XIII. Reform of the Dodd-Frank Act and its Implications

The Dodd–Frank Wall Street Reform and Consumer Protection Act[1311] (Dodd-Frank Act or Act) emerged from the ashes of the global financial crisis and was introduced by the Obama administration in an effort to prevent another financial crisis from crippling the United States.[1312] The Act has been described as "the biggest overhaul of financial regulations since the Great Depression."[1313] It was designed "[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system, to end 'too big to fail,' to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes."[1314] The financial reform introduced by the Dodd-Frank Act was more aggressive than past reforms, with a clear emphasis on consumer protection, financial stability, and prudential regulation.[1315]

From its conception, the Dodd-Frank Act has been a severe point of contention.[1316] Many market participants have opposed the Dodd-Frank Act for being overly stringent and ineffective, and its dissenters have called for its repeal or amendment.[1317] The Act has been generally criticized for imposing massive regulatory costs on financial institutions, driving out smaller banks that are unable to take on the regulatory burden of compliance.[1318] The Dodd-Frank Act

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[1311] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111–203, 124 Stat. 1376 (2010) (codified in scattered sections of the U.S.C.).

[1312] *See generally* President Obama, Remarks at Cooper Union on Wall Street Reform (Apr. 22, 2010), http://abcnews.go.com/Politics/transcript-obama-wall-street-speech-financial-reform/story?id=10446690 [https://perma.cc/KXF9-296V].

[1313] Don Lee & Jim Puzzanghera, *Trump has vowed to slash regulations. Where he might start and the hurdles he faces*, L.A. TIMES (Jan. 19, 2017), http://www.latimes.com/politics/la-fi-trump-regulatory-reform-20170119-story.html [https://perma.cc/PJJ8-TUC3].

[1314] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. (2010).

[1315] *See* WORLD SCIENTIFIC, DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT 5 (Douglas Evanoff & William F. Moeller eds. 2014).

[1316] *See* Lee & Puzzanghera*, supra* note 3.

[1317] *See The right way to redo Dodd-Frank*, THE ECONOMIST (Feb. 11, 2017), http://www.economist.com/news/leaders/21716607-make-rules-simpler-all-means-not-expense-safety-right-way-redo [https://perma.cc/G6H6-N595].

[1318] *See* Jeb Hensarling, *After Five Years, Dodd-Frank Is a Failure*, WALL ST.

has its supporters, however, with many fighting against its repeal or reform, fearing that the very values the Dodd-Frank Act sought to protect in the aftermath of the crisis would be diluted.[1319]

The election of Donald J. Trump as the 45th President of the United States and confirmation of Steven Mnuchin,[1320] a staunch opponent of the Dodd-Frank Act,[1321] signal drastic changes to the Dodd-Frank Act.[1322] In the build-up to the General Election, then GOP candidate Trump believed that the Dodd-Frank Act was stifling to the financial markets.[1323] Since assuming office, President Trump signed an Executive Order on February 3, 2017,[1324] directing the Treasury Secretary and Financial Stability Oversight Council (FSOC) to assess and identify financial regulations that promote or inhibit his stated principals for the regulation of the U.S. financial system.[1325] The

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J. (July 19, 2015), https://www.wsj.com/articles/after-five-years-dodd-frank-is-a-failure-1437342607 [https://perma.cc/ENK2-BFKR].

[1319] *See* Michael S. Barr, *Trump's Dismantling of Dodd-Frank Would Be 2008 All Over Again*, FORTUNE (Dec. 8, 2016), http://fortune.com/2016/12/08/trump-dodd-frank-2008-financial-crisis-steve-mnuchin/ [https://perma.cc/5MTC-WFET].

[1320] David Lawder, *Ex-Goldman banker Mnuchin installed as Treasury secretary,* REUTERS (Feb. 14, 2017), http://www.reuters.com/article/us-usa-congress-mnuchin-idUSKBN15S0H0 [https://perma.cc/Y4ZR-8JYZ].

[1321] *See* Lee & Puzzanghera, *supra* note 3.

[1322] *See* Ben Lane, *Pence, Hensarling: Dismantling Dodd-Frank remains a high priority*, HOUSINGWIRE (Jan. 26, 2017), http://www.housingwire.com/articles/39051-pence-hensarling-dismantling-dodd-frank-remains-a-high-priority [https://perma.cc/N98G-T5FG].

[1323] *See* Telis Demos & David Reilly, *Maybe Trump's Friends 'Can't Borrow Money,' but Banks Are Lending*, WALL ST. J.: MONEYBEAT (Feb. 3, 2017, 5:53 PM), http://blogs.wsj.com/moneybeat/2017/02/03/maybe-trumps-friends-cant-borrow-money-but-banks-are-lending/ [https://perma.cc/B9VQ-FUWU].

[1324] *See* Exec. Order No. 13772, 82 Fed. Reg. 9965 (Feb. 3, 2017), https://www.gpo.gov/fdsys/pkg/FR-2017-02-08/pdf/2017-02762.pdf [https://perma.cc/TAQ9-CM8N].

[1325] *Id.* (listing President Trumps principles of regulations, as: "(a) empower Americans to make independent financial decisions and informed choices in the marketplace, save for retirement, and build individual wealth; (b) prevent taxpayer-funded bailouts; (c) foster economic growth and vibrant financial markets through more rigorous regulatory impact analysis that addresses systemic risk and market failures, such as moral hazard and information asymmetry; (d) enable American companies to be competitive with foreign firms

Executive Order was introduced as a starting point for significant financial deregulation under the Trump administration.[1326] This Executive Order indicates the potential repeal or clawback of portions the Dodd-Frank Act.[1327] The Trump administration's commitment to reform the Dodd-Frank Act has been lauded by the many, with the House Financial Services Committee releasing their proposed alternative to the Act, Financial Choice 2.0, which includes detailed considerations on parts of the Act that should be repealed or undergo reform.[1328]

This article focuses on the most pressing specific areas of reform of the Dodd-Frank Act based on indications from members of the Trump administration. The article identifies three potential areas of reform and discusses the implication of each reform. Section A discusses the Volcker Rule, analyzing criticisms of the rule and implications of the repeal. Section B addresses reform to the Consumer Financial Protection Bureau (CFPB), including potential areas of reform in its governance and funding structure. Lastly, Section C discusses reform to oversight of non-bank institutions deemed systemically important, including mechanisms of reform to this area and implications.

A. The Volcker Rule

The Volcker Rule (the rule) is embodied in Section 619 of the Dodd-Frank Act.[1329] It modified the Bank Holding Company Act 1957

in domestic and foreign markets; (e) advance American interests in international financial regulatory negotiations and meetings; (f) make regulation efficient, effective, and appropriately tailored; and (g) restore public accountability within Federal financial regulatory agencies and rationalize the Federal financial regulatory framework").

[1326] *See* Justin Sink et al., *Trump to Order Dodd-Frank Review, Halt Obama Fiduciary Rule*, BLOOMBERG (Feb. 3, 2017), https://www.bloomberg.com/politics/articles/2017-02-03/trump-to-halt-obama-fiduciary-rule-order-review-of-dodd-frank [https://perma.cc/SKS2-QBM8].

[1327] *Id.*

[1328] Financial Choice Act, H.R. 10, 115th Cong. (Discussion Draft 2017), https://financialservices.house.gov/uploadedfiles/choice_2.0_discussion_draft.pdf [https://perma.cc/UE8M-B5GR]; Daniel F.C. Crowley et al., *The Financial CHOICE Act 2.0, Legislative Text Revealed*, NAT'L L. REV. (Apr. 27, 2017), http://www.natlawreview.com/article/financial-choice-act-20-legislative-text-revealed [https://perma.cc/7HP3-B74M].

[1329] 12 U.S.C. § 1841 (2012).

(BHCA) by adding Section 13 to the BHCA.[1330] The rule is designed to prohibit "banking entities" from engaging in forms of propriety trading and from having interests in certain hedge funds and private equity funds.[1331] Therefore, under the rule, banks are prohibited from using capital of their own to trade and from engaging in forms of investments deemed speculative, such as investments into hedge funds and private equity. [1332]

1. Criticism of the Rule

The rule has been opposed by the Republican-led Congress and the Trump administration.[1333] Its application is broad, as it applies to "banking entities," a new term coined by the provision, which includes "all banking institutions and all affiliates of banking institutions."[1334] As such, the rule is broader in its application than to merely banks or Bank Holding Companies.[1335] The rule even extends to entities not affiliated with insured depository institutions, such as foreign banks with uninsured branches in the United States and limited-purpose trust companies with insured deposits.[1336] Accordingly, there has been concern over the competitiveness of U.S. institutions subject to the rule compared to foreign banks that are not subject to the rule.[1337]

A staff working paper circulated by the Federal Reserve Board's Divisions of Research & Statistics and Monetary Affairs on December 22, 2016 substantiates some criticisms and provides support for softening or repealing the rule.[1338] The paper suggests the

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[1330] *Id.*; § 1851.

[1331] § 1851(a)(1); *see* Bryan Settelen, Dev. Art., *The Volcker Rule's Market Making Exemption,* 31 REV. BANKING & FIN. L. 556 (2012); *Volker Rule: Frequently Asked Questions*, BOARD GOVERNORS FED. RES. SYS., https://www.federalreserve.gov/bankinforeg/volcker-rule/faq.htm [https://perma.cc/2J82-5FDU].

[1332] § 1851.

[1333] *Drop the Volcker rule and keep what works*, FIN. TIMES (Feb. 12, 2017), https://www.ft.com/content/72f3ba98-eef1-11e6-930f-061b01e23655 [https://perma.cc/6SFE-AG8N].

[1334] MICHAEL S. BARR ET AL., FINANCIAL REGULATION: LAW AND POLICY 683 (University Casebook Series ed., 2016).

[1335] *Id*. at 684.

[1336] *Id*.

[1337] Chloe Brighton, Dev. Art., *The Finalized Volcker Rule*, 33 REV. BANKING & FIN. L. 514 (2014).

[1338] Jack Bao et al., *The Volcker Rule and Market-Making in Times of Stress*, rule has a "deleterious effect on corporate bond liquidity and dealers subject to the rule become less willing to provide liquidity during stress times. While dealers not affected by the rule have stepped in to provide liquidity, we find that the net effect is a less liquid corporate bond market."[1339]

The rule has also been critiqued for its ambiguity from a regulatory agency standpoint.[1340] Many banking agencies have authority to manage and regulate the rule over the financial industry and have issued their own guidance on the rule.[1341] The Securities and Exchange Commission (SEC) and several federal banking agencies issued joint rules governing the addition of Section 13.[1342] These points indicate that the ambiguities surrounding the rule have forced agencies and market participants to promulgate their own interpretation of the rule.[1343]

2. Implications of Repeal

There have been numerous possibilities on the future of the rule. Financial Choice 2.0, a Republican-sponsored bid[1344] for financial regulatory reform has proposed that the rule be completely abolished and repealed.[1345] There have also been suggestions that the "market making" exception to the rule be revised to reduce complexity and confusion to make it easier to distinguish between legitimate market making and proprietary trading.[1346] In addition, the rule's application

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(Bd. of Governors of the Fed. Reserve Sys., Finance and Economics Discussion Series 2016-102, 2016), https://www.federalreserve.gov/econresdata/feds/2016/files/2016102pap.pdf [https://perma.cc/WTB7-SNBJ].

[1339] *Id.* at 30.

[1340] BARR ET AL., *supra* note 24, at 683.

[1341] *Id.*

[1342] *See generally* Prohibitions and Restrictions on Proprietary Trading and Certain Interests In, and Relationships With, Hedge Funds and Private Equity Funds, 79 Fed. Reg. 5536 (Jan. 31, 2014) (codified at 12 C.F.R. pt. 255).

[1343] *Id.*; BARR ET AL., *supra* note 24, at 683.

[1344] *See* SULLIVAN & CROMWELL, FINANCIAL CHOICE ACT "2.0" 3 (2017), https://sullcrom.com/siteFiles/Publications/SC_Publication_Financial_CHOICE_Act_2.0.pdf [https://perma.cc/3BNG-X3MK].

[1345] Financial Choice Act, H.R. 10, 115th Cong. 1 (2017).

[1346] SULLIVAN & CROMWELL, *supra* note 34 ("Modifications to the Volcker Rule to simplify compliance, encourage market making, and preserve market liquidity."). *See generally* Milan Dalal, Lecture at Boston University School of Law, Lessons from the Financial Crisis Course (Apr. 18, 2017) (summarizing may be modified to only apply to depository institutions.[1347] Another way of weakening the rule would be via passive enforcement, where the Trump administration could decide to elect regulators who are inclined not to enforce the rule.[1348] A final suggestion would be to require financial institutions that engage in proprietary trading to hold higher levels of capital as a safeguard.[1349]

The absolute repeal of the rule may dangerously lead to a pre-crisis situation, by allowing banks to abuse public money for speculative gain.[1350] Concern over the possibility of the rule's repeal has led supporters to remind Congress of the consequences of allowing speculative investments.[1351] Supporters of the rule point to Bear Sterns, the first financial institution to fail during the crisis due to heavy losses incurred from speculative investments in real estate.[1352] The rule is seen as a safeguard against such risky activity by banks.[1353]

However, a key aggravating factor of the 2008 financial crisis being one of the worst in history was the liquidity crunch faced by market participants.[1354] Relaxing the application of the rule may be beneficial and necessary to enhance liquidity, particularly during

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the conventional application of market making and surveying the Federal Reserve's and financial industry's commentary on the rule).

[1347] Lisa Lambert & David Lawder, *Trump Treasury nominee wants to loosen limits under Volcker rule: document*, REUTERS (Jan. 23, 2017), http://www.reuters.com/article/us-usa-trump-volcker-idUSKBN1572X9 [https://perma.cc/HD4D-GEQS] (stating that Mnuchin believes the rule should only apply to "a bank that benefits from federal deposit insurance").

[1348] *See* Matt Egan, *Wall Street hates the Volcker Rule. Will Trump finally kill it?*, CNN MONEY (Jan. 9, 2017), http://money.cnn.com/2017/01/09/investing/volcker-rule-trump-wall-street/ [https://perma.cc/PV2K-MZUL].

[1349] *See* Interview with James Gorman, Chairman & CEO, Morgan Stanley, on Charlie Rose (Apr. 9, 2012), https://charlierose.com/videos/15813 [https://perma.cc/6Z3K-6NQA] ("[A] much more elegant solution to the Volcker rule was not to try and legislate what you can and can't do. Simply say if you want to do that, here's the amount of capital we're going to require you to hold against those activities and make it so punitive nobody is going to want to do it because your shareholders won't let you.").

[1350] *See* Egan, *supra* note 38 (explaining that institutions such as Bear Stearns failed due to the speculative investments that the rule was designed to prohibit).

[1351] *Id.*

[1352] *Id.*

[1353] *See id.*

[1354] *Id.*

times of stress for the U.S. financial markets.[1355] The Federal Reserve staff working paper studied the behavior of dealers subject to the Volcker Rule, concluding that such dealers rely on agency trades rather than dealer-customer trades, and are less likely to commit their own capital, which contributes to illiquidity.[1356] The paper concluded that the illiquidity of bonds in stress periods is dangerously close to the pre-crisis era.[1357] It may actually be necessary to soften the reach of the rule to stimulate liquidity to avoid triggering a repeat of 2008.[1358]

B. Consumer Financial Protection Bureau

The CFPB was established by the Dodd-Frank Act[1359] to address the flaws in consumer financial regulation.[1360] Its sole mandate is to protect consumers, with wide functions spanning from financial education programs, to research, supervision, and investigation.[1361] The CFPB has sweeping powers over nearly all consumer financial services providers, including non-banks.[1362] Proposed by Senator Elizabeth Warren,[1363] its creation has been opposed as providing an excessively paternalistic mandate over consumer choice.[1364] Critics believe the powers of the CFPB, which cover almost every aspect of

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[1355] *See id.* (citing a paper published by the Federal Reserve that concluded that the rule had a harmful effect on corporate bond liquidity).
[1356] Bao et al., *supra* note 28, at 30.
[1357] *Id.* at 29 (explaining that illiquidity levels are now approaching the levels seen in the financial crisis).
[1358] *See* Egan, *supra* note 38.
[1359] *See generally* Dodd-Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C § 5491(b)–(c) (2012).
[1360] *See* BARR ET AL., *supra* note 24, at 552.
[1361] *See id.* at 566.
[1362] *Id.* at 552.
[1363] *See* Elizabeth Warren, *Unsafe at Any Rate*, DEMOCRACY J., Summer 2017, at 8, 16, http://democracyjournal.org/magazine/5/unsafe-at-any-rate/ [https://perma.cc/7TDK-SX6C] ("If it's good enough for microwaves, it's good enough for mortgages. Why we need a Financial Product Safety Commission.").
[1364] *See Creating a Consumer Financial Protection Agency: Hearing Before the Comm. on Banking, Hous., & Urban Affairs*, 111th Cong. 1 (2009) (statement of Sen. Richard C. Shelby), https://www.gpo.gov/fdsys/pkg/CHRG-111shrg54789/pdf/CHRG-111shrg54789.pdf [https://perma.cc/7E4A-5438].

the financial industry linked to consumers, are too far-reaching and broad.[1365]

Before the creation of the CFPB, its functions of consumer financial responsibility were divided among several federal regulators, including Office of the Comptroller of the Currency, the Federal Reserve Board, and the Office of Thrift Supervision, with the task of consumer protection being spread over a variety of agencies with different regulatory powers and concerns.[1366] The CFPB was tasked with protecting consumers against financial fraud and is fighting to stay alive under the Trump administration.[1367]

1. Areas of Potential Reform for the CFPB

It is unlikely that the CFPB will be disbanded under the Trump administration, but it may undergo reform to its governance and funding structure.[1368] These areas have been proposed for reform under the recently introduced Financial Choice 2.0.[1369]

Currently, the CFPB is headed by a director, who is appointed by the President with the Senate's approval for a five-year term.[1370] A CFPB Director can be removed for cause, such as "inefficiency, neglect of duty, or malfeasance in office."[1371] This governance structure and added safeguard protect against the removal of the Director for political reasons.[1372] However, this structure has been subject to criticism during its formation[1373] and has recently been declared unconstitutional by the U.S. Court of Appeals for the D.C. Circuit in

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[1365] *See id*. at 46 (statement of Yingling).

[1366] Adam J. Levitin, *The Consumer Financial Protection Bureau: An Introduction*, 32 REV. BANKING & FIN. L. 327 (2012); Adam J. Levitin, *The Consumer Financial Protection Agency* 1, 3 (Georgetown Law & Econ. Research Paper No. 1447082, 2009), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1447082 [https://perma.cc/8UZC-4CNJ].

[1367] Suzanne O'Halloran, *Consumer Financial Protection Bureau Fights to Stay Alive Under Trump*, FOX BUS. (Jan. 27, 2017), http://www.foxbusiness.com/politics/2017/01/27/consumer-financial-protection-bureau-fights-to-stay-alive-under-trump.html [https://perma.cc/ZXC5-5BC9].

[1368] *Id.*

[1369] Financial Choice Act, H.R. 10, 115th Cong. (2017).

[1370] BARR ET AL., *supra* note 24, at 567.

[1371] 12 U.S.C. § 5491(c)(3) (2012); BARR ET AL., *supra* note 24, at 567.

[1372] BARR ET AL., *supra* note 24, at 568.

[1373] O'Halloran, *supra* note 57.

PHH Corp. v. Consumer Financial Protection Bureau.[1374] The court ruled that the CFPB's organization is unconstitutionally structured, as the CFPB's single director can only be removed for cause, and not at the President's will.[1375] The U.S. Department of Justice (DOJ) signaled it will not support the CFPB on appeal, and has taken the stance that the CFPB governance structure is unconstitutional by filing an amicus brief supporting the court's ruling.[1376] The CFPB is cornered, given it will face an uphill battle without the DOJ's support should this constitutionality issue reach the Supreme Court.[1377] Furthermore, the Trump administration has made strides to dismantle the present CFPB governance structure in order to create one that is not wholly independent of the President, where the CFPB is chaired by a board of governors (possibly elected by the President) rather than a single director.[1378]

The CFPB is automatically funded by "the combined earnings of the Federal Reserve System."[1379] This funding structure, which is distinct from congressional apportions, enables the CFPB to operate independently from congressional pressures on enforcement and rulemaking.[1380] While it grants the CFPB independence, it also

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[1374] PHH Corp. v. Consumer Fin. Prot. Bureau, 839 F.3d 1 (D.C. Cir. 2016) (stating the CFPB was unconstitutionally structured as its single director could not be removed at will). *See generally* William Simpson, Note, *Above Reproach: How the Consumer Financial Protection Bureau Escapes Constitutional Checks & Balances*, 36 REV. BANKING & FIN. L. 343 (2017).

[1375] *Id.* at 64; *see* DAVIS POLK, WHAT'S NEXT FOR PHH V. CFPB? (2016), https://www.davispolk.com/sites/default/.../2016-10-17_whats_next_phh_v._cfpb.pdf [https://perma.cc/6RTQ-WQ96].

[1376] Brief for the United States as Amicus Curiae at 23, *PHH Corp.*, 839 F.3d 1 (2017) (No. 15-1177), https://assets.documentcloud.org/documents/3519662/3-17-17-US-Amicus-Brief-PHH.pdf [https://perma.cc/W6QU-RX56].

[1377] *See* Jonathan H. Adler, *What happens when the Justice Department files a brief against a federal agency?*, WASH. POST (Mar. 18, 2017), https://www.washingtonpost.com/news/volokh-conspiracy/wp/2017/03/18/what-happens-when-the-department-of-justice-files-a-brief-against-a-federal-agency/?utm_term=.06e0b5d35a21 [https://perma.cc/T7EH-97UG0].

[1378] O'Halloran, *supra* note 57.

[1379] 12 U.S.C § 5497(a)(1) (2012); BARR ET AL., *supra* note 24, at 567.

[1380] BARR ET AL., *supra* note 24, at 568; *see* Kirti Dalta & Richard L. Revesz, *Deconstructing Independent Agencies (and Executive Agencies)*, 98 CORNELL L.J. 769, 806 (2013) ("[T]he relationship between independence from the President and OMB budget control is clear: 'it cannot be denied that there is makes the CFPB unaccountable to the taxpayer, as its budget is not approved by Congress annually, leading to criticisms in its choice of spending.[1381] A reform of the funding structure of the CFPB is being discussed, to ensure the CFPB does not rely on the Federal Reserve.[1382] Steve Mnuchin has supported the alteration of funding of the CFPB to provide Congress more control, steering the organization away from Federal Reserve funding.[1383]

2. Implications of CFPB Reform

The CFPB's structure, which protects it from immediate political influence, is also a source of criticism for those who demand more accountability from the CFPB.[1384] The CFPB's sweeping powers have enabled it to conduct investigations into the fraudulent accounts scandal perpetuated by Wells Fargo, protecting financial consumers from corrupt practices and indicating a politically neutral stance in pursuing its mandate.[1385] Curbing the CFPB's broad powers would mean that the United States would lose the effectiveness of its

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a direct relation between budget control and policymaking.'").

1381 Dorothy Jetter, *Rep. Ratcliffe and Sen. Cruz Introduce Legislation to Dismantle the CFPB*, AMER. TAX REFORM (July 23, 2015), https://www.atr.org/rep-ratcliffe-and-sen-cruz-introduce-legislation-dismantle-cfpb [https://perma.cc/XWE6-VSLY] ("The Bureau's wasteful spending has largely gone unchecked due to an overall lack of oversight and accountability. The CFPB is not required to have their budget approved by Congress, unlike other government agencies.").

1382 *Id.*

1383 Jessica Dye, *Trump treasury secretary pick Mnuchin eyes streamlined bank regulation*, FIN. TIMES (Jan. 19, 2017), https://www.ft.com/content/bcb5c46e-bb0b-30ec-adee-178454e0560f [https://perma.cc/T5G3-4XQ3] (explaining that Steven Mnuchin did not support the CFPB being funded from the Federal Reserve without undergoing an appropriation process).

1384 BARR ET AL., *supra* note 24, at 568.

1385 *Consumer Financial Protection Bureau Fines Wells Fargo $100 Million for Widespread Illegal Practice of Secretly Opening Unauthorized Accounts*, CONSUMER FIN. PROTECTION BUREAU (Sep. 8, 2016), https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-fines-wells-fargo-100-million-widespread-illegal-practice-secretly-opening-unauthorized-accounts/ [https://perma.cc/G4SM-PBF4]. *See generally* Merric Kaufman, Dev. Art., *"Lions Hunting Zebras": The Wells Fargo Fake Accounts Scandal and its Aftermath*, 36 REV. BANKING & FIN. L. 436 (2017).

strongest consumer-centric regulator, one that was deemed necessary to fill in regulatory gaps that led to the 2008 sub-prime crisis.[1386] Altering the CFPB's funding structure by requiring congressional approval for its budget would make the independent regulator subject to political influence, which can impact the scope and effectiveness of its investigations.[1387] Likewise, the altering the governance structure from a single-director structure to that of a panel or board of governors elected by the President presents the same concern—political interference in an organization that was designed to be politically neutral.[1388]

C. Reduced Oversight Over Large Non-Banks Deemed Systemically Important

1. The SIFI Designation

The regulatory landscape was shifted by the Dodd-Frank Act, from one that exclusively focused on microprudential regulation to one that included macroprudential regulation, taking into account overall market risks.[1389] The Systemically Important Financial Institution (SIFI) designation was established after the 2008 financial crisis, when it became apparent that many financial institutions, due to their size and control of the market, could cause system-wide failures.[1390] The phenomenon of "Too Big to Fail" manifested, with large, complex, and interwoven institutions[1391] having the ability to devastate the economy with externalities from their failure having a cumulative, trickle-down impact on various sectors.[1392] There was a need for regulation of such systemic risk, as there was no existing incentive for market participants to manage the impact of risky market behavior on third parties or the economy as a whole.[1393]

In line with the regulatory shift to broader macroprudential regulation, the Dodd-Frank Act created the FSOC[1394] and granted

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[1386] Barr, *supra* note 9
[1387] O'Halloran, *supra* note 57.
[1388] BARR ET AL., *supra* note 24, at 568.
[1389] WORLD SCIENTIFIC, *supra* note 5, at 6.
[1390] BARR ET AL., *supra* note 24, at 698.
[1391] WORLD SCIENTIFIC, *supra* note 5, at 114.
[1392] BARR ET AL., *supra* note 24, at 698.
[1393] Steven L. Schwarcz, *Systemic Risk*, 97 GEO. L.J. 193, 198 (2008).
[1394] *See* BARR ET AL., *supra* note 24, at 704 ("The FSOC is headed by the

it power to designate an institution as a SIFI if it is "predominantly engaged in financial activities."[1395] The SIFI designation can be given to both bank financial institutions and non-bank institutions.[1396] Bank financial institutions are banks or bank holding companies.[1397] Non-bank SIFIs are institutions that hold the SIFI designation but are not chartered as banks or bank holding companies.[1398] Examples of non-banks include insurance agencies, such as Prudential and AIG.[1399] SIFIs are subject to higher scrutiny in terms of regulation and capital requirements.[1400] Such costs are naturally passed on to consumers, making the institution with the designation less competitive and burdening the consumer with greater costs.[1401]

Republicans, President Trump, and market participants have criticized the SIFI designation for a number of reasons, including its application to non-bank institutions.[1402] Critics claim the designation process employed by FSOC is unnecessary, in breach of due process norms, non-transparent, and misapplied to non-bank institutions.[1403] The Republican Staff of the Committee on Financial Services of the U.S. House of Representatives (the Committee) recently voiced its concern over the power wielded by FSOC over non-bank

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Secretary of the Treasury and is comprised of ten voting members and five non-voting members.").

1395 12 U.S.C § 5311 (2012) (explaining when a company is considered to be predominantly engaged in financial activities); § 5323(a)(1) (detailing FSOC's powers to designate an institution as SIFI).

1396 BARR ET AL., *supra* note 24, at 699.

1397 *Id.* at 701.

1398 *Id*. at 704.

1399 *See* U.S. DEP'T OF TREASURY, BASIS FOR THE FSOC'S FINAL DETERMINATION REGARDING PRUDENTIAL FINANCIAL, INC., (2013), https://www.treasury.gov/initiatives/fsoc/designations/Documents/Prudential%20Financial%20Inc.pdf [https://perma.cc/PF4E-3EP7]; BARR ET AL., *supra* note 24, at 705.

1400 Bob Ehrlich & J.C. Boggs, *The Next Repeal And Replace: Dodd-Frank*, FORBES (Jan 28, 2017), http://www.forbes.com/sites/realspin/2017/01/28/the-next-repeal-and-replace-dodd-frank/#4eed8e486978 [https://perma.cc/VH6W-AWXH].

1401 *Id.*

1402 *See* Roland Goss & Carlton Fields, *Dodd-Frank in a Trump Administration*, JD SUPRA (Jan 5, 2017), http://www.jdsupra.com/legalnews/dodd-frank-in-a-trump-administration-26348/ [https://perma.cc/KC2G-UJYG].

1403 *Id.*

institutions.[1404] It criticized the FSOC's designation process as arbitrary and inconsistent partly due to poor record management and internal guidance.[1405] In doing so, the Committee published clear examples of arbitrary considerations made by the FSOC in determining the SIFI designations for several non-bank institutions, pointing out discrepancies and vulnerabilities of the SIFI designation process.[1406] The Committee focused on FSOC's use of a purely subjective test in assessing non-bank institutions and their discrepancy in weighing the importance of collateral in its various evaluations of companies.[1407]

The application of the designation has even faced judicial scrutiny in *MetLife, Inc. v. Financial Stability Oversight Council.*[1408] In this case, insurance company MetLife, a non-bank institution, successfully challenged the SIFI designation it was assigned.[1409] The designation was struck down by the district court, with criticism levied by the court over the evaluation process used by the FSOC in allocating the designation.[1410] The court criticized FSOC's analysis in determining MetLife's SIFI designation as the FSOC failed to assess potential losses resulting from an institutional failure, determine which institutions should manage their finances, and consider the overall market impact.[1411]

Financial Choice 2.0 proposes a major change in the application of the SIFI designation to non-bank institutions.[1412] It would repeal the FSOC's power to designate any non-bank institution as a SIFI, including prior designations given to non-banks.[1413] It has also been

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[1404] COMM. ON FIN. SERV., U.S. HOUSE OF REPRESENTATIVES, 115[TH] CONG., THE ARBITRARY AND INCONSISTENT FSOC NONBANK DESIGNATION PROCESS, 1 (2017), https://financialservices.house.gov/uploadedfiles/2017-2-28_final_fsoc_report.pdf [https://perma.cc/66W6-34LN].
[1405] *See id.* at 5–10.
[1406] *See id.* at 11–36 (detailing examples of memorandums issued by FSOC that showed discrepancies in the manner of designating the SIFI status).
[1407] *Id.*
[1408] MetLife, Inc. v. Fin. Stability Oversight Council, 177 F.Supp.3d 219 (D.D.C. 2016).
[1409] *See* Goss & Fields, *supra* note 92.
[1410] *MetLife*, 177 F. Supp.3d at 237.
[1411] *Id.* ("FSOC never projected what the losses would be, which financial institutions would have to actively manage their balance sheets, or how the market would destabilize as a result.").
[1412] Financial Choice Act, H.R. 10, 115th Cong. (2017).
[1413] *Id.*

suggested that the current administration's approach to easing the application of the SIFI designation to non-bank institutions may be passive rather than impliemented via outright regulatory reform.[1414] Treasury Secretary Mnuchin is unlikely to support the designation of any new financial institutions as SIFIs during his term.[1415]

The Trump administration has recently issued a memorandum to suspend the designation of any new non-bank financial institutions as SIFIs for 180 days pending review on this power.[1416] While it is unclear whether the SIFI designation will be eliminated entirely by the Trump administration, it is likely that its application to non-bank institutions will be repealed given these criticisms and developments.[1417]

2. Implications of Reduced Oversight

There are numerous concerns that led to the creation of the SIFI designation, such as the bailout of AIG,[1418] and the belief that deregulation in this area will lead to another market failure.[1419] However, many commentators believe the SIFI designation for non-bank institutions is no longer necessary,[1420] and that the designation has led to reduced profitability for SIFI non-banks due immense regulatory scrutiny.[1421] As these institutions are regulated like banks,

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[1414] *See* Dalal, *supra* note 36.

[1415] *Id.*

[1416] *Trump suspends SIFI designations by FSOC pending review*, SEC. FIN. MONITOR (Apr. 25, 2017), http://finadium.com/trump-suspends-sifi-designations-by-fsoc-pending-review/ [https://perma.cc/858H-ABPD].

[1417] Pete Scroeder, *Trump orders review of financial rules to prevent future crises*, REUTERS (Apr. 21, 2017), http://www.reuters.com/article/us-usa-trump-regulation-idUSKBN17N248 [https://perma.cc/3BNG-X3MK].

[1418] AIG is an insurance company. *See generally* AIG, http://www.aig.com/ [https://perma.cc/H8DF-PKDH].

[1419] Schwartz, *supra* note 83, at 115 (arguing that deregulation is now problematic as unregulated financial institutions and markets have become increasingly interdependent, leading to greater systemic risk).

[1420] Kayla Tausch, *Insurance giants may no longer be 'too big to fail'*, CNBC (Feb. 10, 2017), http://www.cnbc.com/2017/02/09/insurance-giants-may-no-longer-be-too-big-to-fail.html [https://perma.cc/U6FC-Z4AY] (stating Rep. Jen Hensarling circulated a memo proposing certain insurance companies were no longer too big to fail).

[1421] *See* Valerie Young, *AIG Chief Promises Risk Is Lower Than Ever Despite Grim Quarter*, YAHOO FIN. (Feb 16, 2017), http://finance.yahoo.com/news/aig-chief-promises-risk-lower-204300597.html [https://perma.cc/7W3Qthey have an increased cost of regulatory compliance and face strict capital requirements.[1422] Despite their low-risk status, they are required to comply with the Dodd-Frank Act, reducing their profitability.[1423] Relaxing the application of the SIFI designation will give the institutions a chance to stimulate the economy and recover from their dismal financial results.[1424]

D. Conclusion

The Dodd-Frank Act has unmistakably shifted the dynamic of financial regulation in the United States.[1425] It was built as a result of the weaknesses exposed by the 2008 financial crisis, and represented the changing attitude towards consumer protection and conduct of market participants.[1426] The Act has been praised for steering the U.S. economy towards a stable recovery, and has been criticized for being overly broad and burdensome.[1427] The introduction of Financial Choice 2.0 implies support in the Republican-led Congress that the financial sector should be deregulated.[1428] The future of the Dodd-Frank Act is now in the hands of the Trump administration, which has signaled that the economy is moving into an era of significant deregulation.[1429] However, it is unlikely that key pillars of the Dodd-Frank Act will be wholly demolished, as they have become an integral component of the U.S. economy.[1430]

Nisha K. Sundra Rajoo[1431]

C5NT] (explaining it may be financially viable for AIG to downsize in order to escape the regulatory burden that comes with the SIFI designation).

1422 *Id.*

1423 *See* WORLD SCIENTIFIC, *supra* note 5, at 6.

1424 *See* Young, *supra* note 111 (stating that stock price of AIG increased in light of remarks about easing the SIFI designation for non-banks).

1425 *See* WORLD SCIENTIFIC, *supra* note 5, at 5.

1426 *Id*. at 113–123.

1427 *See id.* at 279.

1428 *See generally* Crowley et al., supra note 18.

1429 Lane, *supra* note 12.

1430 *See* Barr, *supra* note 9.

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