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WHITE PAPER

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After the U.S. Presidential and Congressional Elections, What's Next for Financial Services Regulation?

Republican majorities in both chambers of Congress and changes in the leadership of executive departments and agencies provide President-elect Trump with a rare opportunity to make significant changes to the U.S. financial regulatory landscape. The new Administration's agenda, if implemented, may markedly affect the competitive environment for all types of financial services companies.

This *White Paper* reviews the financial services priorities of the new Trump Administration based upon positions articulated during the election campaign and in the early stages of the transition period.

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The presidential and congressional elections of 2016 have resulted in the election of Donald J. Trump as the 45th U.S. President and Republican majorities in both chambers of Congress. What do these elections mean for the future of financial services regulation?

As the new Trump Administration develops comprehensive policy positions and makes important personnel decisions, we offer early indications of the financial services regulatory agenda that is unfolding. At this time, prevailing themes and observations for the future of financial services regulation are:

- President-elect Trump is most likely to pursue policies of deregulation, focusing early attention on reforming one of President Obama's signature domestic accomplishments, the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), signed into law in July 2010.[1]

- President-elect Trump has called for a temporary moratorium on new executive agency rules "that are not compelled by Congress or public safety,"[2] although the scope of the specific agency proposals that would be covered is not yet clear.

- The likely starting points for amendments to the Dodd-Frank Act are two similar bills drafted and sponsored by the Republican Chairmen of the relevant banking committees in the Senate and House of Representatives.[3]

- Republican efforts to make substantial changes to the Dodd-Frank Act will likely be met with some opposition in the Senate, where Republicans hold a narrow majority, and this would likely necessitate compromise discussions.[4]

- Several changes to the Dodd-Frank Act could be embraced on a bipartisan basis, aiding enactment into law relatively quickly if these changes do not become ensnared in compromise negotiations. Examples include raising the $50 billion asset threshold for application of enhanced prudential regulation to bank holding companies, weakening the authority of the Financial Stability Oversight Council ("FSOC") within the Department of the Treasury, and replacing the single Director structure of the Consumer Financial Protection Bureau ("CFPB"), and possibly that of other federal agencies, with a bipartisan multimember commission.

- The heads and many subordinate officials of each cabinet department and agency will be nominated by President Trump following his inauguration. Leadership positions of many of the federal financial institutions regulatory agencies[5] are likely to turn over as well. Vacant positions may be filled quickly. Senate confirmation of these political appointees should proceed apace as current Senate rules permit a simple majority vote on executive branch nominations, disallowing filibusters and facilitating confirmation.

- As the federal financial services landscape develops, state financial services regulators and state attorneys general ("AGs") could choose to continue to apply state laws and rules that are aligned with parts of the Dodd-Frank Act or to pursue novel theories concerning consumer protection and corporate conduct.

Our *White Paper* discusses the financial services priorities of the new Trump Administration based upon positions that have been disclosed thus far. We discuss possible changes in the leadership of the federal financial institutions regulatory agencies and identify some of the congressional leaders who will have significant influence over financial services reform going forward. We conclude with an overview of the CHOICE Act, which is most likely to kick off the legislative process for financial regulatory reform. We will publish additional *White Papers* as the framework for financial services regulation continues to take shape.

The new regulatory environment is likely to significantly affect the competitive environment for financial services companies of all types and sizes, including foreign banks doing business in the United States. Financial services companies should stay abreast of regulatory and legislative developments to take full advantage of opportunities and make appropriate adjustments to their business plans and operations.

PRIORITIES OF THE NEW TRUMP ADMINISTRATION

Although the agenda for regulation of the financial services industry will continue to evolve for some time, the Trump transition team has indicated that deregulation will be the hallmark of the new Administration's financial institutions regulatory policy: "The Financial Services Policy Implementation team will be working to *dismantle the Dodd-Frank Act* and replace it with new policies to encourage economic growth and job creation."[6]

President-elect Trump has consistently advocated for repeal of all or part of the Dodd-Frank Act, and several influential Republican members of Congress support taking up reforms on grounds that the Act is stifling economic growth and limiting consumer choice. In the words of the Trump transition team, "Federal policy should focus on free enterprise, while protecting consumers by policing markets for force and fraud. Both Wall Street and Washington [D.C.] should be held accountable."[7]

These views were manifest in the 2016 Republican Platform, which criticized the Dodd-Frank Act for having established "unprecedented government control over the nation's financial markets" and created "new unaccountable bureaucracies."[8] The Republican Platform cited the "excessive regulation and burdensome requirements" of the Dodd-Frank Act as having "helped contribute to the slow economy we all endure today."[9]

President-elect Trump has placed regulatory reform within his three main policy objectives. During the presidential campaign, President-elect Trump called for scaling back existing federal rules and ceasing issuance of new rules. For example, in a speech before the Detroit Economic Club, Mr. Trump stated that, if elected, he would "cut regulations massively," beginning by having all federal regulatory agencies review their rules for streamlining and rescission and by issuing an executive order placing a moratorium on new agency regulations.[10]

House Majority Leader Kevin McCarthy (R-CA) and 20 Republican committee heads reportedly recently sent a letter to executive government agencies cautioning against finalizing pending rules until after the presidential inauguration to give the new Administration and Congress time to review and impart direction regarding pending rulemakings.[11] The letter advised that any final rules would be subject to review and potential reversal under the Congressional Review Act,[12] which allows Congress 60 legislative days to overturn executive agency rules.

On November 17, 2016, the House of Representatives, which is currently majority-Republican, passed legislation, the "Midnight Rules Relief Act," that would amend the Congressional Review Act to allow Congress to overturn federal regulations that have been issued during the final year of the Obama Administration by a single *en bloc* vote instead of through the current procedure of considering one regulation at a time.[13] President Obama has reportedly threatened to veto the legislation if it passes the Congress.

The House of Representatives' passage of the "Midnight Rules Relief Act" is significant as an indicator of the seriousness of purpose with which Congress is likely to consider regulatory reform when the 115th session begins in January 2017. Regulatory and legislative efforts to roll back regulations of a prior Administration are not uncommon.

An important component of the evolution of the financial services landscape resides with state regulators and state AGs. As the federal deregulatory framework advances, state financial services regulators and state AGs may continue to apply state laws and rules that are aligned with parts of the Dodd-Frank Act as they exist today. In a recent statement, for example, Maria Vullo, Superintendent of the New York Department of Financial Services ("DFS"), said: "DFS works every day to anticipate and stay ahead of events affecting the financial services industry, will continue to protect consumers and our financial markets, and will seek opportunities to further the department's mission."

Additionally, Doug Cohen, a spokesman for the New York AG, reportedly indicated that the AG "will remain focused on rooting out fraud in financial markets, protecting consumers, and ensuring equal protection under the law for all New Yorkers."[14] A number of state AGs have already utilized their powers to investigate and prosecute nonconsumer-facing conduct and stand ready to expand their efforts to a broader scope of the financial industry.

AGENCY LEADERSHIP

The leadership of executive departments and agencies is responsible for carrying out the President's agenda. One of the first steps President-elect Trump must take is nominating the heads of the executive departments and agencies that will form his cabinet. President-elect Trump has announced his intention to nominate Steven Mnuchin as the Secretary of the Treasury and Dr. Ben Carson as the Secretary of Housing and Urban Development.

Over time, President-elect Trump will have the opportunity to appoint new heads of the executive agencies that are members of the FSOC.[15] Of greatest significance, however, is the immediate opportunity to nominate a new Secretary of the Treasury, who serves as Chairman of the FSOC, and thereby influences the FSOC's agenda. This appointment may have a significant impact on the operations of the FSOC even in the absence of any congressional consideration of legislation to amend the operations of the FSOC.

In addition to filling cabinet positions, President-elect Trump will have the ability to fill important leadership positions within the federal financial institutions regulatory agencies. With Republican leadership in place, the regulatory programs of each of these agencies is likely to undergo substantive changes since the direction of the agencies will be aligned with the policy objectives of the new President.

Our survey of the terms of office of the leaders of the federal financial institutions regulatory agencies reveals numerous critical appointment possibilities that will significantly alter the course of financial services regulation. Several of these agencies currently have vacancies, and the number of vacant positions may increase as more incumbents announce their intention to resign at the conclusion of the Obama Administration.

- **Board of Governors of the Federal Reserve System**—The Board of Governors of the Federal Reserve is a seven-member board that currently has five members and two vacancies.[16] President-elect Trump can fill the two vacancies very quickly. One of the two current vacancies is the position of Vice Chairman for Supervision, a position created by the Dodd-Frank Act.

  Chairwoman Janet Yellen's term as Chair ends in February 2018; her term as a member of the Board of Governors ends in January 2024. Shortly after the 2016 elections, an economic adviser to President-elect Trump was reported to have said the President-elect is not seeking Chairwoman Yellen's resignation, although he would not nominate her for another term as Chair.[17] Chairwoman Yellen recently stated that she intends to complete her term as Chair.[18] Past Chairs of the Federal Reserve Board have traditionally resigned when their term as Chair ended.

- **Commodity Futures Trading Commission**—The CFTC is governed by a five-member commission that currently has three commissioners:

  - Chairman Timothy Massad, a Democrat, whose term ends in April 2017;
  - Commissioner Sharon Bowen, a Democrat, whose term ends in April 2018; and
  - Commissioner J. Christopher Giancarlo, a Republican, whose term ends in April 2019.

  No more than three CFTC commissioners may belong to the same political party.

  As the only current Republican Commissioner, Commissioner Giancarlo is widely considered to be a top contender for the Chairman position. He could become the Acting Chairman on a temporary basis until a permanent Chairman is nominated by the President and confirmed by the Senate, and he, or someone else, could ultimately become the permanent Chairman.

  In September 2016, President Obama's Republican nominee, Brian Quintenz, and his Democratic nominee, Christopher Brummer, were reported favorably out of the Senate Agriculture Committee, but the full Senate had not confirmed either nominee by the time of the elections. President-elect Trump could support these nominations, allowing the Senate to confirm these individuals, or could make entirely new nominations.

- **Comptroller of the Currency**—Comptroller Thomas Curry's term of office ends in March 2017. The Comptroller performs his duties under the general direction of the Secretary of the Treasury, who will be one of the first appointments made.[19] Accordingly, it is possible that the Comptroller will choose to step down at the end of the Obama Administration. In that event, the First Deputy Comptroller may act in his stead until a permanent

Comptroller is nominated by the President and confirmed by the Senate.

- **Director of the Consumer Financial Protection Bureau**—CFPB Director Richard Cordray's term of office ends in July 2018. The CFPB Director could choose to resign effective at the end of the Obama Administration. In that event, the Deputy Director of the CFPB could become the acting Director.

  The President may remove the CFPB Director only for cause. The constitutionality of the CFPB's structure was recently decided by the U.S. Court of Appeals for the D.C. Circuit in *PHH v. CFPB*.[20] The panel ruled that the CFPB is unconstitutionally structured and severed the for-cause removal provision from the rest of the statute, making the CFPB Director subject to the supervision, direction, and removal power of the President. The CFPB has sought rehearing by the full D.C. Circuit Court, which has sought the views of the U.S. Solicitor General.

  Prior to the 2016 elections, the Republican Chairman of the House Financial Services Committee, Jeb Hensarling, asked the CFPB Director to consider carefully any appeal of *PHH v. CFPB* and to provide written assurance that the CFPB would comply in full with prevailing Executive Orders during rulemaking proceedings and before issuing any future final rules.[21] The views expressed by Chairman Hensarling are consistent with the provisions of the CHOICE Act that passed the Committee in June 2016 and may foreshadow the direction Congress may take in legislation to change the processes that apply to CFPB rulemakings.

- **Director of the Federal Housing Finance Agency**—FHFA Director Melvin Watt's term of office ends in January 2019. The President may remove the FHFA Director only for cause. In *PHH v. CFPB*, the U.S. Court of Appeals for the D.C. Circuit commented that the structure of the FHFA presents the same question of constitutionality as the structure of the CFPB.[22]

- **Federal Deposit Insurance Corporation**—The FDIC is governed by a five-member bipartisan board of directors. Chairman Martin Gruenberg's term ends in November 2017. The board of directors has one existing vacancy. The board has two *ex officio* members, the Comptroller of the Currency and the Director of the CFPB. No more than three board members may belong to the same political party. Changes in these *ex officio* members could have important impacts on the FDIC's operations.

- **Securities and Exchange Commission**—The SEC is governed by a five-member commission that currently has three commissioners:

  - Chairwoman Mary Jo White, a Democrat, who recently announced that she will resign at the conclusion of the Obama Administration;
  - Kara Stein, a Democrat, whose term ends in June 2017; and
  - Michael Piwowar, a Republican, whose term ends in June 2018.

  Commissioners may continue to serve up to 18 months after the end of their term unless the President nominates, and the Senate confirms, a replacement Commissioner. No more than three SEC commissioners may belong to the same political party.

  With Chairwoman White stepping down, President-elect Trump will have the opportunity to fill three vacancies. Following the departure of the Chairwoman, Commissioner Piwowar would become acting Chairman on a temporary basis until a permanent Chairman is nominated by the President and confirmed by the Senate, and he, or someone else, could ultimately become the permanent Chairman. During the time an acting Commissioner is in place, two Commissioners, rather than the customary three, would constitute a quorum for purposes of conducting the SEC's business. The incoming Chair of the SEC also has responsibility for appointing the Chair of the Public Company Accounting Oversight Board.

CONGRESSIONAL LEADERSHIP

Senate Republicans recently reelected Mitch McConnell (R-KY) as Majority Leader; Senate Democrats recently elected Charles Schumer (D-NY) to be Senate Minority Leader.

Senator Michael Crapo (R-ID) will likely become Chairman of the Senate Committee on Banking, Housing and Urban Affairs because Senator Richard Shelby (R-AL) is term-limited and unable to remain as Committee Chairman.[23] Senator Crapo was previously Ranking Member of the Committee during 2013 and 2014. Senator Sherrod Brown (D-OH) is expected to remain as Ranking Member of the Committee.

House of Representatives Speaker Paul Ryan (R-WI) has been renominated by unanimous vote and is expected to be reelected to that position. Jeb Hensarling (R-TX) is likely to remain as Chairman of the House Financial Services Committee. This would be Chairman Hensarling's final term as Committee Chairman due to caucus term limits. Maxine Waters (D-CA) is expected to remain as Ranking Member of the House Financial Services Committee.

LEGISLATIVE AGENDA

The election of a Republican President, together with Republican control of the House of Representatives and the Senate, portends potentially significant changes to the financial services landscape.

Consistent with the positions expressed during the presidential campaign and in the 2016 Republican Platform, the Trump Administration may support a variety of broad legislative initiatives, including those for:

- Rolling back major provisions of the Dodd-Frank Act that cover the CFPB, the FSOC, too-big-to-fail and bailout funding, the Volcker Rule, and more;
- Requiring the Government Accountability Office ("GAO") to audit the Federal Reserve and report its findings to Congress;
- Providing regulatory relief for smaller institutions with regulations focused more on risk and complexity rather than multiple subjective thresholds of what constitutes a "large" institution;
- Raising the current threshold of $50 billion in assets for bank holding companies to become subject to enhanced prudential supervision and regulation by the Federal Reserve;
- Increasing and simplifying bank capital requirements with a greater focus on leverage capital ratios, as opposed to risk-based capital ratios;
- Increasing and expanding SEC-imposed penalties for financial fraud, self-dealing, and insider trading;
- Repealing the Dodd-Frank Act rulemaking on incentive-based compensation and pay ratio reporting requirements;
- Requiring the SEC to carry out a fiduciary rulemaking on standards of conduct for brokers and dealers, which would effectively block the Department of Labor's ("DOL") final fiduciary rules from becoming effective in April 2017, even absent adverse judicial decisions on the DOL fiduciary rules;
- Reforming Fannie Mae and Freddie Mac, which have been operating under FHFA conservatorship since 2008; and
- Strengthening the national flood insurance program administered by the Federal Emergency Management Agency.

The Trump Administration and the Republican-controlled Congress will likely target the FSOC and the CFPB for substantial reforms. The 2016 Republican Platform stated that "no financial institution is too big to fail" and that "any financial institution can be resolved through the Bankruptcy Code,"[24] instead of through the orderly liquidation authority in Title II of the Dodd-Frank Act. In keeping with the party Platform, President-elect Trump and Republican leaders in Congress have supported removing the FSOC's authority to designate systemically important financial institutions ("SIFI") as such. The Trump Administration could decide not to continue to pursue an appeal of a recent ruling by the U.S. District Court for the District of Columbia repealing the FSOC's designation of MetLife as a SIFI.[25] The FSOC has also designated AIG and Prudential as SIFIs, and new leadership may remove those designations.

The structure, mission, budget, and regulatory requirements of the CFPB will very likely be subject to scrutiny during the upcoming session of Congress. The 2016 Republican Platform described the CFPB as a "rogue agency" that was the worst element in the Dodd-Frank Act because "[i]t answers to neither Congress nor the executive, has its own guaranteed funding outside the appropriations process, and uses its slush fund to steer settlements to politically favored groups."[26] Depending upon the timing of departure of the current CFPB Director and the outcome of *PHH v. CFPB*, among other factors, the Trump Administration could take steps to stop CFPB rulemakings on short-term installment loans and mandatory arbitration clauses, which are not expected to be finalized until well after the new Administration is in place.[27]

As mentioned during the presidential campaign and in the 2016 Republican Platform, the new Trump Administration may support reinstatement of the division between commercial and investment banking previously embodied in the Glass-Steagall Act. During the presidential campaign, the 2016 Democratic Platform supported updating and modernizing the Glass-Steagall Act as well. While both parties seemingly support legislation to bring back the Glass-Steagall Act, the path to that end may involve substantial disruptions to the capital markets, where all the major players have been regulated as bank holding companies since fall 2008.

Prior Republican-sponsored legislation that would dismantle major parts of the Dodd-Frank Act is likely to be reintroduced and considered in the upcoming 115th session of Congress. Both the House Financial Services Committee and the Senate Committee on Banking, Housing, and Urban Affairs have previously passed partisan blueprints for dismantling the Dodd-Frank Act.

The Financial Regulatory Improvement Act of 2015, approved by the Senate Committee on Banking, Housing, and Urban Affairs on a party-line vote, contains a subset of the provisions of the CHOICE Act that passed the House Financial Services Committee in June 2016 on a partisan vote of that Committee. Additionally, the CHOICE Act is aligned with House Speaker Ryan's "A Better Way" policy agenda, which was rolled out at about the same time.[28] For these reasons, the Trump Administration may choose to embrace key elements of the CHOICE Act as the initial legislative vehicle for revising the Dodd-Frank Act.

OVERVIEW OF THE CHOICE ACT

We provide an overview of the principal provisions of the CHOICE Act in light of the high probability that the substance of this legislation will be the starting point for revising the Dodd-Frank Act in the next session of Congress.[29] Enactment of all or a part of the CHOICE Act is not a certainty since much of the legislation will likely face some opposition during consideration by the Senate, where Republicans have a slim majority.

The process for promulgating new regulations would increase in complexity under the CHOICE Act, with more steps, more oversight, and more opportunities for participation. We plan to publish an additional *White Paper* following the introduction of financial services reform legislation in the 115th session of Congress.

Convert Each Financial Regulatory Agency Currently Headed by a Single Director into a Commission

The CHOICE Act would change the current single-head structure of the CFPB, the OCC, and the FHFA with a bipartisan, multimember commission in each case.

Statutorily Repeal the *Chevron Doctrine* and End the Practice of Judicial Deference to Agency Interpretations

The CHOICE Act would seek to eliminate the *Chevron* doctrine for the federal financial institutions regulatory agencies.[30] As an example of the need for repeal of the *Chevron* doctrine, the comprehensive summary of the legislation highlighted *PHH v. CFPB*, in which PHH challenged a CFPB order that "departed from legal interpretations of a law that other regulators had adhered to for decades and applied [the] newly-decreed standard retroactively to justify levying an unprecedented penalty 18 times larger than what a CFPB Administrative Law Judge had previously assessed under the settled legal interpretation."[31] Elimination of the *Chevron* doctrine would likely multiply and intensify administrative law challenges to rules and other actions of these agencies.

Regulatory Relief for Well-Capitalized, Well-Managed Banking Organizations

Under the CHOICE Act, a banking organization that maintains a leverage ratio of at least 10 percent and has a composite rating of 1 or 2[32] may elect to obtain relief from Basel III capital and liquidity standards and the Federal Reserve's enhanced prudential standards, among other rules and requirements. The CHOICE Act is intended to allow banks to opt in to a regime that replaces excessive regulatory complexity with market discipline and that ensures the equity investors of SIFIs stand in for taxpayers if the institution fails.

Repeal of the Volcker Rule

The CHOICE Act would completely repeal the so-called Volcker Rule. The Volcker Rule is a part of the Dodd-Frank Act that prohibits banks from conducting proprietary trading, and limits their sponsorship and holding of ownership interests in hedge funds and private equity funds and other vehicles such as collateralized loan obligations that would be "investment companies" subject to the Investment Company Act of 1940 registration but for the Section 3(c)(1) or 3(c)(7) exemptions of that Act.

Repeal of the Durbin Amendment

The CHOICE Act would repeal the Durbin amendment, a part of the Dodd-Frank Act that requires the Federal Reserve to set limits on interchange fees charged to retailers by banks with more than $10 billion in assets for debit card processing.

Elimination of the Office of Financial Research

The CHOICE Act would eliminate the Office of Financial Research within the Department of the Treasury. The Dodd-Frank Act created this Office to promote financial stability by delivering financial data, standards, and analysis to the FSOC, the FSOC's members, and the public.

Repeal of "Too Big to Fail"

In an effort to end "too big to fail" and prevent future taxpayer bailouts, the CHOICE Act would make the following six changes:

- Repeal of the "Orderly Liquidation Authority" ("OLA") in Title II of the Dodd-Frank Act;
- Replacement of the OLA with a new chapter of the Bankruptcy Code designed to accommodate the failure of a large, complex financial institution;
- Addition of new limitations on the Federal Reserve's emergency lending authority under Section 13(3) of the Federal Reserve Act;
- Prohibition on the future use of the Exchange Stabilization Fund to bail out a financial firm or its creditors;
- Repeal of the FDIC's authority to establish a widely available program to guarantee obligations of banks during times of severe economic stress; and
- Repeal of the authority vested in the FSOC by Titles I and VIII of the Dodd-Frank Act to designate certain financial companies as "too big to fail."

Repeal of SIFI Designations for Non-Banks

The CHOICE Act would: repeal the FSOC's authority to designate non-bank financial companies as SIFIs; retroactively repeal the FSOC's previous designations of non-bank financial companies as SIFIs; repeal the FSOC's related authority to designate particular financial activities for heightened prudential standards; and repeal the FSOC's authority to break up a large financial institution if the Federal Reserve finds that the firm "poses a grave threat to the financial stability of the United States." The legislation would also repeal Title VIII of the Dodd-Frank Act, which empowers the FSOC to designate so-called "financial market utilities" as "systemically important," and gives those organizations access to the Federal Reserve's discount window.

The FSOC would continue to: (i) monitor market developments; (ii) facilitate information-sharing and regulatory coordination; (iii) bring the primary federal regulators together with the goal of identifying and mitigating risks to financial stability; and (iv) report to Congress, but it would be required to operate with a higher degree of transparency, through the following reforms:

- The FSOC would be subject to both the Government in the Sunshine Act and the Federal Advisory Committee Act;
- All of the members of the commissions and boards represented on the FSOC would be permitted to attend and participate in the FSOC's meetings;
- Before the principal of a Commission or Board represented on the FSOC votes as an FSOC member on an issue before the FSOC, his or her Commission or Board must vote on the issue, and the principal would have to abide by the results of that vote at the FSOC meeting; and
- Members of the House Financial Services Committee and Senate Committee on Banking, Housing, and Urban Affairs would be permitted to attend all FSOC meetings, whether or not the meeting is open to the public.

Reform of the CFPB

The CHOICE Act would establish the CFPB as an independent agency outside the Federal Reserve with a dual mission of protecting consumers and creating competitive markets. The legislation would replace the CFPB's single Director with a multimember, bipartisan commission. The legislation would also create an independent Inspector General of the CFPB, who must be nominated by the President and confirmed by the Senate. The legislation would subject the CFPB to the congressional appropriations process instead of permitting the CFPB to rely on a percentage of Federal Reserve revenues.

The legislation would provide courts with enhanced authority to change interpretations made by the CFPB of its own legal authority. The bill would require that the CFPB complete a comprehensive cost-benefit analysis before adopting any regulations, and would afford Congress the opportunity to approve significant CFPB regulations before they take effect.

Further, the CHOICE Act would repeal the CFPB's authority to decide that any consumer financial product or service is "abusive," repeal the CFPB's indirect auto lending guidance, and require the CFPB to obtain consumer permission before collecting personally identifiable financial information about them.

Alignment and Tailoring of Rules for Smaller Community Institutions

The CHOICE Act would require the federal financial institution regulatory agencies to appropriately tailor regulations to fit an institution's business model and risk profile. This provision is intended to reduce fixed compliance costs and allow banks to devote more of their operating budgets to meeting customer needs. Similarly, the legislation aims to reduce reporting burdens for highly rated and well-managed institutions, such as by minimizing the granularity of consolidated reports of condition and income and by eliminating redundancies in the data collection demands made by different regulators on the same institution, in order to free up resources for lending.

The legislation is intended to grant regulatory relief to community banks by providing greater due process protections for both banks and their officers, which would enhance their ability to challenge supervisory and enforcement actions. The legislation would require regulators to increase transparency, make final examination reports available for an institution's review at an earlier time, and afford the institution a right to appeal material supervisory determinations to an independent arbiter. The CHOICE Act would prohibit regulators from requiring banks to terminate relationships with legitimate businesses in the absence of material risk beyond "reputational risk," and would therefore prohibit regulatory actions such as Operation Choke Point.[33]

Credit unions would also obtain significant regulatory relief under the CHOICE Act. In addition to benefiting from many of the same reforms applicable to community banks, the CHOICE Act is intended to afford credit unions regulatory relief unique to their charter, including but not limited to the following:

- Requiring the National Credit Union Administration ("NCUA") to hold annual budget hearings that are open to the public, and to include in each annual budget a report detailing the NCUA's "overhead transfer rate";
- A less frequent examination cycle for well-managed, well-capitalized credit unions; and
- A new Credit Union Advisory Council to advise the NCUA Board on the full scope of regulatory impacts across federal laws and regulations.

The CHOICE Act would promote portfolio lending. The bill incorporates legislation authored by Representative Andy Barr (H.R. 1210) that would create a legal safe harbor for mortgage loans that are originated by a company and then held in portfolio on the company's balance sheet. The bill is intended to incent lenders to conduct sound underwriting to determine whether the borrower has the ability to repay the loan.

Reform of the Federal Reserve

The CHOICE Act would direct the GAO to conduct an audit of the Federal Reserve within 12 months of the date of enactment, with a report to be delivered to Congress within 90 days of completion of the audit.

Subjecting the Federal Financial Institutions Regulators to Congressional Appropriations

The CHOICE Act calls for bringing the CFPB, FDIC, OCC, FHFA, NCUA, FSOC, and the non-monetary functions of the Federal Reserve into the regular congressional appropriations process. While the legislation would apply to the Federal Reserve's prudential regulatory activities, it would not apply to its conduct of monetary policy, which would continue to be funded through open market operations and other sources of income, outside of the congressional appropriations process. Bringing these agencies' budgets into the congressional appropriations process could substantially alter their operations by making them more responsive to Congress in order to receive funding to fulfill their responsibilities.

Rule-Based Monetary Policy. The CHOICE Act is intended to improve how the Federal Reserve communicates monetary policy, by requiring it to generate a monetary policy rule and explain to the public how its chosen course compares to a standard reference rule specified in the legislation. The

Federal Reserve would select the policy inputs that go into the formulation of its rule and would retain the power to change or depart from its chosen strategy whenever it determines that economic circumstances warrant.

Reforms to Resolution Planning and Stress Testing Processes

The CHOICE Act would: (i) require banking organizations that currently submit resolution plans or "living wills" to continue to submit living wills until they make an effective capital election to rely on a specific minimum leverage ratio; and (ii) permit the banking agencies to conduct stress tests (but not limit capital distributions) of a banking organization that has made a qualifying capital election. For banking organizations that do not make a qualifying capital election and continue to submit living wills, the CHOICE Act would specify that banking agencies: (i) could request living wills only once every two years; (ii) must provide feedback on living wills to banking organizations within six months of their submission; and (iii) must publicly disclose their living will assessment frameworks.

In addition, the CHOICE Act would overhaul the current regime for stress testing banks by requiring the federal banking agencies to issue regulations that provide for at least three different sets of conditions under which the evaluation required by Section 165 of the Dodd-Frank Act, or under the banking agencies' rules implementing stress testing requirements, will be conducted, including baseline, adverse, and severely adverse conditions, and methodologies, including models to estimate losses on certain assets. The legislation would also require the banking agencies to provide copies of such regulations to the GAO and the Congressional Budget Office's Panel of Economic Advisors before publishing such regulations, and it would require the banking agencies to publish a summary of all stress test results.

Imposing Checks and Balances on Administrative Agencies and Regulation

Application of the "Regulations from the Executive in Need of Scrutiny Act" ("REINS Act"). The REINS Act, H.R. 427, is incorporated into the CHOICE Act. The REINS Act would require Congress to pass, and the President to sign, a joint resolution of approval for all "major regulations" before they become effective. "Major regulations" would be those that produce $100 million or more in impacts on the U.S. economy, spur substantial increases in costs or prices for consumers, or have certain other significant adverse effects on the economy.

Require All Financial Regulators to Conduct Meaningful Cost-Benefit Analysis Before Issuing Rules. In an effort to enhance regulatory transparency and accountability in rulemaking processes, the CHOICE Act would require extensive cost-benefit analyses. When proposing a rule, regulators would be required to include an assessment of the need for the rule and conduct a rigorous cost-benefit analysis of quantitative and qualitative impacts. Regulators would be required to allow at least 90 days for notice and comment on a proposed rule and publicly release the data underlying their analyses. If the costs of the rule outweigh its benefits, the regulators would be prohibited from finalizing the rule without express authorization from Congress.

The CHOICE Act would strengthen retrospective rule review requirements. Within five years of a new rule's implementation, the regulator would be required to complete an analysis that examines the economic impact of the rule, including its direct and indirect costs. The CHOICE Act would also direct regulators to conduct retrospective reviews of previously issued rules every five years to modify, streamline, expand, or repeal existing regulations.

Finally, the legislation would create a Chief Economist Council composed of the chief economists from each of the federal financial institution regulatory agencies, which would meet on a quarterly basis. The Chief Economist Council would be required to conduct a review and report on the costs and benefits of all financial regulations released in the previous year and the cumulative effects of regulations finalized within the same timeframe.

SEC Enforcement and Reforms

Expanded Penalties. The CHOICE Act would significantly increase the SEC's civil penalty authority, as well as criminal sanctions under the federal securities laws, for the most serious offenses. The legislation would increase amounts of first- and second-tier penalties and would nearly double the penalty amounts for third-tier offenses involving substantial losses for the victim, or substantial pecuniary gain for the offender, for both individuals and corporations. Additionally, the CHOICE Act would establish a new fourth-tier penalty for recidivist offenders that would allow amounts that are triple the otherwise maximum monetary penalties. The bill would also significantly increase criminal penalties for individuals who engage in insider trading and other corrupt practices.

Enforcement. The CHOICE Act would require the SEC to implement policies consistent with the principles of predictability, fairness, and transparency. For example, the legislation would require the SEC, when issuing a civil penalty against an issuer, to include findings, supported by the SEC Chief Economist, that the alleged violations resulted in direct economic benefit to the issuer and that the penalties do not harm the issuer's shareholders.

The CHOICE Act would give defendants in SEC administrative proceedings the right to remove the enforcement action to federal court. The legislation would require the SEC to allow defendants to appear before the Commission prior to the initiation of a formal enforcement action and would establish an Enforcement Ombudsman to review complaints about the enforcement program.

Further, the SEC would be required to approve and publish an enforcement manual to ensure transparency and uniform application of its procedures. In an effort to help ensure that the worst offenders can be barred from certain business activities, the CHOICE Act would eliminate the system of automatic disqualifications and instead allow the SEC to disqualify offenders in its discretion.

Public Company Accounting Oversight Board. The CHOICE Act would require the Public Company Accounting Oversight Board, which is subject to the oversight of the SEC, to conform its disciplinary proceedings to the SEC's rules and make such proceedings public, generally.

SEC Structure and Organization. Section 967 of the Dodd-Frank Act requires the SEC to hire a consultant to examine the operations, structure, funding, and need for reform of the SEC. To comply with this mandate, the SEC retained the Boston Consulting Group, which issued a report ("BCG Report") on its findings in March 2011.[34] The BCG Report contained recommendations focused on four key themes intended to optimize the operational capacity of the SEC: (i) reprioritize regulatory activities; (ii) reshape the organization; (iii) invest in enabling infrastructure; and (iv) enhance the self-regulatory organization engagement model.

The CHOICE Act would address these findings by requiring the SEC to implement the BCG Report's recommendations and submit legislative proposals to Congress for additional authority or flexibility. The legislation would update the structure of several SEC divisions and offices, including the Investor Advisory Committee, the Office of Credit Ratings, the Office of Municipal Securities, and the Ombudsman.

The CHOICE Act would reauthorize the SEC for a period of five years, subject to regular appropriations. The bill would eliminate the SEC Reserve Fund (created by Section 991 of the Dodd-Frank Act), which provides the SEC up to $100 million annually to spend at its discretion. Finally, the bill would reinstate the SEC's authority to collect registration fees, as well as transaction fees, under the federal securities laws to lower the amount of its appropriations.

Investor Protections. The CHOICE Act legislation would amend Section 913 of the Dodd-Frank Act, which authorizes, but does not require, the SEC to establish a uniform standard of care for broker-dealers and investment advisers, and also requires the SEC to study and issue a report on the issue. The CHOICE Act would require the SEC, before promulgating any such rule, to report to the House Committee on Financial Services and the Senate Committee on Banking, Housing, and Urban Affairs on whether:

- Retail customers are being harmed because broker-dealers are held to a different standard of conduct from that of investment advisers;
- Alternative remedies will reduce any confusion and harm to retail investors due to the different standard of conduct;
- Adoption of a uniform fiduciary standard would adversely impact the commissions of broker-dealers or the availability of certain financial products and transactions; and
- The adoption of a uniform fiduciary standard would adversely impact retail investors' access to personalized and cost-effective investment advice or recommendations about securities. Additionally, the SEC's chief economist would be required to support the report's conclusions with economic analysis.[35]

Section 921 of the Dodd-Frank Act would be eliminated under the CHOICE Act. That section authorizes the SEC to prohibit or restrict the use of predispute arbitration upon finding such a prohibition or restriction to be in the public interest and necessary for the protection of investors.

Asset-Backed Securities. The CHOICE Act would eliminate the risk retention requirements for asset-backed securities other than those backed by residential mortgages.

Credit Rating Agencies. The CHOICE Act would repeal Section 939F of the Dodd-Frank Act. That Section directs the SEC to study the credit rating process for structured finance products and the conflicts associated with the "issuer-pay" and the "subscriber-pay" models, as well as the feasibility of establishing a system in which a public or private utility or a self-regulatory organization assigns Nationally Recognized Statistical Rating Organizations ("NRSRO") to rate structured finance products, rather than permitting issuers to choose the NRSRO that will rate their products.

Accredited Investors. The CHOICE Act would expand the universe of accredited investors to include sophisticated individuals who do not otherwise satisfy the net worth test. The CHOICE Act is intended to promote capital formation and extend investment opportunity to less wealthy individuals. The legislation would amend the meaning of "accredited investor" under the Securities Act of 1933 to include persons who, in addition to current standards, either have a current securities-related license, or the SEC determines the person has demonstrable education or job experience to qualify as having professional subject-matter knowledge related to a particular investment. The last test would require the Financial Industry Regulatory Authority to verify the person's education or job experience.

Small Issuers. Section 989G of the Dodd-Frank Act made permanent the exemption for nonaccelerated filers to comply with an outside auditor's attestation of a company's internal financial controls mandated by Section 404(b) of the Sarbanes-Oxley Act. The CHOICE Act would extend the exemption to cover issuers with a market capitalization of up to $250 million and depository institutions with less than $1 billion in assets—small institutions.[36]

Executive Compensation. The CHOICE Act would repeal Sections 956 and 953(b) of the Dodd-Frank Act regarding incentive-based compensation and pay ratio disclosures.

Capital Formation. The CHOICE Act includes numerous provisions that are intended to further capital formation. The bill would facilitate the creation of venture exchanges in an effort to encourage smaller companies to access capital in the public markets. The bill would establish an independent SEC Small Business Capital Formation Advocate.

Repeal Conflict Mineral, Extractive Industries, and Mine Safety Disclosures. The CHOICE Act repeals the disclosure requirements of Title XV of the Dodd-Frank Act regarding conflict minerals, extractive industries, and mine safety.

Improving Insurance Regulation

The Dodd-Frank Act made two major changes to the role the federal government plays in the insurance industry. Title V of the Dodd-Frank Act created a new Federal Insurance Office ("FIO") within the Treasury Department to provide the federal government with information and expertise on insurance matters. The FIO Director is a nonvoting member of the FSOC. The Dodd-Frank Act mandated that one of the FSOC's voting members be an Independent Member with Insurance Expertise, with no other federal supervisory or regulatory duties.

The CHOICE Act would merge the FIO and the Independent Member with Insurance Expertise into one unified Independent Insurance Advocate ("IIA") who is nominated by the President, subject to the advice and consent of the Senate, for a six-year term of office. The IIA would be housed as an independent Office of the Independent Insurance Advocate within the Treasury Department.

The IIA would replace the Independent Member with Insurance Expertise as a voting FSOC member and would coordinate federal efforts on the prudential aspects of international insurance matters, including representing the United States in the International Association of Insurance Supervisors and assisting in the negotiations of covered agreements. The IIA would also consult with state insurance regulators regarding insurance matters of national importance and prudential insurance matters of international importance and will assist Treasury in administering the Terrorism Risk Insurance Act.

To promote accountability and transparency in the new office, the IIA would be required to testify before Congress twice a year. The IIA would be required to discuss in testimony the activities and objectives of the Office, any actions taken by the Office pursuant to covered agreements, the state of the insurance industry, and the scope of global insurance and reinsurance markets and the role such markets play in supporting insurance in the United States.

CONCLUSION

The U.S. financial regulatory landscape is likely to experience significant statutory and regulatory changes following the 2016 elections. Many of these changes may narrow the scope of financial services regulation, and some of these changes could raise the stakes by strengthening enforcement of existing and new laws and rules.

Changes in the leadership of executive departments and agencies will affect how existing laws are administered and interpreted even in the absence of statutory changes. Monetary and fiscal policy changes will also have significant effects on the financial services industry.

All of these changes could affect domestic institutions and foreign organizations that conduct business in the United States, and they could in some ways influence regulation in other countries.

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ENDNOTES

1 Pub. L. 111-203 (Jul. 21, 2010).

2 Trump-Pence Campaign information.

3 The House bill is H.R. 5983, the Financial Creating Hope and Opportunity for Investors, Consumers and Entrepreneurs Act ("CHOICE Act"), sponsored by House Financial Services Committee Jeb Hensarling (R-TX), and the Senate bill is S. 1484, the Financial Regulatory Improvement Act, sponsored by Sen. Richard C. Shelby (R-AL), who has reached his term limit as Chairman of the Senate Committee on Banking, Housing, and Urban Affairs.

4 A vote to end a filibuster of legislation requires 60 favorable votes to limit debate and advance a bill to the Senate floor.

5 For purposes of this *White Paper*, the federal financial institutions regulatory agencies are the Board of Governors of the Federal Reserve System ("Federal Reserve"), the Commodity Futures Trading Commission ("CFTC"), the CFPB, the Federal Deposit Insurance Corporation ("FDIC"), the Federal Housing Finance Agency ("FHFA"), the Office of the Comptroller of the Currency ("OCC"), and the Securities and Exchange Commission ("SEC").

6 President-elect Donald J. Trump, Financial Services (accessed Nov. 28, 2016) (italics added).

7 President-elect Donald J. Trump, Financial Services (accessed Nov. 28, 2016) (italics added).

8 Republican Platform 2016, Republican National Convention, p. 3.

9 *Id*.

10 Remarks of Donald J. Trump, Detroit Economic Club, Aug. 8, 2016. *See also* Remarks of Donald J. Trump, New York Economic Club, Sep. 15, 2016, available at.

11 *See* "Regulatory Insiders: Repeal of Dodd-Frank Unlikely," *F&I Magazine*, Greg Arroyo (Nov. 17, 2016).

12 5 U.S.C. §§ 801-808. The Congressional Review Act was enacted as Section 251 of the Contract with America Advancement Act of 1996 (Pub. L. 104-121), also known as the Small Business Regulatory Enforcement and Fairness Act of 1996.

13 The Midnight Rules Relief Act, H.R. 5982, passed the House of Representatives by a party-line vote of 240 in favor, 179 against.

14 *See* Trump Presidency Could Shift Regulatory Spotlight to State and AG," *New York Law Journal*, Joel Stashenko, Nov. 14, 2016, and "NY To Keep Up Pressure On Banks In Age of Trump," Law 360, Evan Weinberger, Nov. 15, 2016.

15 These agencies are the Department of the Treasury, the Federal Reserve, the OCC, the CFPB, the SEC, the FDIC, the CFTC, the FHFA, and the NCUA. The head of each of these agencies is a voting member of the FSOC. The FSOC also has a voting independent member with insurance expertise. The nonvoting members of the FSOC are the directors of the Office of Financial Research, the Federal Insurance Office, a state insurance commissioner, a state banking supervisor, and a state securities commissioner.

16 The Federal Reserve Banks are governed by boards of directors comprising local business and other leaders from their respective districts. Each of these boards appoints its Reserve Bank president. This enables regional and local input, and various Reserve Bank presidents serve as members of the Federal Open Market Committee. In recent years, this practice has been criticized by some in Congress who seek more centralized control from Washington, D.C., with less local, and less bank, influence on the boards of the Reserve Bank. The new Administration may maintain the current Reserve Bank system.

17 *See* "Donald Trump not Seeking Janet Yellen's Resignation," *Dow Jones Business News* (Nov. 9, 2016), and Remarks of Judy Shelton, as reported in *The Wall Street Journal*, "Donald Trump Not Seeking Janet Yellen's Resignation, Economic Adviser Says," (Nov. 9, 2016).

18 Janet L. Yellen, Testimony Before the Joint Economic Committee, U.S. Congress (Nov. 17, 2016); "Yellen Signals Fed Won't Be Cowed After Trump's Election Victory," Richard Miller and Christopher Condon, Bloomberg (Nov. 17, 2016).

19 While the Comptroller performs his duties under the general direction of the Secretary of the Treasury, the Secretary cannot delay or prevent rulemakings or intervene in enforcement proceedings, unless specifically provided by law. 12 U.S.C. § 1.

20 *PHH Corporation, et al., v. Consumer Financial Protection Bureau*, No. 15-117 (D.C. Cir. Oct. 11, 2016) ("*PHH v. CFPB*"). *See* Jones Day's *White Paper*, "In the Eye of the Storm: The Constitutional, Regulatory, and Political Implications of *PHH v. CFPB*," and our *Commentary*, "*PHH v. Consumer Financial Protection Bureau*: What it Means for Current and Future CFPB Enforcement."

21 Letter from House Financial Services Committee Chairman Hensarling (R-TX) to CFPB Director Cordray, Oct. 9, 2016.

22 *PHH v. CFPB* at 33.

23 Senator Shelby is expected to become Chairman of the Senate Appropriations Committee.

24 Republican Platform 2016, Republican National Convention, p. 3.

25 *See MetLife, Inc. v. FSOC,* 15-cv-00045 (D.D.C. Mar. 30, 2016).

26 Republican Platform 2016, Republican National Convention, p. 3.

27 Victoria Guida and Zachary Warmbrodt, *Trump's Victory Sparks Bankers' Hopes for New Deal*, Politico (Nov. 10, 2016).

28 Video release of "A Better Way."

29 Executive summary of the CHOICE Act.

30 In *Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837 (1984), the U.S. Supreme Court articulated a two-part test for determining whether a government agency's reading of a statute it is charged with administering is entitled to judicial deference. The first part of the test requires application of statutory analysis to evaluate whether Congress has directly spoken to the precise question at issue. If the statute is clear, no further analysis is applied. If the statute is ambiguous or silent, the Court moves to the second part of the test and considers whether the agency's interpretation is based on a permissible construction of the statute.

31 The CHOICE Act, A Republican Proposal to Reform the Regulatory System, June 23, 2016, p. 76.

32 The composite rating covers Capital, Assets, Management, Earnings, Liquidity, and Sensitivity to Market Risk, known as a CAMELS rating.

33 *See* FDIC Office of Inspector General, Office of Audits and Evaluations Report No. A4D-15-008, "The FDIC's Role in Operation Choke Point and Supervisory Approach to Institutions that Conducted Business with Merchants Associated with High Risk Businesses," Sep. 2015.

34 Boston Consulting Group, *U.S. Securities and Exchange Commission Organizational Study and Reform* (2011).

35 The Department of Labor finalized rules, effective April 10, 2017, that amend the definition of "investment advice" and "fiduciary" to expand the financial professionals activities and communications that are subject to fiduciary duties covered by the Employee Retirement Income Security Act of 1974, and its conflict of interest provisions. The DOL rules have been challenged in various court proceedings. *See* SIFMA, DOL Fiduciary Standard Resource Center.

36 *See* Pub. L. 113-250 (Dec. 18, 2014) and Amendments to the Federal Reserve's Small Bank Holding Company Policy Statement, 80 Fed. Reg. 20153 (Apr. 15, 2015).