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Financial CHOICE Act (H.R. 5983) as Guide to Possible Financial Regulatory Reform, Including "Dodd-Frank Repeal"

By Timothy P. Mohan and Robert E. Lockner*

The authors of this article highlight some of the important provisions of the Financial CHOICE Act (H.R. 5983), introduced last summer by the chairman of the House Financial Services Committee, which is the best indication of Republican Congressional aspirations for such reform.

With Republicans retaining control of both chambers of Congress and Donald Trump elected President, the prospects for financial regulatory reform have changed. Many observers point to the Financial CHOICE[1] Act (H.R. 5983), introduced last summer by Representative Jeb Hensarling, chairman of the House Financial Services Committee, as the best indication of Republican Congressional aspirations for such reform. Rep. Hensarling has already indicated he is interested in introducing a "2.0" version of the bill when the new Congress convenes. There has recently been speculation that the selection of Steven Mnuchin as Secretary of the Treasury suggests the Trump administration might not support financial reform as wide ranging as the CHOICE Act.

BACKGROUND

H.R. 5983 was approved by the Financial Services Committee in September.[2] Most reports of the CHOICE Act have concentrated on two controversial

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1 This is an acronym for Creating Hope and Opportunity for Investors, Consumers, and Entrepreneurs.

2 Although the bill could have received a House vote last year, it certainly was not taken up by the Senate before the new Congress convened. In any case, President Obama would have certainly vetoed the bill if it were passed by both houses of Congress. Hensarling released a detailed outline and justification, *available at* http://financialservices.house.gov/uploadedfiles/financial_choice_act_comprehensive_outline.pdf, for the bill on June 23, 2106. He (and several Republican co-sponsors) introduced H.R. 5983 on September 9, after a July House Financial Services Committee hearing on the June outline. The Committee approved (i.e., "reported out")

features: (1) a provision for banks and bank holding companies to exempt themselves from Dodd-Frank enhanced prudential standards and other regulations by maintaining an adjusted leverage ratio of 10 percent, and (2) the reformation of the Consumer Financial Protection Bureau ("CFPB") into a five member commission with more limited authority and a dual mandate to protect consumers and to enhance consumer choice and competition by providers of consumer finance.

The bill, however, is much broader in repealing numerous Dodd-Frank provisions (e.g., Orderly Liquidation Authority, Federal Reserve supervision of "systemically important" nonbank financial companies and financial utilities, the Volcker Rule, risk retention requirements for all securitizations except those limited to residential mortgages, the Durbin Amendment, the Office of Financial Research, and various executive compensation and rating agency provisions), reorganizing and imposing new duties on federal financial regulators, subjecting financial regulations to greater cost-benefit analyses and Congressional and judicial review, and modifying numerous other federal legal standards and penalties.

The bill is not a full repeal of Dodd-Frank. Many Dodd-Frank provisions would not be modified. Both the Financial Stability Oversight Council ("FSOC") and the CFPB would continue, but in different forms and with reduced powers. The bill is also not limited to Dodd-Frank matters. In particular, the bill would dramatically affect the authority of federal financial regulators by subjecting their actions to strict cost-benefit analysis and review requirements, broader judicial review, and (for "major rules") a new requirement that they receive Congressional approval. Similarly, the bill's restrictions on Federal Reserve monetary policy would dramatically change how the Federal Open Market Committee ("FOMC") operates.

IMPORTANT PROVISIONS BY TITLE

Like Dodd-Frank, the lengthy bill is divided into titles. For each of the 11 titles, this article highlights some of the important provisions.

Title I: Potential Replacement of Other Regulations by a Single Leverage Limit

The most publicized and criticized provision of the bill is this "off ramp from

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H.R. 5983, *available at* https://www.congress.gov/114/bills/hr5983/BILLS-114hr5983ih.pdf, on September 13, 2016, in a 30-26 vote, http://financialservices.house.gov/uploadedfiles/crpt-114-hmtg-ba00-fc125-20160913.pdf, with all Republican members except one approving and all Democratic members joining that one Republican in opposing the bill.

Dodd-Frank and Basel III" for banks and bank holding companies ("qualified banking organizations") willing to maintain a 10 percent ratio of "CET 1" to "total leverage exposure." Critics have argued that the 10 percent limit is weak because large banks already maintain close to 10 percent leverage ratios and such ratios are subject to manipulation.[3]

The "off ramp" for all but "traditional banks," however, is much more restrictive than the simple "leverage ratio" currently reported by U.S. banks that measures "tier 1 capital" against adjusted "average total consolidated assets." By instead measuring "common equity Tier 1" ("CET 1") capital against Basel III "total leverage exposure" (which adds off-balance sheet exposures), the 10 percent minimum would require the largest four U.S. bank holding companies to increase their existing CET 1 capital levels by roughly $370 billion (an increase of between 37.5 percent and 72.9 percent for each of the four).[4] Banks

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[3] Critics have complained that the leverage test would only require compliance at the end of a calendar quarter and have cited "window dressing" schemes to reduce reported assets for such last day of a reporting period. The bill refers to the "quarterly leverage ratio" as that determined "on the last day" of a quarter, but the bill also defines "total leverage exposure" by reference to that term's definition in federal banking regulations as in effect on January 1, 2015. Those regulations are intended to prevent such "window dressing" by mandating that the exposure is computed as the daily average of on-balance sheet consolidated assets during the quarter ending on such date and the average of off-balance sheet exposures computed for the last day of each of the three months in that quarter.

[4] According to their "Pillar 3 Regulatory Capital Disclosures" for the quarterly period ended September 30, 2016, the four largest US bank holding companies had the following reported CET 1 and TLE levels:

> JP Morgan Chase: CET 1=$181.606 billion. TLE=$3.140733 trillion. CET 1/TLE=5.78%. To reach 10% ratio requires CET 1=$314.0733 billion. Required CET 1 increase=$132.4673 billion or 72.94% of reported $181.606 billion.
>
> Bank of America: CET 1=$169.925 billion. TLE=$2.704794 trillion. CET 1/TLE=6.2824%. To reach 10% ratio requires CET 1=$270.4794 billion. Required CET 1 increase=$100.5544 billion or 59.18% of reported $169.925 billion.
>
> Citigroup (incorporating FFIEC 101 figures): CET 1=$172.046 billion. TLE=$2.366219 trillion. CET 1/TLE=7.27%. To reach 10% ratio requires CET 1=$236.6219 billion. Required CET 1 increase=$64.5759 billion or 37.53% of reported $172.046 billion.
>
> Wells Fargo: CET 1=$148.845 billion. TLE=$2.213544 trillion. CET 1/TLE=6.72%. To reach 10% ratio requires CET 1=$221.3544 billion. Required CET 1 increase=$72.5094 billion or 48.71% of reported $148.845 billion.
>
> Current total CET 1 for the four BHCs=$672.422 billion. Current total TLE=$10,42529 trillion. Total required CET 1 to meet the 10% adjusted leverage ratio=$1.042529 trillion. Total required additional CET 1=$370.107 billion.

Reported TLE is computed using "transition requirements" and is expected to vary slightly under the final requirements.

with no trading assets or liabilities and limited interest rate and foreign exchange swaps could qualify by using the traditional balance sheet leverage ratio (i.e., CET 1/adjusted average total consolidated assets).[5]

On the other hand, the 10 percent CET 1 to total leverage exposure requirement seems to be less restrictive than the 23.5 percent CET 1 to risk-weighted assets and 15 percent CET 1 to balance sheet assets minimums recently proposed by the Federal Reserve Bank of Minneapolis for non-"systemically important" banking companies with assets more than $250 billion.[6]

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[5] The simple leverage ratio currently reported by U.S. banks is Tier 1 capital/adjusted average total consolidated assets. Reported average total consolidated assets are adjusted by deducting amounts deducted from Tier 1 capital. Tier 1 capital includes certain preferred stock and other "additional Tier 1 capital" items that are not included in CET 1. CET 1 is closer to what a "traditional bank" would consider to be its "common equity" for purposes of determining its "leverage."

[6] The Minneapolis Plan to End Too Big to Fail is *available at* https://www.mpls.frb.org/~/media/files/publications/studies/endingtbtf/the-minneapolis-plan/the-minneapolis-plan-to-end-too-big-to-fail-2016.pdf?la=en. The Minneapolis Plan would require any banking company with assets of more than $250 billion to maintain a minimum CET 1/risk weighted assets ratio of 23.5 percent. If the Treasury Secretary were to deem such a banking organization "systemically important" even at such leverage level, the CET 1/RWA ratio requirement could increase to 38 percent. Based on the average ratio of balance sheet assets being 60 percent greater than risk-weighted assets, the Plan imposes a "back-up" 15 percent CET 1/consolidated assets requirement for non-systemically important banking companies with consolidated assets of more than $250 billion. The Plan does not impose a leverage limit based on "total leverage exposure."

Using the same sources as in note 4, the reported CET 1/"risk-weighted assets" ("RWA") and CET 1/"adjusted average assets" ("AAA") ratios for the four largest U.S. bank holding companies were:

JP Morgan Chase: CET 1=$181.606 billion. RWA=$1.515177 trillion. AAA=$2.427423 trillion. CET 1/RWA=11.99%. If CET1=$314.0733 billion as required to meet 10% test in note 4, CET 1/RWA would=20.73% (less than 23.5% requirement of Minneapolis Plan). CET 1/AAA=7.48%. If CET 1=$314.0733 billion as required to meet 10% test in note 4, CET 1/AAA would=12.94 (less than 15% requirement of Minneapolis Plan).

Bank of America: CET 1=$169.925 billion. RWA=$1.547221 trillion. AAA=$2.111234 trillion. CET 1/RWA=10.98%. If CET 1=$270.4794 billion as required to meet 10% test in note 4, CET 1/RWA would=17.48% (less than 23.5% requirement of Minneapolis Plan). CET 1/AAA=8.05%. If CET 1=$270.4794 billion as required to meet 10% test in note 4, CET 1/AAA would=12.81% (less than 15% requirement of Minneapolis Plan).

Citigroup: CET 1=$172.046 billion. RWA=$1.204384377 trillion. AAA=$1.777662 trillion (from page 30 of Form 10-Q for period ending September 30, 2016). CET 1/RWA=14.285%. If CET 1=$236.6219 billion as required to meet 10% test in note 4, CET 1/RWA would=19.65% (less than 23.5% requirement of Minneapolis Plan). CET 1/AAA=9.68%. If CET 1=$236.6219 billion as required to meet 10% test in note 4, CET

The scope of the "off ramp" would also be controversial. It is clear the bill intends to exempt "qualifying banking organizations" ("QBOs") from Basel III standards, such as the liquidity coverage ratio ("LCR"), the net stable funding ratio ("NSFR"), and global systemically important banks ("G-SIB") requirements, as it expressly exempts QBOs from all the Dodd-Frank Section 165 "enhanced standards" other than subsection (c) public disclosure and subsection (k) inclusion of off-balance sheet exposures in capital computations. It would also clearly eliminate long standing risk-based capital requirements for QBOs as part of eliminating "any capital or liquidity" requirement other than the 10 percent leverage test.

Title I provides that any QBO would be considered well capitalized under "prompt corrective action" requirements. It would permit federal banking regulators to impose stress tests on QBOs (except the annual stress test required for companies with more than $10 billion but less than $50 billion in consolidated assets),[7] but would eliminate the regulators' ability to limit a QBOs "distributions," which has been the enforcement tool for requiring better stress test results.

Title I would also expressly exempt a QBO from all "systemic risk" determinations in receiving regulatory approvals for acquisitions or other activities and from both the Dodd-Frank Section 622 concentration limits on large financial firms[8] and the longstanding requirement that the deposit

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1/AAA would=13.31% (less than 15% requirement of Minneapolis Plan).

Wells Fargo: CET 1=$148.845 billion. RWA=$1.361405 trillion. Adjusted Average Assets=$1.883305 trillion (from page 158 of Form 10-Q for period ending September 30, 2016). CET 1/RWA=10.93%. If CET 1=$221.3544 billion as required to meet 10% test in note 4, CET 1/RWA would=16.26% (less than 23.5% requirement of Minneapolis Plan). CET 1/AAA=7.90%. If CET 1=$221.3544 billion as required to meet 10% test in note 4, CET 1/AAA would=11.75% (less than 15% requirement of Minneapolis Plan).

Neither Citigroup nor Wells Fargo report their simple leverage ratios in their Basel III Capital Disclosures, but do in their Form 10-Qs.

[7] Critics have argued the "off-ramp" is only useful to the largest banks, because they are the only banks that would benefit from the exemption from enhanced prudential and other standards. This exemption from annual stress tests could be a motivation for smaller bank holding companies to select the "off-ramp." They would also be freed from the obligation to compute risk-weighted assets under the risk based capital rules that apply to all banks. So long as such banks qualified as "traditional banks" they would only need to meet the standard balance sheet leverage test to qualify as a QBO.

[8] Section 622 of Dodd-Frank prohibits bank holding companies and insured depository institutions from making acquisitions if as a result the consolidated liabilities of the financial company would exceed 10 percent of the consolidated liabilities of all financial companies in the U.S.

holdings of a bank holding company or insured depository institution may not exceed 10 percent of total deposit holdings of insured depository institutions in the U.S. after an acquisition.

Some commentators have suggested that the federal banking regulators could still impose all capital, liquidity, and other requirements on QBOs through normal supervisory evaluations under the CAMELS rating system[9] or similar systems. The bill, however, seems to require a CAMELS or equivalent "satisfactory" (i.e., one or two) rating only for the most recent evaluation before a bank or bank holding company makes the QBO election. A QBO seems to lose that status only by failing the 10 percent test for four consecutive quarters or at any time the ratio reaches six percent.

Tile I requires that a bank holding company and all of its subsidiary banks jointly make a QBO election, so that no subsidiary bank or bank holding company could selectively gain such status.

Title II. Repeal of "Orderly Liquidation Authority" and Replacement with New Chapter 11 Bankruptcy Code Proceeding; Repeal of Federal Reserve Supervision of "Nonbank Financial Companies" and "Financial Utilities"; Elimination of Office of Financial Research and Revisions to Financial Stability Oversight Council; Repeal of "Government Guarantees"

Title II would repeal Dodd-Frank Title II's "orderly liquidation authority" ("OLA"), which adopted much of the Federal Deposit Insurance Act's provisions for bank receivership. It would replace those provisions with a new subchapter V to Chapter 11 of the Bankruptcy Code.

The proposed subchapter V is drawn from a House Judiciary Committee bill (HR 2947) passed by the House earlier this year that reflects a multi-year effort to develop Bankruptcy Code provisions that could accommodate a "two day single point of entry" resolution of a large financial holding company. Although subchapter V would provide for the Treasury Department and financial regulators to be involved in the proceeding, it would only permit the debtor to initiate the proceeding. The only eligible subchapter V debtors would be a bank holding company and any other financial holding company with consolidated assets of $50 billion or more.

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[9] The CAMELS rating system is a regulatory ratings system applied to U.S. banks. Ratings are assigned based on ratios derived from a bank's audited financial statements combined with on-site regulatory examinations. CAMELS is an acronym for the components of a bank's condition that are assessed, and stands for: (C) = capital adequacy; (A) = assets; (M) = management capacity; (E) = earnings; (L) = liquidity; and (S) = sensitivity (to market risk, especially interest rate risk). Bank holding companies are evaluated under a similar BOPEC system, *see* https://www.federalreserve.gov/boarddocs/srletters/2004/sr0418.htm.

Title II would also greatly reduce the role of FSOC by repealing its authority to (1) designate nonbank financial companies or "financial utilities" for Federal Reserve supervision, (2) recommend to the Federal Reserve "enhanced prudential standards," reporting, or disclosure requirements for companies supervised under Dodd-Frank Section 165, which would be limited to bank holding companies with $50 billion or more in consolidated assets, or to recommend heightened standards to any federal regulator based on financial stability concerns or (3) impose restrictions on, or require divestitures by, companies supervised under Dodd-Frank Section 165. As part of the reduction in the FSOC's role, Title II would eliminate the Office of Financial Research, which provides information and analysis for FSOC and its member agencies.

With all of its major powers repealed, the FSOC would apparently become a vehicle for reviewing financial stability and reporting to Congress its analysis. Title II revises FSOC's membership by providing that each of the represented Boards or Commissions (including the new ones created by Title VI) would determine its FSOC actions through a vote of all its members, rather than having the various Chairs make those decisions, as currently provided. The new Title V Office of Independent Insurance Advocate would replace the current "independent insurance expert" as a voting FSOC member.

Consistent with the repeal of all Federal Reserve supervision of nonbank financial companies, Title II would also repeal the Dodd-Frank Section 164 expansion of the prohibition on management interlocks to such companies as if they were bank holding companies and the Section 117 "Hotel California" provision preserving Federal Reserve Section 165 "enhanced" supervision of any bank holding company with $50 billion or more in consolidated assets on January 1, 2010, that received TARP funds, even after such company reorganized itself to no longer be a bank holding company.

Title II would also revise the Federal Reserve's ability to impose "enhanced prudential standards" and other restriction on companies it supervised under Dodd-Frank Section 165 (which the bill would limit to bank holding companies with $50 billion or more in consolidated assets). It would require the Federal Reserve to establish stress test conditions through normal notice and public comment procedures. This would force the Federal Reserve to describe the scenarios to be used and to receive comments before using such scenarios. Similarly, the Federal Reserve and Federal Deposit Insurance Corporation ("FDIC") would be prevented from requiring "living wills" more frequently than every two years and would be required to (1) provide public notice of and comments on their assessment procedures before finalizing such procedures, and (2) feedback within six months of receiving a company's living will.

The repeal of Dodd-Frank Section 166 would eliminate the Federal Reserve's

authority to require "early remediation" by companies supervised under Dodd-Frank Section 165 (which, as noted above, the bill would limit to bank holding companies with consolidated assets of $50 billion or more). The repeal of Dodd-Frank Section 115 would seem to eliminate the Federal Reserve's authority to increase the asset threshold for the application of certain "enhanced prudential standards" to bank holding companies.[10]

Finally, Title II would repeal the Dodd-Frank permission for the FDIC to establish a "widely available program to guarantee obligations during times of severe economic stress" and the longer standing "systemic risk" exception to the "least cost" resolution requirement for insolvent banks, thereby prohibiting the FDIC from providing "open assistance" to prevent or limit systemic risk. Title II would also prevent the "exchange stabilization fund" from being used to guarantee any nongovernmental entity.[11]

These provisions "ending government guarantees" along with the rest of Title II are intended to eliminate "market expectations" that certain financial companies would be "bailed out."

Title III. Conversion of CFPB into Five Member Consumer Financial Opportunity Commission with Dual Mandate to Protect Consumers and Encourage Competition in Providing Financial Services to Consumers; Elimination of Authority to Ban "Abusive" Practices, Limitation of Supervision to Companies with more than $50 Billion in Assets, Increasing Congressional Supervision, Including Annual Appropriations, and Subjecting Rules to Cost Benefit Analyses; Repeal of Durbin Amendment

Title III would achieve three longstanding Republican goals: First, it would convert the CFPB into a five member bipartisan commission like the Securities and Exchange Commission ("SEC") and Commodity Futures Trading Commission ("CFTC").

Second, it would "balance" the CFPB's mandate by (1) renaming it the Consumer Financial Opportunity Commission ("CFOC") with the "dual

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[10] Dodd-Frank Section 165(2)(B) permits the Federal Reserve to establish an asset threshold above $50 billion for applying certain Section 165 standards to bank holding companies "pursuant to a recommendation by the Council in accordance with Section 115." After Title II repealed Dodd-Frank Section 115, that could not happen. As a practical matter, the Federal Reserve has used other Section 165 authority to "tailor," not eliminate, enhanced prudential standards for smaller bank holding companies subject to Section 165.

[11] This fund controlled by the Treasury Department was established in the 1930s to protect the U.S. dollar when still tied to the gold standard. During the financial crisis it was used to guarantee money market funds.

mandate" to ensure (A) "fair and transparent" consumer finance markets and (B) that such markets have "strengthening participation" by providers "without "Government interference or subsidies, to increase competition and enhance consumer choice."

Third, it would subject the new CFOC to annual Congressional appropriations, subject its actions to cost-benefit review by a new Office of Economic Analysis, require periodic reviews of existing rules to review their costs and benefits, establish small business, credit union, and community bank advisory boards and a new Inspector General, repeal its authority to ban "abusive" practices and the judicial "deference" provided for its actions, restrict its ability to obtain nonpublic information, and permit parties to transfer CFOC proceedings to a federal court.

Title III would repeal the CFPB's authority to ban arbitration agreements and its 2013 indirect auto financing guidance. It would also limit CFPB (or CFOC) supervision to companies with more than $50 billion in consolidated assets, the same bank holding companies that the Federal Reserve currently supervises under "enhanced prudential standards" and any nonbanking firms of that size.

Finally, Title III would repeal the "Durbin Amendment" (Dodd Frank Section 1075) restricting interchange fees on debit transactions.

Title IV. Reorganization of SEC and CFTC, along with Subjecting Actions to Stricter Review; Repeal of (a) Risk Retention Rules for all but Residential Mortgage Securitizations, (b) Department of Labor Imposed Fiduciary Standards for Broker-dealers, (c) Executive Compensation Reporting Requirements, (d) Private Equity Fund Advisor Regulation, and (e) Franken Amendment; Changes to "Accredited Investor" Definition; Cross Border OTC Derivatives Rules; Harmonization of SEC and CFTC OTC Derivatives Rules

Subtitle A of Title IV would require the SEC to implement existing reorganization recommendations, subject all of its actions to the Administrative Procedures Act (i.e., notice, comment, and judicial review), and impose other "reform, restructuring, and accountability" requirements.

Subtitle B would make numerous reforms "eliminating excessive government intrusion in the capital markets," several of which have been included in other House bills not acted upon in the Senate.

Subtitle C would make CFTC reforms, including subjecting all its actions to the APA and permitting plaintiffs to challenge CFTC actions in their home Court of Appeals rather than only the DC Circuit, and requiring the CFTC to issue cross border OTC derivatives rules under Dodd-Frank Title VII.

Subtitle D would require the SEC and CFTC to eliminate inconsistencies between their OTC derivatives rules issued under Dodd-Frank Title VII.

Among the many reforms included in Subtitle B, some that relate to Dodd-Frank include:

- Section 441 would repeal the Department of Labor's recent ERISA ruling establishing fiduciary standards for retirement investment advisors and prohibit the Department from taking any further action on the issue until the SEC issues final rules on broker-dealer standard of conduct under Dodd-Frank Section 913(g).
- Section 442 would limit Dodd-Frank Section 941 (the "risk retention" requirements) to an "asset-backed security that is comprised wholly of residential mortgages."[12]
- Section 449 would repeal 40 sections of Dodd-Frank Title IX, including Section 939B (which eliminated the credit rating agency exemption from Regulation FD), Section 939F (the "Franken Amendment," providing for a commission to allocate ratings assignments), Section 939G (which repealed SEC Rule 436G permitting credit ratings to be included in a prospectus without rating agency consent), Section 953(b) (requiring disclosures of the ratio of chief executive officer compensation to the median compensation of employees at the relevant company), Section 955 (requiring public company reporting of restrictions on employee and director hedging of stock options), and Section 956 (requiring federal financial regulators to restrict incentive compensation programs).
- Section 450 would exempt private equity fund advisors from the registration and reporting requirements established by Dodd-Frank Section 403. Section 451 would eliminate "systemic risk" information reporting requirements. Section 452 would revise the definition of "accredited investor."[13] Section 455 would repeal all the "miscellaneous" provisions in Dodd Frank Title XV except Section 1501 (restrictions on use of U.S. funds for foreign governments), which

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[12] It is, of course, possible that residential mortgage securitizations with supporting assets tied to the mortgages would remain subject to risk retention requirements, but the bill seems to intend to exempt multi-asset securitizations that include residential mortgages.

[13] The amendment would qualify individuals with $200,000 ($300,000 for couples) in income, without inflation adjustment, $1,000,000 in assets outside personal residence, and any person the SEC determines has "demonstrable education or job experience to qualify such person as having professional knowledge of a subject related to a particular investment."

would repeal the "conflicts mineral" disclosure requirements that were an unexpected Dodd-Frank result.[14]

Title V. Repeal of Federal Insurance Office and Creation of Office of Independent Insurance Advocate

Dodd-Frank created a Federal Insurance Office within the Treasury Department, the Director of which became a "non voting" member of FSOC, and separately provided for an "independent" voting member of FSOC "with insurance expertise." Title V would repeal the FIO and the "insurance expertise" FSOC member and would replace both with the new Office of Independent Insurance Advocate.[15]

Title VI. Requiring Enhanced Cost Benefit Analysis for all Federal Financial Regulations, "Major Regulations" issued by Financial Regulators only Becoming Effective if approved by Congress, Elimination of Chevron Doctrine Deferring to Regulator Actions, Conversion of Regulators into Five Member Commissions, and Subjecting Regulators to Annual Appropriations

Title VI would dramatically reshape federal financial regulators and their authority. Subtitle A would impose new, more stringent requirements for conducting cost benefit analyses for all actions of such regulators (including the CFPB restructured as the CFOC), facilitate appeals from those findings, and establish a new Chief Economists Panel to review, and potentially overturn, such analyses.

Subtitle B would specify that a major rule (i.e., one estimated to cost $100 million or more) issued by any federal financial regulator would only become

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[14] Title XV was added to Dodd-Frank during a House/Senate conference. When nonfinancial companies learned of the extensive disclosure obligations created by Dodd-Frank Section 1502, it became a prime example of the unexpected effects "buried" in Dodd-Frank. Dodd Frank Sections 1503 and 1504 (which would also be repealed by Title IV of the bill) created reporting requirements for mine safety matters and disclosure requirements for "payments by resource extraction issuers."

[15] Although the bill would eliminate FSOC's authority to designate insurance companies (and all other nonbank financial companies) as "systemically important" companies subject to Federal Reserve supervision, the bill's proponents suggest the new OIIA would provide a more persuasive voice for insurance issues on FSOC and better coordinate with state insurance regulators "federal efforts on the prudential aspect of international insurance matters." The FSOC voting member with insurance expertise voted against designating Prudential and Met Life as "systemically important" companies subject to Federal Reserve supervision, but was only joined by one other member in the Prudential vote and none in the Met Life vote. The bill's proponents argue this demonstrated the "independent insurance expertise" member was not an effective member of FSOC.

effective if Congress specifically approved the rule.[16]

Subtitle C would overturn, for statutory interpretations by federal financial regulators, the 1984 *Chevron* decision requiring federal courts to uphold agency interpretations that are not "arbitrary or capricious."[17]

Subtitle D would reform the FDIC, Federal Housing Finance Agency ("FHFA"), National Credit Union Administration ("NCUA"), and OCC to have bipartisan five member boards similar to the SEC and CFTC.[18]

Subtitle E would subject to annual Congressional appropriations the budgets of the FDIC, FHFA, NCUA, OCC, and (for nonmonetary policy activities) the Federal Reserve. Each of these organizations currently has independent funding mechanisms, which would continue for the Federal Reserve's monetary policy through earnings from its open market operations.

Subtitle F would require the Federal Reserve, FDIC, and the Office of the Comptroller of the Currency ("OCC") to inform Congress and the public, and consult with appropriate Congressional Committees, before taking any action in international bodies, such as the Basel Committee.

Title VII. Reforms to FOMC and Requirements for Establishing and Auditing Monetary Policy; Limits on Federal Reserve Emergency Lending; Potential Revision of Federal Reserve Mandate

Although Title VI preserves the Federal Reserve's budgetary independence in conducting monetary policy, Title VII would mandate that the Federal Reserve's Federal Open Markets Committee establish and publicly announce a "directive policy rule" for establishing monetary policy. This rule would then be the basis for a "policy instrument target" for the interest rates on federal funds, nonborrowed reserves, and the discount rate.

These provisions are intended to force the FOMC to justify publicly the basis

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[16] The Congressional Review Act currently provides Congress with expedited procedures to disapprove a "major rule." Because the President can veto any such resolution, only one rule has been so rejected in the 20 years since the Act became law. Title VI would reverse the procedure for rules issued by any federal financial regulator. While this means no new major rule could become effective without Congressional approval, Section 632 also provides that the rule would be treated as rejected if Congress did not act within 70 legislative or session days.

[17] Title VI would provide for *de novo* review of all statutory interpretations by federal financial regulators, with the court determining the meaning of the statute.

[18] While the FDIC currently has a five member board, that includes two automatic members (the Comptroller and the CFPB Director), which Title VI would eliminate so that all the Boards would have only appointed members. In any case, both the Comptroller and the CFBP Director would also be eliminated by establishing five member boards for the OCC and the new CFOC.

for its monetary policy based on something similar to the "Taylor Rule"[19] and for the Government Accountability Office ("GAO") GAO to audit the Federal Reserve's compliance with such public explanation and its consistency in issuing new policy instrument targets. Congress would then review the Federal Reserve's actions.

Title VII would also expand the FOMC to include six representatives of District Federal Reserve Banks (along with the seven Governors of the Federal Reserve Board) and repeal the New York Federal Reserve Bank president's permanent membership.[20]

Title VII would require the FOMC to record its meetings and release unedited public transcripts and would establish a "black out" period near FOMC meetings. It would also subject the Board and its staff to the same ethics requirements as the SEC and its staff, and would require that Federal Reserve staff salaries above a certain level be reported through a public database.

Title VII would restrict the Federal Reserve's emergency lending powers under Section 13(3) of the Federal Reserve Act by requiring the affirmative vote of at least nine presidents of District Reserve Banks (along with the existing requirement for at least five Governors of the Board) that the "unusual and exigent" circumstances justifying such lending also "pose a threat to the financial stability of the United States," confirmation of the adequacy of collateral for such lending, and a penalty rate.

Finally, Section 709 would require an annual GAO audit of the Board and each of the 12 District Banks and remove existing restrictions on the audit covering monetary policy matters. Section 710 would establish a new "Centennial Monetary Commission" (modeled after the 1908 Monetary Commission that led to the Federal Reserve Act) to review the history of the Federal Reserve and its success in fulfilling its current dual mandate for controlling inflation and limiting unemployment.

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[19] The "Taylor Rule" is a mechanistic rule that stipulates how much a central bank should change nominal interest rates in response to economic conditions proposed by John B. Taylor, Professor of Economics at Stanford University and former Undersecretary of the Treasury and member of the Council of Economic Advisors under President George W. Bush. Specifically, the rule provides that for each one percent increase in inflation, the central bank should raise nominal interest rates by more than one percent.

[20] Six pairs of District Banks would rotate membership annually. New York would alternate with Boston. The New York Bank's permanent membership on the FOMC has always been justified by the fact that Federal Reserve open market operations are conducted by the New York Bank. The changes to the FOMC are obviously intended to increase the role of district banks and reduce the traditional role of the President of the New York Bank.

The report would also be required to recommend changes to the Federal Reserve System and to its Congressional mandate.

Title VIII. Increases to SEC and FIRREA Penalties

Among the increased penalties, the maximum "third tier" penalties would be increased through both a higher absolute dollar cap and a tripling of the defendant's "pecuniary gain." Currently, the latter maximum is the actual gain with no tripling.

Title IX. Repeal of Volcker Rule and of Moratorium on New FDIC Insurance for BHCA Nonbank Banks

Section 901 of the bill would repeal the the Dodd-Frank Section 619 "Volcker Rule" limitations on "banking entity" "proprietary trading" and "relationships with hedge funds and private equity funds."[21]

The rest of Title IX would repeal Dodd-Frank Sections 603, 618, 620, and 621. The repeal of Section 603 would end the moratorium on approving FDIC insurance for industrial loan companies, trust banks, and credit card banks that are not "banks" under the Bank Holding Company Act and that are not currently insured.

Title X. Simplification of SEC Requirements for Small Businesses, Safe Harbors, SEC Small Business Advocate, Expanded Capital Access for BDCs, Regulation D Reform, and Other Provisions for "Unleashing Small Business, Innovation, and Job Creators by Facilitating Capital Formation"

Many of Title X's provisions come from other House legislation that has not become law. Broadly, Title X expands upon the JOBS Act by creating additional exemptions for small offerings and by promoting liquidity for such securities through new exchanges.

This lengthy Title is divided into 19 separate subtitles that modify various existing statutes and create new provisions. This includes revisions to SEC Regulation D, increases in dollar limits for exemptions from disclosure requirements for stock issuances to employees, expanded Form S-3 eligibility, and expanded preemption of state Blue Sky laws.

Title XI. Regulatory Relief for Main Street and Community Banks

Title XI is also divided into 19 subtitles providing various forms of relief

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[21] The less well known part of the original "Volcker Rule," the Dodd-Frank Section 622 "concentration limits on large financial firms" would not be repealed, but would not apply to QBOs who "opt out" under Title I's adjusted leverage test, as described above.

from regulatory requirements for mortgages, community banks, credit unions, and other transactions or parties.

For mortgages, Title XI would increase the threshold for a "high-cost mortgage," create safe harbors from ability to pay and other requirements, and ease licensing and disclosure requirements for mortgage originators and lenders.

Section 1136 would revise FFIEC examination procedures by adjusting examination standards and establishing report issuance requirements, establish a new Office of Independent Examination Review to receive and investigate complaints from financial institutions, and provide financial institutions with both a right to an independent review of a material supervisory determination and a right to appeal the findings of such review to a Federal Court of Appeals.

Section 1146 would require federal financial regulators to take into consideration "the risk profile and business models" of regulated entities in taking any actions and to tailor their actions for each such class of regulated entities to limit "burdens as is appropriate for the risk profile and business model involved."

Section 1161 would repeal Dodd-Frank Section 1071's requirements to collect data on credit applications by women owned, minority-owned, and small businesses.[22]

SUMMARY

As noted above, the CHOICE Act would not repeal all of Dodd Frank, and it would make important changes that go much further than simply undoing Dodd-Frank. In 2015, the Senate Banking Committee approved a much less ambitious bill that also would have modified Dodd-Frank. News reports suggest that the President Trump's transition team is interested in supporting a bill similar to the CHOICE Act that "would do more." It is unclear whether that would mean a broader repeal of Dodd-Frank or more changes that go beyond Dodd-Frank repeal. As previously stated, the selection of Steven Mnuchin as Secretary of the Treasury has raised speculation that the Trump Administration may not support financial reform as wide ranging as the CHOICE Act.

Any bill containing provisions similar to those described above would be very controversial. Although Republicans will have control of both houses of Congress in 2017, their majorities, especially in the Senate, are much smaller than the 2009-10 Democratic majorities that permitted passage of Dodd-

[22] This would repeal Section 704B of the Equal Credit Opportunity Act, which was created by Dodd-Frank Section 1071.

Frank. While the 2017 House could likely pass a bill similar to the CHOICE Act, as with Dodd-Frank it is likely any such House based bill would be subject to important amendments if it were to pass the Senate.[23]

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[23] Many of Dodd-Frank's most publicized provisions (including the Volcker Rule and the Collins, Durbin, Franken, and Lincoln amendments) were not in the original Treasury Department proposed bill or the House passed bill. The 2016 Republican Platform contains the sentence: "We support reinstating the Glass-Steagall Act of 1933 which prohibits commercial banks from engaging in high-risk investment." The two "Glass-Steagall" provisions repealed by the 1999 Gramm-Leach-Bliley Act (Sections 20 and 32 of the Banking Act of 1933) did not regulate "high risk investment" but instead limited bank affiliation with companies underwriting or distributing securities (and common officers and directors for such companies and banks). Federal Reserve interpretations of Section 20 ultimately eliminated most of the practical significance of these restrictions, and the 1998 affiliation of Citibank with Salomon Smith Barney (then one of the largest broker dealers) demonstrated that even the largest broker-dealer could affiliate with a bank under Section 20. The GLBA was not needed to permit that affiliation. The GLBA, however, was needed to permit Citibank to continue to affiliate with certain Travelers insurance companies because of Bank Holding Company Act restrictions. In political and much academic discourse, however, "Glass-Steagall" has come to mean restrictions on "risky activities." Because "Glass-Steagall" has come to have a very popular "elastic" meaning, it is unclear what effects discussion of Glass-Steagall might have on any financial reform bill. Since the financial crisis, many bills have been introduced in Congress to "reinstate Glass-Steagall," very few of which have been limited to reenacting Sections 20 and 32. Ironically, the GLBA's only other change to "Glass-Steagall" was the addition of municipal revenue bonds to the list of "bank eligible" securities under "Glass Steagall" Section 16, a change that is not controversial.