Forbes

# The Senate Punts on Financial Reform

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October 4, 2017

Hopes for real financial regulation reform in 2017 pretty much evaporated this week as the Senate decided to focus solely on tax reform. Given the importance of a policy victory, especially in the wake of the Obamacare repeal fiasco, the singular focus on tax reform makes perfect sense.

Throwing something as controversial as repealing parts of Dodd-Frank into the reconciliation process could sink tax reform, and losing that battle is simply not an option right now.

Still, it is hard to imagine that if the roles were reversed, liberals would give up so easily.

Would they start down the road to victory, only to retreat before even extracting any sort of success or making a strong statement? (Earlier drafts of the budget resolution included the necessary instructions for the Banking Committee to find savings; they've disappeared from the resolution.)

Would they fracture or stay unified? Would they hesitate to use the Congressional Review Act to stop the Consumer Financial Protection Board's arbitration rule?

Regardless, Americans lose because conservatives are not unified in rolling back the Dodd-Frank Act. Given the circumstances, that's rather bizarre.

Dodd-Frank became law during the Obama presidency, when Nancy Pelosi (D-Calif.) led the House of Representatives and Harry Reid (D-Nev.) presided over a *near* filibuster-proof Senate majority. It was a partisan bill that garnered no Republican votes in the House and just three in the Senate.

It was largely a progressive wish-list of policies that failed to fix what caused the financial crisis. Based on the demonstrably false notion that deregulation caused the financial crisis, it wound up enshrining "too-big-to-fail" into law.

Dodd-Frank provided more than one lifeline to largefailing financial firms and created possibly the most politically charged so-called independent regulatory agency that financial markets have ever known.

The 800-plus page boondoggle expanded the failed regulatory approach that helped create the crisis, and it further relied on the federal government to plan, protect, and prop up the financial system.

The U.S. House has already passed a bill that would fix many of these problems and implement many other sensible reform ideas to strengthen financial markets. The Trump administration has voiced strong support for this approach, and practically begged the Senate for companion reforms.

At least one recent survey suggests a majority of Americans would be on board. Conducted by the Cato Institute in collaboration with YouGov, the survey found the following:

- 65% of Americans oppose too-big-to-fail policies (57% of Democrats and 72% of Republicans), saying "Any bank or financial institution should be allowed to fail."
- Nearly three-fourths (72%) of Americans don't believe that the financial regulations passed since the 2008 financial crisis will make future crises less likely.
- Only about one quarter (26%) believe these regulations will make future financial downturns less likely.
- 60% believe that banks would make better financial decisions if they were convinced the government would let them go out of business.
- Clinton voters are about twice as likely (41%) as Trump voters (20%) to believe some banks are too integral to the U.S. economy to fail.
- Despite distrust of "Wall Street," Americans like their own banks and financial institutions.

The survey also uncovered partisan divisions. For example, most (56%) Democrats believe lenders charge some people higher interest rates because they are predatory and take advantage of the vulnerable. In contrast, two-thirds (67%) of Republicans believe banks need to do this to compensate themselves for some borrowers' greater credit risk.

In another partisan divide, large majorities of Republicans (73%) and independents (69%) don't think government should restrict people's financial choices to protect them, while 57% of Democrats felt that way.

The survey yielded many other interesting results, but the big takeaway is simply this: Americans are not as tied to the Dodd-Frank bill as the Senate appears to think they are.

Nonetheless, Americans will have to wait for reforms. Specifically, they will have to wait on Senate Majority Leader Mitch McConnell (R-Ky.) and Senate Banking Chairman Mike Crapo (R-Idaho), to move on reforms that will strengthen financial markets, end bailouts, and protect taxpayers.

It is possible that the Senate will craft some sort of bipartisan financial reform bill this year. But liberals are unified in their commitment to protect Dodd-Frank from any real changes, so any bipartisan reforms would be merely symbolic.

Raising the so-called SIFI threshold (the size at which bank holding companies are subject to enhanced regulation) from $50 billion to $250 billion is one example of a symbolic reform. Another is the recently introduced bill to "give the Federal Reserve flexibility in designating banks as systemically important."

These changes leave in the place the misguided – and dangerous – notion that federal bureaucrats can apply the right set of regulations to the right set of large financial companies, thus ending financial disasters.

They completely ignore that meeting arbitrary capital and liquidity standards do little more than provide a false sense of security. In reality, even companies that meet the rules fail. (Maybe it's because they're more concerned with meeting the rules than anything else?)

They also ignore that two of the worst financial crises in the history of the U.S. dealt primarily with highly regulated *small* banks.

Many provisions in the CHOICE Act would do a better job of strengthening financial markets. Take the "regulatory off-ramp," an incredibly simple yet powerful idea also known as a capital election. It provides that, if a bank chooses to improve its ability to absorb losses, it earns regulatory relief.

There is, after all, little reason to heavily regulate banks that can absorb their own financial risks. This type of provision could ultimately be expanded to provide even more regulatory relief and build even stronger markets.

Real reforms, such as those in the CHOICE Act, would undo the most harmful parts of Dodd-Frank. In particular, they would:

- Eliminate the ability of the Financial Stability Oversight Council to identify firms that regulators believe are too big to fail.

- Eliminate the same problem with respect to Financial Market Utilities.

- Eliminate Dodd-Frank's Orderly Liquidation Authority, a new avenue for federal bailouts that allows federal regulators to seize troubled financial firms—with minimal judicial review—and close down their affairs.

- Rein in the unparalleled rulemaking, supervisory, and enforcement powers of the Consumer Financial Protection Bureau.

- Repeal the Volcker Rule, the incredibly wasteful and misguided provision that ignores the fact that banks make risky investments every time they make a loan.

Americans understand that the Dodd-Frank Act will not make them safer. They also understand how important it is to reform the tax code, so they'll likely wait for the Senate to fix the problem. But they won't wait forever.