Obama Reg Reform Plan is Victim of Distraction

Bill details show first hurdle for Tier I firms is just $10B assets

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July 23, 2009

Just more than a month after President Obama unveiled it, an ambitious plan to reform the regulation of the financial system is being eviscerated.

Key elements including handing the Federal Reserve Board power to monitor systemic risks and eliminating thrift and other specialty charters, appear dead. Legislating the authority to unwind troubled nonbanks — once a top priority — has fallen by the wayside. And House Financial Services Committee Chairman Barney Frank acknowledged Wednesday that bankers had made significant progress in lobbying against a centerpiece of the effort, a new consumer protection agency.

Critics and proponents alike agreed the problem is that the administration and lawmakers are simply trying to accomplish too much at the same time. Most noted that President Obama and Senate Banking Committee Chairman Chris Dodd are more focused on health-care reform.

"The administration is trying to do too much," said Paul Miller, an analyst with Friedman, Billings, Ramsey. "They are trying to revamp health care, energy and financials all in one year. … Obama's plate is very big and the political process is not made to move that fast."

After moving Tuesday to delay on a vote on consumer protection, Frank on Wednesday held a press conference and vowed to work on building support for the legislation over the August recess. "Of all of the changes that I think we need, the high priority is creating this agency," he said.

Frank said he was "surprised" by the strength of industry opposition, calling it disappointing, but said he is confident lawmakers' constituents will weigh in to support a new agency.

"I accept the fact that they want to have a big national debate over this, so that's what we are going to have," he said. "I welcome a national debate. Frankly, if I were the bankers, I would not invite a debate over whether or not I'd been all that great in the consumer area and whether or not people should just suffer, but if that's what they want, I think this is what we will have."

While Frank is side by side with the administration with regard to the consumer protection agency, he has raised concerns with other parts of the regulatory reform plan. He has flatly rejected calls to eliminate the thrift charter, and earlier this week objected to identifying the most systemically risky firms as Tier 1 financial holding companies.

Under legislative language released Wednesday, the Obama administration defined a Tier 1 financial holding company for the first time and the threshold is lower than expected.

The bill would give the Fed the power to seek information from any firm that has more than $10 billion in assets, $100 billion or more of assets under management or $2 billion or more in gross annual revenue.

That data would be the basis for the Fed decision on whether a firm should be slotted into the Tier 1 designation.

Frank appeared to agree with critics that publicly naming such firms would only exacerbate the problem of too big to fail. "I'm going to suggest that they substitute a different model," he said during a hearing on financial companies deemed too big to fail. "With regard to identifying the companies that might be particularly systemic risk, the administration is going to have to adopt the approach applied to deal with pornography. They are going to be able to know it when they see it, but they are not going to have a pre-existing list. I think that idea is pretty much gone."

Frank said he favored a system of gradually increased capital requirements instead. "The bigger you are and as you get bigger your capital requirements go up. Not just proportionately but disproportionately," he said.

But which regulators will supervise large, systemically important firms remains up for grabs. Though Obama and Treasury Secretary Tim Geithner have insisted it be the Fed, lawmakers continue to resist that approach — and the administration has been able to do little about it.

At a hearing with Fed Chairman Ben Bernanke on Wednesday, Senate Banking Committee members reiterated their support for a strong systemic risk council, instead of the Fed, which would oversee exceptionally large bank and nonbank firms.

Observers said that five weeks after the plan was announced, there remains very little political support to give such power to the Fed.

"I don't know anyone besides Obama and Geithner who thinks the Fed is going to get all this new power," said Mark Calabria, director of financial regulation studies at the Cato Institute. "I don't want to go as far as to say the battle's been fought and lost, but it's come pretty close to it."

A plan to give the government resolution powers, meanwhile, appears to have vanished. Just a few months ago, Obama made the issue a top priority, saying Congress should separately pass a bill to give the Federal Deposit Insurance Corp. and the Treasury power to resolve systemically important firms.

But the plan was too linked to systemic risk oversight, and lawmakers balked at moving pieces of legislation separately. As a result, the issue has almost completely disappeared for now.

While none of these issues was expected to be a slam dunk, the speed at which the administration's plan is crumbling is still surprising.

Even banking lobbyists had assumed that Frank would be able to quickly pass a consumer protection agency bill, holding out hope they could change it before it went to the full floor and the Senate. But by scrapping a planned committee vote for next week, most observers saw that as a sign that the industry had been even more successful than they expected.

While Frank cast the delay as a chance for consumer groups and other supporters of the bill to regain momentum, many said the longer the legislation sits, the more chance lobbyists will have to pick it apart.

"They are getting a lot of push back," said Bert Ely, an independent analyst in Alexandria, Va. "They are kind of having to regroup. The expectation or the hope is that support will build for this stuff over the August recess, but I'm skeptical. The more people study these bills, the more reservations seem to develop about them. … They are not going to be able to jam this stuff through as fast as they had hoped."

Though the administration released detailed legislative language on other parts of regulatory reform on Wednesday, observers said momentum for the plan would continue to slip as long as the administration is distracted.

"They are pushing too many things too fast," Ely said. "They had to do a lot of arm-twisting on the climate change bill and Democrats are having problems with health care. … Financial services regulatory reform is very much of a second-tier issue compared with those other two."