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The end of Dodd-Frank?

Tweaks to onerous banking regulations are more likely

By Mark Calabria
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The results of the midterm elections, with Republicans increasing their House majority and capturing the Senate, seem like a repudiation of President Obama's policies. After health care, the administration commonly lists financial reform, the Dodd-Frank Act, as one of its signature achievements. Do the election results signal the end of Dodd-Frank?

It's worth noting that the coming Republican majorities in both houses and their committee leadership voted against Dodd-Frank. In the House, current Financial Services Committee Chairman Jeb Hensarling retains his leadership position, while in the Senate, my former employer, Sen. Richard C. Shelby, retakes his seat as chairman of the Banking, Housing and Urban Affairs Committee. Both have previously introduced measures to repeal Dodd-Frank and were leaders against its passage. It's fair to say Dodd-Frank will not have any friends among the leadership of both the House and Senate majorities.

Mr. Shelby and Mr. Hensarling are also vocal opponents of bailouts. For Mr. Shelby it goes back to at least his 1979 vote (then as a House Democrat) against the first Chrysler bailout. Both were also leaders in their respective houses against the Troubled Asset Relief Program. Mr. Shelby famously walked out of a Bush White House meeting to denounce the plan in front of the press.

While these two are no fans of Dodd-Frank, nor are they protectors of Wall Street. They share that Southern populist suspicion of both big finance and big government. Mr. Shelby went so far as voting for the Brown-Kaufman amendment to break up the banks, offered during Senate consideration of Dodd-Frank. Mr. Shelby was also one of the few Republicans to vote against Gramm-Leach-Bliley, which formally ended the separation of investment and commercial banking. My own experience interacting with Mr. Shelby and Mr. Hensarling is that you would be hard-pressed to find two members more opposed to the privatization of profits and socialization of losses that so characterizes our financial system.

Still, does any of this really spell the end of Dodd-Frank? Not likely. Most difficult of all for both Mr. Shelby and Mr. Hensarling is that many within their own caucuses, while opposing

Dodd-Frank and happy to make marginal changes, are increasingly comfortable with the Wall Street view that it is simply time to move beyond additional changes to our financial system. Dodd-Frank is widely viewed on Wall Street as the "devil you know," and while costly, is ultimately manageable. Of course, some of the worst elements of Dodd-Frank, such as the Consumer Financial Protection Bureau, do not even cover Wall Street.

It is also important to recall that a simple majority does not constitute "control" in the Senate. For Mr. Shelby, the critical number will be 60, not 51. Often the number will actually be 100, as Sen. Mitch McConnell is unlikely to devote much floor time to financial issues. While this will be a missed opportunity for Republicans to prove themselves opposed to bailouts, Mr. McConnell won't want to remind voters of his role - or that of Republicans in general - in creating the bailouts.

What does favor Republicans is that about half of the almost 400 regulations required under Dodd-Frank have yet to be written. Many of those that are written, such as the Volcker rule, are written in such a vague, discretionary manner that what really matters will be enforcement. My experience as a former Senate banking committee staffer, is that regulators, especially the so-called "independent" kind, care what their congressional oversight committees think. So while I do not see regulators suddenly changing course, I do expect a slight bending toward the positions favored by Mr. Shelby and Mr. Hensarling.

What these will be, however, can be surprising. For instance, before the financial crisis, Mr. Shelby fought against the Federal Reserve's efforts to reduce bank capital under the Basel Accords. This, fortunately, meant that Basel II was never implemented in the United States. Clearer and higher capital has long been a Shelby mantra. In some areas, regulation will actually be tougher; in others, it will soften.

While full repeal of Dodd-Frank is unlikely, a number of modest changes are possible. Senate Democrats generally bottled up even bipartisan proposals to modify Dodd-Frank. Some, such as directing the Federal Reserve to treat banks and insurance companies differently for capital purposes, actually passed the Senate and are again likely to move. Others, such as clarifying the process for deciding who exactly is "systemically important," also enjoy bipartisan support. More partisan issues, such as bringing the Consumer Financial Protection Bureau on-budget (like most other agencies) may be possible via the appropriations process. Other tweaks are quite likely, but again, they will be tweaks.

It's been said that "timing is everything." The next Congress will bring to the leadership of the House Financial Services and Senate banking panels two members devoted to ending bailouts and bringing market discipline to our financial markets. Unfortunately, such grand changes are rarely possible outside of a financial crisis. For the sake of our economy, let's hope the next

Congress offers that rare exception.

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