



FACT SHEET

An Analysis of the House Republicans' Plan to Dismantle Financial Reform

Gregg Gelzinis, Ethan Gurwitz, Sarah Edelman, and Joe Valenti April 19, 2017

During his campaign, Donald Trump promised a near-dismantling of the Dodd-Frank Act, the core piece of financial reform legislation enacted following the 2007-2008 financial crisis.¹ He doubled down on that promise once in office, vowing to both “do a big number” on and give “a very major haircut” to Dodd-Frank.² In early February, he took the first step in fulfilling this dangerous promise by signing an executive order directing U.S. Secretary of the Treasury Steve Mnuchin to conduct a review of Dodd-Frank.³ Per the executive order, Secretary Mnuchin will present the findings in early June.⁴ While the country waits for President Trump’s plan, it is useful to analyze one prominent way Trump and Congress might choose to gut financial reform—through the Financial CHOICE Act.⁵

Introduced in the last Congress by U.S. House of Representatives Financial Services Committee Chairman Jeb Hensarling (R-TX) and expected to be reintroduced in the coming weeks, the Financial CHOICE Act offers a blueprint for how Trump might view these issues. During the presidential campaign, Rep. Hensarling briefed Trump on his ideas regarding financial deregulation and was reportedly on Trump’s short list for treasury secretary.⁶

A return to financial instability that threatens the economy

Each prong of Dodd-Frank’s financial stability reforms is directly related to clear and unmistakable lessons learned in the financial crisis. The Financial CHOICE Act’s desire to unwind these reforms demonstrates a willful ignorance of those very lessons at best and a malicious disregard at worst.

Bank deregulation

- If a bank maintains a 10 percent quarterly leverage ratio, it can choose to opt out of Dodd-Frank’s enhanced prudential standards—including risk-based capital requirements, liquidity requirements, risk management standards, resolution plans such as living wills, stress testing, and others—an insufficient level of capital to justify massive deregulation.

- If a bank that opted out of these enhanced standards fell below the 10 percent quarterly leverage ratio, it would have a full year to raise its quarterly leverage ratio back to 10 percent—making it easy for banks to game this 12-month clock and fluctuate above and below the leverage ratio.
- For banks that do not opt out of the Dodd-Frank Act’s enhanced prudential standards, the Financial CHOICE Act severely weakens the annual stress testing process.

Systemic risk deregulation

- Eliminates the Financial Stability Oversight Council’s, or FSOC’s, authority to designate nonbank financial institutions as systemically important and subject them to enhanced oversight and prudential regulation by the Federal Reserve
- Eliminates FSOC’s authority to break up financial institutions that pose a grave threat to U.S. financial stability
- Eviscerates FSOC’s budget and eliminates the Office of Financial Research, created by Dodd-Frank to give FSOC the data and research capacity necessary to successfully execute its role

Fewer orderly shut-downs, more bailouts

- Repeals the Orderly Liquidation Authority, a new tool created by Dodd-Frank that gives regulators the ability to wind down a big bank when it fails, so that no government bailouts are necessary

Derivatives deregulation

- Repeals Title VIII of the Dodd-Frank Act, which gives FSOC the authority to designate financial market utilities as systemically important and subject them to heightened risk management standards

Willful blindness on insurance

- Merges the Federal Insurance Office with FSOC’s Office of the Independent Member with Insurance Expertise to create a new, severely weakened insurance office

Concentration, accountability, and the real economy

Financial firms with hundreds of billions and even trillions of dollars in assets are the real winners in the Financial CHOICE Act, while accountability and the real economy are the losers.

Reopening the Wall Street casino

- Repeals the Volcker rule, allowing banks to engage in risky proprietary trading and sponsor and invest in private equity/hedge fund units for their profit

Concentration limits and return to mega-mergers

- Rolls back Dodd-Frank Act provisions that give regulators the authority to evaluate and limit mergers and acquisitions of financial institutions based on consideration of financial stability and concentration

Bringing the U.S. Securities and Exchange Commission, or SEC, to heel

- Shifts SEC enforcement of complex cases away from administrative hearings and toward federal court proceedings, removing an important tool for overseeing regulated industries
- Eliminates the requirement for banks to hold a specified percentage of the credit risk of the nonresidential assets they securitize, reinjecting into the market the perverse securitization incentives that contributed to the financial crisis

Removing transparency in private equity

- Eliminates registration and reporting requirements for private equity firms, preventing regulators from having access to important data on hundreds of billions of dollars in assets and leaving investors in these funds to once again fend for themselves

Excessively compensating the wealthy and powerful

- Eliminates regulators' authority to curb compensation practices that, prior to the crisis, created perverse incentives for CEOs to take excessive risks for huge bonuses tied to short-term gains and little downside if massive losses were incurred
- Eliminates the requirement that companies disclose the pay ratio comparing the median employee compensation with the CEO's compensation

Undermining the goals of monetary policy

- Requires the Federal Reserve to calculate an interest rate target according to a version of the Taylor rule and then justify to Congress any deviation between that value and the interest rate target actually chosen⁷

Consumer protection

The Financial CHOICE Act rejects the painful lessons about toxic financial products learned from the financial crisis and Great Recession in which 10 million families lost their homes and Americans collectively lost trillions of dollars in wealth.⁸

Crippling the Consumer Financial Protection Bureau, or CFPB

- Takes away the CFPB's independence by politicizing its director and replacing direct funding from the Federal Reserve with annual congressional appropriations

- Shrinks the agency's ability to identify and address financial wrongdoing by ending its supervision authority, consumer complaint database, and research and education functions and by greatly limiting regulation and enforcement authority

Reopening the door to known predatory practices

- Allows a creditor of any size to once again make most mortgages without regard to a consumer's ability to repay the loan as long as the creditor holds the mortgage in its portfolio
- Guts protections against overcharging consumers on title insurance through affiliated companies, which are companies that are often under the same corporate umbrella as the lender
- Strips consumer protections from manufactured home borrowers, many of whom are rural, lower-income, and/or seniors
- Enables recklessness by removing the CFPB's ability to pursue financial actors engaged in unfair, deceptive, or abusive practices and by scaling back enforcement powers to exclude cash compensation for victims
- Blocks the fiduciary rule, which requires all retirement financial advisers to act in the best interest of their clients, closing a 40-year-old loophole, and is expected to save retirees \$17 billion annually⁹
- Prohibits both the CFPB and the SEC from taking steps to limit the use of mandatory consumer arbitration

Gregg Gelzimis is a Special Assistant for the Economic Policy team at the Center for American Progress. Ethan Gurwitz is a Research Associate with the Economic Policy team at the Center. Sarah Edelman is the Director of Housing Policy at the Center. Joe Valenti is the Director of Consumer Finance at the Center.

Endnotes

1 Billy House and Kevin Cirilli, "Trump's Dodd-Frank Plan Will Be Early Test of Republican Unity," Bloomberg, May 19, 2016, available at <https://www.bloomberg.com/politics/articles/2016-05-19/trump-s-dodd-frank-plan-will-be-early-test-of-republican-unity>.

2 Glenn Thrush, "Trump Vows to Dismantle Dodd-Frank 'Disaster,'" *The New York Times*, January 30, 2017, available at https://www.nytimes.com/2017/01/30/us/politics/trump-dodd-frank-regulations.html?_r=0; Jessica Dye, "Trump vows 'major haircut' for Dodd-Frank," *Financial Times*, April 4, 2017, available at <https://www.ft.com/content/fb08a355-f7fc-3021-8c92-d94a-f9a2f35b>.

3 Executive Order no. 13,772, *Code of Federal Regulations* (2017), available at <https://www.whitehouse.gov/the-press-office/2017/02/03/presidential-executive-order-core-principles-regulating-united-states>.

4 Ibid.

5 *Financial CHOICE Act of 2016*, H. Rept. 5983, 114 Cong. 2 sess. (Government Printing Office, 2016), available at <https://www.congress.gov/114/bills/hr5983/BILLS-114hr5983rh.pdf>.

6 Donna Borak, "Donald Trump, Jeb Hensarling Meet on Dodd-Frank Alternative," *The Wall Street Journal*, June 7, 2016, available at <https://www.wsj.com/articles/donald-trump-jeb-hensarling-meet-on-dodd-frank-alternative-1465335535>; Damien Palette, Ryan Tracy, and Michael C. Bender, "Trump Team Considering Rep. Jeb Hensarling as Treasury Secretary," *The Wall Street Journal*, November 10, 2016, available at <https://www.wsj.com/articles/donald-trump-considering-rep-jeb-hensarling-as-treasury-secretary-1478812583>.

7 For a brief description of the Taylor Rule, see Ben S. Bernanke, "The Taylor Rule: A benchmark for monetary policy?," Brookings Institution, April 28, 2015, available at <https://www.brookings.edu/blog/ben-bernanke/2015/04/28/the-taylor-rule-a-benchmark-for-monetary-policy/>.

8 Annalyn Kurtz, "U.S. soon to recover all jobs lost in crisis," CNN Money, June 4, 2014, available at <http://money.cnn.com/2014/06/04/news/economy/jobs-report-recovery/>; U.S. Department of the Treasury, *The Financial Crisis Response In Charts* (2012), available at https://www.treasury.gov/resource-center/data-chart-center/Documents/20120413_FinancialCrisisResponse.pdf; National Center for Policy Analysis, "The 2008 Housing Crisis Displaced More Americans than the 1930s Dust Bowl," May 11, 2015, available at http://www.ncpa.org/sub/dpd/index.php?Article_ID=25643.

9 Joe Valenti, "A Secure Retirement Demands Limiting Conflicts of Interest," Center for American Progress, April 6, 2016, available at <https://www.americanprogress.org/issues/economy/news/2016/04/06/134883/a-secure-retirement-demands-limiting-conflicts-of-interest/>.