that those who control banks and enjoy the privilege of federal deposit insurance and the trust it symbolizes to consumers must be scrutinized with regard to their integrity and purpose. Accordingly, regulators have promulgated rules and policies that presume that an investment of as little as 10% (and sometimes as low as 5%) ownership in the voting stock of a bank or bank holding company, rather than the 25% set forth in these statutes, is a proxy for control and triggers the need for regulatory review and approval.[89] Moreover, regulators generally require that investors with more than 10% of the voting stock execute passivity agreements, stripping them of their customary shareholder rights. These limitations have had negative effects, and it is not clear that they have improved the quality of bank control.

First, capital investment in banks is discouraged given the limited financial role that investors can have. Second, bank control rules have created an environment unlike any in the U.S. where banking executives are significantly insulated from shareholder influence and pressure. That is both good and bad: Good to the extent that shareholders who have not been screened should not be determining the future of an FDIC-insured depository but bad to the extent that the discipline of the marketplace may be reduced by the limited influence that shareholders can have.

Banks today operate in markets that have seen significant changes, including vast improvements in the corporate governance of public companies since 2001. It is not likely that a 9.9% investor can control a bank without violating some other laws. If the concern is that others will follow a significant investor and support its actions, acting in concert rules can be adjusted to deal with those situations. The rules were made even more cumbersome during the Great Recession when private equity and hedge fund investors were targeted in guidance issued by the FDIC and standards employed by the FRB that largely disinvited them from investing capital in troubled and failed banks on the same terms that other investors could.[90]

A simple increase in the current control thresholds to the statutory standard of 25% could make a meaningful difference in the ability of banks to attract capital, without diluting the oversight that investors who wish to control a bank should have. Further evaluation may confirm that an increase of the 25%-statutory threshold by Congress would better balance the concept of control in today's markets with the need for capital in the industry.

89 See Vartanian, Ansell and Ledig, "*The Bank Investor's Survival Guide*", 2016 (Dechert); the FDIC and the FRB have each adopted policy statements with regard to control limitations on investors in insured banks and their holding companies. See FDIC Statement of Policy on Qualifications for Failed Bank Acquisitions and Statement of Policy on Qualifications for Failed Bank Acquisitions; and the FRB's Policy Statement on Equity Investments in Banks and Bank Holding Companies, 12 CFR 225.144.

90 See FDIC Statement of Policy on Qualifications for Failed Bank Acquisitions, 74 Fed. Reg. 45440 et seq.; see also "Q&As Posted In January 2010."

The Immediacy of the Cybersecurity Threat

Cybersecurity is a serious threat and compliance issue for financial institutions. Technology's role in banking has increased dramatically, which increases the potential effects of major cyber incidents such as data breaches or system crashes. To address fast-developing cybersecurity threats, the regulatory system must be as informed, agile and effective as the institutions they regulate.

The Treasury Report acknowledges the significant cybersecurity risks to financial institutions and calls the prevention of operational disruption a "critical component of financial regulation" yet identifies regulatory fragmentation and overlap in its regulation and oversight.[91] To address these problems, the Report recommends that regulators harmonize regulations and the specific rules and guidance.

The Clearing House Report acknowledges the same cybersecurity risks, but emphasizes, in agreement with a 2016 Presidential commission report on cybersecurity, a collaborative public-private partnership would be more efficient and productive than rulemaking. While cybersecurity risks are numerous and significant, reducing the industry's increasing compliance cost with the overlapping and conflicting regulations remains a core priority. The Clearing House Report calls for banking regulators to cease their cybersecurity rulemaking efforts begun in 2016 and defer to the Department of Homeland Security, the Office of Management and Budget, and the National Institute of Standards and Technology for broad cybersecurity guidelines and frameworks.[92]

Where it is already acknowledged that cybersecurity is a dynamic issue, the Treasury and the industry both agree on a principles-based solution rather than a rules-based regime.

91 Treasury Report, p. 31.

92 Clearing House Report, p. 45.

Conclusion: Always a Question of Balance

Since the enactment of Dodd-Frank, the best efforts of Congress and the regulators have produced a hodge-podge of compliance and operating challenges that, by any stretch of the imagination, is having a significant impact on banks, the cost of financial services in the U.S. and the future of the U.S. economy.

No one can reasonably argue that banks, the beneficiaries of federal deposit insurance and all that it connotes, should not be highly regulated. No one can argue that banks should not be held to task when they do not respect the relationship of trust that they enjoy with their consumers. The question today, however, is whether we can make bank regulation smarter for the benefit of all of us.

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