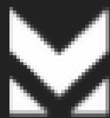

What Would Dismantling Dodd-Frank Look Like?

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Calls to dismantle Dodd-Frank, the post-crisis Wall Street overhaul that requires banks to cushion themselves against collapse and aims to prevent "too-big-to-fail" institutions from sinking the economy, have been a battle cry for Republicans in Congress and on the campaign trail.

But taking the financial law apart could be a complex process.

The regulatory unfolding of the law, enacted in 2010, has been in the works for six years. About 70 percent of the law's prescribed rules were finalized as of July 2016, according to an analysis by law firm Davis Polk.

In those six years, Dodd-Frank has been condemned by its detractors as a stranglehold on the U.S. economy. Industry critics range from large Wall Street firms to small banks to business groups. Still, analysts say breaking down the regulatory behemoth could be as ponderous, and as lengthy, as the process of putting it in place.

Despite a steady barrage of political rhetoric lobbed at the law, it's difficult to imagine a congressional repeal, said Lawrence Baxter, a professor and financial regulation expert at Duke University School of Law, in an interview. Even if that happened, the next step would involve a complex rulemaking process that consists of hurdles similar to the ones required for putting the current regulations in place, he said.

"Assuming that took place, which is hard to imagine, then there would be notice and comment rulemaking that would be at least as difficult as it has been to implement," Baxter said. "It's a very slow, time-consuming process."

The dismantling process could take many forms, financial regulation experts say. Adding a replacement to the financial law, which many view as a necessity if there is a repeal, only adds to the complexity.

House Financial Services Committee Chairman Jeb Hensarling (R-Texas) has put forward a replacement plan, the Financial CHOICE Act. It would strip the Financial Stability Oversight Council of its authority to designate firms as too big to fail, overhaul the Consumer Financial

Protection Bureau, and offer financial institutions an “off-ramp” from some regulatory requirements if they maintain certain capital levels.

Meanwhile, the easiest step of peeling away Dodd-Frank’s layers would be to target the rules that haven’t yet been proposed or finalized, said Amit Narang, regulatory policy advocate at the left-leaning advocacy group Public Citizen, in an interview. Rules that are finalized in the “midnight” regulatory period — President Obama’s final months in office — could potentially be overturned by a Congressional Review Act vote, he said. (That vote would not require a 60-vote threshold in the Senate, meaning the majority party could push it through even if there is opposition in the minority.)

Questions also remain about what the deregulation process would look like if GOP nominee Donald Trump, who has called for a temporary freeze on new federal regulations, takes office. Trump’s administration, through agency heads, could halt some Dodd-Frank rules that have been proposed but not yet finalized, Narang said.

Then comes the hard part. Breaking down Dodd-Frank’s foundation — the rules that are solidly on the books — would be much more complicated, requiring lawmakers to push the regulations through the notice and comment process, Narang said.

“In order to get rid of the rule itself, they will have to go through a notice and comment rulemaking process,” he said. “If they don’t go through a notice and rulemaking comment process, and they just somehow short-circuit it or something like that, they’re going to have some legal issues at the back end.”

A Trump administration could simply refuse to enforce Dodd-Frank regulations, Narang said, creating a “policy of non-enforcement.”

“That is where Trump and his agency heads could weaken the impact of Dodd-Frank regs. They have the discretion not to enforce regulations on the books,” he said.

But a lack of public enforcement wouldn’t make the rules disappear. Investors could still bring civil lawsuits pointing to Dodd-Frank regulatory requirements as evidence. “There’s no way to get them off the books unless you go through a notice and comment rulemaking process to modify or repeal those Dodd-Frank rules,” he said.

Using non-enforcement to muffle Dodd-Frank would require coordination between many moving parts, Baxter concurred. The president would have to wrangle the independent regulators — i.e., by appointing new agency heads and in some cases replacing and restructuring entire boards — and deal with potential pushback from Congress and the banks themselves.

“It would be very analogous to saying, ‘What if a sheriff got elected and told his police not to enforce the law?'” he said. “It wouldn’t be as dramatic as one might expect, because banks don’t want to commit suicide financially, so they’re not going to do very stupid things.”

In the event of a big bank collapse, a lack of Dodd-Frank enforcement could backfire on a large scale, he said. “It would become an extremely politically controversial issue and would certainly explode if a big bank were to get in serious trouble and go, cap in hand, looking for taxpayer support.”

Banks have already devoted significant sums to regulatory compliance, he added, and a public lack of enforcement could lure shady banking practices over U.S. borders. “Countries that have done that have become offshore financial centers for banks that don’t actually want to be seen doing what they’re doing,” he said. “I’m not sure the U.S. wants to end up that way.”

Narang estimated that a deregulation of Dodd-Frank could take from two to four years, the extent of the next presidential term. “In theory, it should take as long as regulating in the first instance,” Narang said. “The way that it actually works in practice is, political will matters. The orientation of the administration matters.”

Public Citizen released a report in June showing that economically significant federal rules completed in 2016 up to that time have taken an average of 3.8 years to finish, about the length of a presidential term. But when it comes to Dodd-Frank, Narang noted that Congress could speed up the repeal process through interim final rules, or it could supersede Dodd-Frank with a legislative package like the Hensarling plan.

One historical precedent for financial deregulation is the repeal of the Glass-Steagall Act, a 1933 regulation that placed a strict division between commercial and investment banking. Deregulatory rumblings for Glass-Steagall were stirring as early as 1980 with the enactment of the Depository Institutions Deregulation and Monetary Control Act. The takedown of Glass-Steagall got serious in 1996 when the Federal Reserve under Chairman Alan Greenspan reinterpreted the law several times, eventually allowing bank holding companies to derive up to 25 percent of their revenues from investment banking. Glass-Steagall was finally dead in 1999 with the Gramm-Leach-Bliley Act.

Republicans, however, have rebutted the idea that dismantling Dodd-Frank would prove as complex as the law itself.

“This criticism is amusingly hypocritical coming from supporters of Dodd-Frank, which is so complicated that its regulations are still being drafted six years after it became law,” said Jeff Emerson, a spokesman for Hensarling, in an email to Morning Consult.

“Democrats claimed Dodd-Frank was narrowly targeted at Wall Street’s ‘too big to fail’ banks. But by layering mind-numbing amounts of complexity onto an already labyrinthine regulatory edifice, Dodd-Frank played into the hands of the largest banks at the expense of American households and small- and medium-sized community financial institutions.”

Emerson, citing a July 2015 study by the Mercatus Center at George Mason University that referred to Dodd-Frank as perhaps “the biggest law ever,” said replacing Dodd-Frank with Hensarling’s plan would be a simpler process than implementing it.

Mark Calabria, director of financial regulation studies at the libertarian-leaning Cato Institute, disputed the notion that a straight Dodd-Frank repeal would need a notice and comment process. “Notice and comment periods for rulemakings are only required when they’re statutorily directed,” he said in an interview. “If Congress says tomorrow that X law goes away, then any regulations that have been issued pursuant to X law go away.”

Lawmakers should repeal and replace Dodd-Frank, not just scrap it wholesale with no framework to take its place, Calabria said. “We should repeal and replace, not just repeal,” he said. “We don’t want to go back to 2008.”

And Dodd-Frank isn’t the only regulatory measure with a strong impact on banks, he said.

“There have been a number of things that have run parallel to Dodd-Frank that have been mixed together,” he said. “The most important of that has been the whole Basel capital process.”

Calabria also said that Hensarling’s replacement proposal, as opposed to a simple congressional repeal of Dodd-Frank, would require some new rulemaking that would take some time. “Would it require 400-some rules like is required in Dodd-Frank?” he said. “No, probably more like a dozen or so rulemakings.”

As for the GOP presidential nominee’s call for a regulatory halt, Calabria said it is more of a signaling tactic than a practical proposal. “Most of the financial regulators are independent,” he said. “You couldn’t just issue an executive order saying all financial regulators would stop.”

Baxter said Dodd-Frank should be fixed in some areas, but a blanket approach to deregulation is not appropriate.“I think tweaks are necessary, and maybe even some significant reform in certain areas, but the whole lock, stock and barrel approach of, ‘We’re going to just deregulate,’ is just mindless.”