The Art of the Possible

Prospects for Financial Services Legislation in the 114th Congress

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It has been some time since we were last governed by a Republican-controlled Congress and a Democratic president. The last time was nearly fifteen years ago during the final six years of the Clinton Administration. Almost no one expects the next two years to yield the same legislative results as did that previous experiment in divided government. In fact, for a variety of reasons, not the least of which is the looming 2016 presidential election, it seems rather unlikely that the incoming 114th Congress will be as productive as any of those previous Congresses, measured in terms of enacted legislative output. Indeed, conventional wisdom (both inside and outside the Beltway, it would seem) holds that the next two years portend an extended and bitterly partisan political stalemate that will stymie any prospect for enactment of financial services legislation.

Call me a contrarian, but I take a different view. Despite the partisan politics that will inevitably animate both ends of Pennsylvania Avenue over the next two years, there will be opportunities in the new Congress to enact meaningful (albeit targeted and incremental) financial services legislation.

There are several potential procedural paths to enactment of such legislation. For example, there has been a lot of chatter in Washington recently about Congressional Republicans using the “budget reconciliation” process to circumvent Democratic-led filibusters in the Senate. There is also talk of attaching GOP legislative riders to appropriations bills and other “must-pass” legislation. But with Senate Republicans still short of a filibuster-proof majority and a Democratic president armed with a veto pen, the most likely avenue for enactment of financial services-related legislation in the new Congress will involve regular procedural order and bipartisan compromise. As discussed below, there are already a few legislative proposals percolating on Capitol Hill around which a bipartisan consensus seems to be emerging.

The new Congress is also likely to feature vigorous – and now bicameral – Congressional oversight of the Obama Administration and the financial regulatory agencies, which could be particularly impactful with respect to the ongoing regulatory implementation of the Dodd-Frank Act.

Even if this optimistic outlook on the prospects for legislative action turns out to be Pollyannaish, the results of this month’s mid-term elections are certain to alter the balance of power with respect to executive branch nominations.

Each of these topics is discussed in more detail below, with a focus on the possible legislative and oversight agendas of the key Congressional committees that exercise jurisdiction over the financial services industry.
Post-Election Landscape on Capitol Hill

The new GOP majority in the Senate and the newly-buttressed Republican majority in the House are now poised to pursue a single legislative agenda, one that will likely focus on “big ticket” issues like energy policy and perhaps corporate tax reform. But Congressional Republicans will also have the opportunity to do something that has been off-limits for the last several years: amend Dodd-Frank.

Since the enactment of the Dodd-Frank Act in 2010, the Obama Administration and its Democratic allies in the Senate have consistently and vigorously opposed legislation that would amend the Act. So resolute have Democrats been in defense of this position that some have described it as the political equivalent of the “11th Commandment: Thou Shalt Not Amend Dodd-Frank.”

More recently, however, Senate Democrats, together with all of their Republican colleagues, did vote to amend Dodd-Frank. That unanimous, bipartisan vote occurred on a bill relating to the treatment of certain insurance companies under the “Collins Amendment” to Dodd-Frank.¹ The House of Representatives subsequently approved a companion bill by a bipartisan majority.² With near unanimous support in both chambers, coupled with recent testimony by Federal Reserve Board Governor Dan Tarullo, who said enactment of this legislation “would be very welcome,”³ it appears likely to be fast-tracked and reach President Obama’s desk during the “lame duck” session of the current Congress. Although admittedly technical in nature and targeted in scope, enactment of this legislation could presage a willingness on the part of Senate Democrats to entertain other, targeted amendments to Dodd-Frank in the new Congress.

Senate Banking Committee

Senator Richard Shelby (R-AL), who previously led the Banking Committee from 2003 to 2007, is poised to resume the committee gavel for the remaining two years he is permitted to serve under the term limits imposed by Senate GOP rules. Under his leadership, the Committee will pursue a different set of legislative and oversight priorities than it did under the stewardship of outgoing Chairman Tim Johnson (D-SD), who has consistently supported the Obama Administration’s financial reform efforts and generally opposed amendments to Dodd-Frank (with the exception of the Collins Amendment legislation mentioned above).

Like his predecessor, Chairman Shelby’s agenda will include Dodd-Frank oversight, but led this time by a staunch opponent of that legislation, which he strongly

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denounced in the Banking Committee4 and against which he voted on final passage. Indeed, Senator Shelby has repeatedly expressed concerns with Dodd-Frank-mandated regulations that he considers to be imprudent or unduly burdensome, including the Volcker Rule.5 Nor is it likely that he will hesitate to criticize the Obama Administration and the financial regulators – in particular the Federal Reserve, of which he has been a frequent and outspoken critic.6

Senator Shelby has also been a strong proponent of requiring regulators to conduct cost-benefit analyses of new regulations. In 2011, he introduced legislation,7 co-sponsored by several Banking Committee Republicans, that would require regulators to conduct a “qualitative and quantitative assessment of all anticipated direct and indirect costs and benefits” of any proposed regulation, including compliance costs, effects on “job creation,” “regulatory administrative costs,” and any costs the regulation might impose on state and local governments. This emphasis on cost-benefit analysis is likely to be a signature aspect of his agenda as chairman.

Like his predecessor, Senator Shelby has consistently expressed concerns with the regulatory burden imposed on community banks and may, as he has in the past,8 seek to advance a package of “regulatory relief” measures intended primarily to benefit smaller banking organizations. At times, however, he has also been a harsh critic of the largest banks, perhaps most notably during the Dodd-Frank legislative debate when he voted for the Volcker Rule and cast one of only three Republican votes in favor of an amendment offered by Senators Kaufman (D-DE) and Brown (D-OH) that would have effectively broken up the largest banking organizations in the United States.9 Moreover, in 1999, he voted against the Gramm-Leach-Bliley Act, the legislation that partially repealed the Glass-Steagall Act’s separation of commercial and investment banking. He has also suggested, on more than one occasion, that capital standards should be higher for the largest banks.10

Congressional Republicans will also have the opportunity to do something that has been off-limits for the last several years: amend Dodd-Frank.


5 Hearing before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, 111th Congress – 2nd Session, Examining Recent Restrictions placed on Commercial Banks and Bank Holding Companies’ High-Risk Investment Activities (Feb. 2, 2010), available at http://www.gpo.gov/fdsys/pkg/CHRG-111shrg57709/html/CHRG-111shrg57709.htm. See Statement of Senator Richard Shelby: “...there does not seem to be evidence that . . . that proprietary trading created the losses that resulted in the rate need and race for bailouts.”

6 Brandon Moseley, Shelby Says that Federal Reserve has Engaged in “A Backdoor Stimulus Program through Monetary Policy,” Alabama Political Reporter (Jan. 9, 2014), available at http://alreporter.com/archives/2012-september/146-state/5581-shelby-says-that-federal-reserve-has-engaged-in-a-backdoor-stimulus-program-through-monetary-policy.html. “I have long been concerned that this aggressive and extraordinary purchasing program is artificially propping up home prices. This is especially pertinent since an over-heated housing market greatly contributed to the financial crisis that caused this situation in the first place.”


8 Id.


One issue on which Senators Shelby and Johnson strongly disagree is housing finance reform. Describing the issue as the Committee’s “top priority,”11 Chairman Johnson and Ranking Minority Member Mike Crapo (R-ID) brokered an agreement earlier this year with a bill that would have eliminated Fannie Mae and Freddie Mac and established a new housing finance regulator and backstop guarantor.12 Although approved by the committee with some Republican support, Senator Shelby voted against the measure, arguing that it would “complicate an already complex problem by expanding the role of the federal government in our private housing finance market and creating, yet again, another massive regulator.”13 In this regard, Senator Shelby’s position on the issue of housing finance reform is more aligned with that of current House Financial Services Committee Chairman Jeb Hensarling (R-TX).14 Given the continued divisiveness of this issue in Congress, the ongoing recovery of the housing markets in the U.S., and the very limited window of opportunity to develop, debate, and pass major legislation in advance of the 2016 presidential and Congressional elections, passage of comprehensive housing finance reform legislation does not appear to be in the cards in the 114th Congress.

Even if Senate Republicans maintain their majority after the 2016 elections, as noted above, Senator Shelby can only serve as chairman of the Banking Committee for two more years, which leaves precious little time to see new legislation through to enactment, especially against the backdrop of divided government. Accordingly, Chairman Shelby will likely be inclined to prioritize regulatory burden relief for smaller banks, although as discussed below, such legislation could potentially include some targeted relief for the larger banks.

**House Financial Services Committee**

With Republicans still in firm control of the House of Representatives and leadership of the House Financial Services Committee expected to remain largely intact, the financial services agenda on the House side of the Capitol is likely to resemble in many respects the agenda Chairman Hensarling has pursued in his committee over the last two years. In stark contrast to the Senate, the House has passed literally dozens of bills over the last four years that would amend Dodd-Frank, with the Financial Services Committee approving more than 30 such bills in the 113th Congress alone, none of which has advanced in the Senate. Obviously, it should be easier for Chairman Hensarling to get the Senate Banking Committee’s attention beginning next year.

The Financial Services Committee has also conducted numerous Dodd-Frank oversight hearings in the 113th Congress, during which the panel’s Republican members have been harshly critical of the Obama Administration, the federal banking agencies, and the Financial Stability Oversight Council (FSOC), scrutiny that will only intensify now that the GOP is the majority party on both sides of the Capitol. The harshest of this bicameral scrutiny is likely to be reserved for the Consumer Financial Protection Bureau (CFPB), an agency Senator Shelby has described as the “most powerful yet unaccountable bureaucracy in the federal government”15 and Chairman Hensarling has characterized as the “single most unaccountable agency in the history of America.”16 Accordingly, Congressional Republicans will

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almost certainly direct at least one legislative broadside at the governance, funding, and operation of the CFPB. That sort of legislation is very unlikely to make it through to enactment, however.

In addition to viewing the Dodd-Frank Act as a hindrance to economic growth, House Republicans generally remain skeptical that the law has achieved (or will ever achieve) its stated objectives of ensuring financial stability and ending “too-big-to-fail.” The latter concern has been a particular focus of committee activity under Chairman Hensarling. On the four-year anniversary of the Act’s enactment, committee Republicans issued a staff report concluding that “not only did the Dodd-Frank Act not end ‘too-big-to-fail,’ it had the opposite effect of further entrenching it as official government policy.” In particular, the report’s authors cast doubt on the credibility of the resolution plans (or “living wills”) mandated under Dodd-Frank and allege that, rather than ending “too-big-to-fail” (TBTF) the Orderly Liquidation Authority (OLA), codified in Title II of Dodd-Frank, has become a “fixture in the regulators’ toolkit, . . . subverting market discipline and making future bail-outs more (not less) likely.”

Chairman Hensarling has pledged to pursue a package of TBTF-related provisions, potentially including the repeal of the OLA, various FSOC-related measures, and additional limits on the Federal Reserve’s “lender of last resort” authority. The proposed repeal of the OLA could conceivably be joined with a broader proposal, now pending in the House Judiciary Committee, to modify the Bankruptcy Code to facilitate the orderly resolution of large financial institutions.

**Financial Services Legislation That Could Advance in the New Congress**

So exactly what kind of targeted banking legislation might advance in the new Congress? The leading contenders for now appear to be proposals to modify the current statutory threshold of $50 billion in total assets at which bank holding companies become subject to “enhanced prudential standards” (regarding capital, liquidity, risk-management) and regulation as “systemically-important financial institutions” (SIFIs). Proposals to raise or otherwise modify the SIFI asset threshold have already been endorsed on a bipartisan basis in the House and appear to be gaining support in the Senate. Senior regulators have also expressed support for revisiting the SIFI threshold. Most notably, Governor Dan Tarullo has proposed raising the threshold to $100 billion, arguing that mandatory resolution planning,

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18 Id., at 59-60.
19 Jeb Hensarling, Chairman, House Financial Services Committee, Dodd-Frank Results in Less Freedom, Less Opportunity and a Less Dynamic Economy, Remarks at a Mercatus Center-CATO Institute Conference (July 16, 2014), available at http://financialservices.house.gov/news/documentsingle.aspx?DocumentID=388236. “Our Committee will also soon take legislative action to end Dodd-Frank’s bailout fund and bring to an end the reign of those that are to Too Big to Fail.”
20 Dodd-Frank Act § 165(a)(1)
stress-testing and other regulations “do not seem . . . to be necessary” for banks with between $50 billion and $100 billion in total assets.22 Similarly, Comptroller of the Currency Tom Curry has questioned the utility of the $50 billion “bright line,” and has suggested that a more sensible approach would be to “use an asset figure as a first screen and give discretion to the supervisors based on the risks in their business plan and operations.”23 Even former Rep. Barney Frank recently endorsed the concept in testimony before the committee he previously chaired.24

Modifying the SIFI size threshold has recently been the focus of a legislative effort in the House Financial Services Committee, where two leading proposals have been considered. The first, a bill sponsored by Rep. Blaine Luetkemeyer (R-MO)25 and co-sponsored by 77 others (58 Republicans and 19 Democrats), would eliminate the automatic asset threshold altogether and instead require the FSOC to apply an “indicator-based measurement approach,” which considers several factors in addition to size, to assess systemic importance. A second bill,26 authored by Rep. Joyce Beatty (D-OH) and co-sponsored by Rep. Steve Stivers (R-OH), would direct the FSOC to review banks with total assets of between $50 billion and $250 billion in order to determine whether to subject these firms to enhanced prudential standards and supervision, and expresses the “sense of Congress that consolidated asset size remains a factor, but only one of many factors, that should be considered in determining systemic risk.”27 Although these legislative proposals did not make it out of committee during this Congress, they seem to underscore a growing, bipartisan consensus that Congress should revisit the SIFI threshold.

While no comparable legislation has advanced to date in the Senate, the idea of raising the SIFI threshold has begun to garner some interest on both sides of the aisle. Notably, Sen. Sherrod Brown (D-OH), who could serve as the Ranking Minority Member on the Banking Committee next year, has criticized the $50 billion asset threshold as an approach that treats regional banks operating under a “traditional banking model” whose failure would not “threaten the U.S. or global financial system” the same as larger, more complex institutions.28 In addition, he has underscored the need for regulators to examine the systemic risk posed by banks’ size, leverage, and business model on a case-by-case basis and to “strike the right balance between identifying institutions and activities that present the most risk.”29

With lawmakers and regulators alike now acknowledging that the contours of the SIFI universe, as defined in Dodd-Frank, are overly broad, it may be possible for legislation amending the SIFI threshold to advance in the new Congress, to serve as a vehicle for advancing targeted relief for smaller banks, and potentially to include additional provisions that could provide some limited relief for larger banks (e.g., with respect to the Dodd-Frank derivatives “push-out” requirement). It is also possible that various “FSOC reform” proposals could find their way into such a legislative package.

One possible starting point for a bipartisan discussion in the Senate regarding possible amendments to Dodd-Frank might be legislation Senator Shelby introduced in early 2013 consisting exclusively of purely technical

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25 H.R. 4060.
26 H.R. 4532.
27 Id., at 12.
29 Id.
corrections to Dodd-Frank (e.g., statutory typos, imprecise cross-references, etc.).

Governor Tarullo has proposed tailoring existing and forthcoming regulatory requirements according to banks’ size, scope, and range of activities, noting that certain existing regulatory requirements may be “disproportionately costly for community banks.” He has also suggested that it may be “worthwhile to have a policy discussion of statutes that might be amended explicitly to exclude community banks” with less than $10 billion in total assets, particularly citing the Volcker Rule and the incentive compensation requirements imposed under Sec. 956 of the Dodd-Frank Act. Both of these suggestions could also find their way into new legislation.

Finally, there is a substantial risk that financial services legislation – in particular, punitive measures targeting the largest banks – could advance in the Senate outside of the committee process, especially if incoming Majority Leader Mitch McConnell (R-KY) follows through on his pledge to provide for a “free and open amendment process” on the Senate floor.

The Congressional Bully Pulpit

Even if a two-year legislative stalemate ensues, the new Republican-controlled Congress will nonetheless have a significant impact on financial services regulation and policy through use of the “bully pulpit” that Congressional oversight confers. This can be an especially influential platform when the same party controls both chambers of Congress and could be particularly significant with respect to the regulatory agencies’ ongoing implementation of Dodd-Frank.

For example, the House has passed legislation addressing the treatment of certain collateralized loan obligations (CLOs) on three different occasions, once on a stand-alone basis and twice coupled with separate policy proposals, clarifying that the Volcker Rule does not require banking organizations to divest, prior to July 21, 2017, CLO debt securities issued before Jan. 31, 2014. In what may constitute the nascent stage of another bipartisan Volcker Rule-related initiative on Capitol Hill, three Democrats on the House Financial Services Committee – Gary Peters (MI), John Carney, Jr. (DE), and Dennis Heck (WA) – recently sent a letter urging the Federal Reserve to “streamline the process” for banking entities to avail themselves of the seven-year conformance period for certain investments in legacy venture capital and private equity funds. As the July 21, 2015 expiration of the existing conformance period approaches, the new Congress is likely to be

31 Tarullo, at 13.
32 Id., at 11.

active on Volcker Rule-related issues both in an oversight capacity and potentially through new legislation.

**Executive Branch Nominations**

Finally, the Senate’s new Republican majority is sure to have a significant impact on both pending and forthcoming executive branch nominations, with President Obama’s nominees likely to face even greater scrutiny. As a result of Senate Majority Leader Harry Reid’s (D-NV) invocation of the so-called “nuclear option” in November 2013, only a simple majority, rather than a filibuster-proof 60-vote super majority, is now needed to confirm most executive branch nominations, a rule change the incoming GOP majority seems unlikely to revisit (although they decried the change at the time). This new dynamic is likely to be on display early in the new Congress, when the Senate will consider the president’s nominees to fill several significant positions at the Treasury Department and on the Federal Reserve Board.

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**Conclusion**

The next two years in Washington are certain to be replete with partisan skirmishing – no doubt about that. And chances are that, before the 114th Congress has adjourned, President Obama will have used his veto pen on more than one occasion. Yet, a complete and utter government stalemate is not in anyone’s enlightened self-interest – neither that of the country as a whole, nor that of a president contemplating his second-term legacy, nor that of the incoming Republican majority on Capitol Hill. House Majority Leader Kevin McCarthy (R-CA) was recently quoted in the press as saying “I do know this ... If we don’t capture the House stronger, and the Senate, and prove we can govern, there won’t be a Republican president in 2016.”

Similarly, on election night, Senator Mitch McConnell struck a similar tone, arguing that Republicans and Democrats “have an obligation to work together on issues where we can agree.”

Clearly, Democrats and Republicans will seek to distinguish themselves and their political philosophies and agendas in advance of the 2016 elections, and some of that will likely spill over into financial services legislation. But there will also be opportunities for targeted, incremental financial services legislation to advance in the next Congress, especially if lawmakers from both parties begin to coalesce around targeted fixes, such as those described above.

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