

Alert 10-113

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## Global Regulatory Enforcement Alert

### Seeking Balance: Banking and Financial Regulatory Reform Legislation

Summary: On May 20, the Senate passed S. 3217, the Restoring American Financial Stability Act of 2010, more commonly known as the banking or financial regulatory reform legislation. Most of the four weeks of debate on this legislation was spent working through a list of amendments affecting such areas as proprietary trading by banks; greater consumer protection; and the trading of over-the-counter derivatives, among others. We note, however, that the Senate's actions are not the final word on any of these areas: a number of issues remain unresolved and need to be addressed when the Senate attempts to reconcile its version of this legislation with a differing version, passed earlier by the House of Representatives. As a result, the opportunity remains to direct the impact of this legislation before it reaches the president's desk, which is expected. Beyond that, opportunities will arise to impact final program direction through future rulemaking.

Reed Smith's Public Policy & Infrastructure Practice has been monitoring deliberations on financial reform legislation in the House and Senate since the beginning of the 111th Congress. We have represented clients before congressional committees involved in drafting this legislation, and have developed relationships with a number of Members and staff on those committees, all of whom will be involved in drafting efforts on any House-Senate conference report, along with monitoring implementation by the Executive Branch of a final law. We are available to discuss how to develop an immediate lobbying strategy, as well as a longer-term effort that works with both Congress and the Obama administration.

The Senate passed S. 3217 May 20, 2010, by a vote of 59-39

As noted, yesterday the Senate passed S. 3217, by a vote of 59-39. The final vote came after Senate Majority Leader Reid, that same day, was successful in obtaining "Cloture" on the legislation, meaning three-fifths of the Senate, 60 votes, supported limiting debate to only 30 additional hours. The significance of the Cloture Vote indicated there was enough support for final passage, which occurred quickly thereafter. This was the second attempt at a Cloture Vote by Majority Leader Reid, the first failing by only a few votes the day earlier. The eventual success of the vote, and final passage of the underlying bill, meant that the Senate was unable to vote on all outstanding amendments, including the possibility of a "Manager's Amendment" by Senate Banking, Housing and Urban Affairs Chairman Chris Dodd (D-Conn.). This indicates that additional revisions in many of these areas are expected in any conference the Senate has with the House.

We discuss some of these areas below.

Key Elements of S. 3217

S. 3217, sponsored by Sen. Dodd, includes many of the measures that the Obama administration initially wanted, such as:

- **Consumer Financial Protection Agency.** A consumer financial protection agency is created to make sure consumers get correct information on consumer loan products to protect against some of the most notable problems in the financial system, including the sale of "subprime" mortgages and the marketing of credit cards to those who cannot afford them. Sen. Dodd named this the "Bureau of Financial Protection" and placed it under the Federal Reserve, in part to address Senate Republican concerns about giving the government too much power over banks.
- **Council to Address Systemic Risk.** This provision is intended to address "systemic risk," i.e., when the collapse of a financial institution threatens the nation's financial system. Sen. Dodd creates a council to identify and address systemic risk. It would have the authority to write and enforce regulations for banks and credit unions with assets of more than \$10 billion. The nine-member council would be chaired by the Treasury Secretary and would include representatives from the Federal Reserve, Securities and Exchange Commission, and other agencies. Sen. Dodd did initially require a \$50 billion fund, to be funded by an assessment on the bigger organizations under the Federal Reserve's supervision, for the costs of the liquidation of a major financial institution. That provision was removed by an amendment from Sen. Richard Shelby (R-Ala.), the Ranking Member of the Senate Banking Committee; and now a credit line from Treasury would be used instead.
- **Efforts to Regulate Derivatives.** The trading of over-the-counter derivatives would be regulated for the first time. Derivatives are financial contracts promising a payment based on the performance of an asset, such as a security, the change in an interest rate index, or the default of a company. Sen. Dodd allowed Sen. Blanche Lincoln (D-Ark.), Chair of the Agriculture, Nutrition & Forestry Committee, to insert a tough provision on derivatives, including (1) rules requiring all standardized transactions between dealers and other larger market participants to be cleared and traded on an exchange or electronic platform, and (2) a ban on derivatives-trading by banks. The latter provision, especially, has drawn a considerable backlash by the financial industry and is one of many areas that could see modification on the conference level.
- **Volcker Rule.** Limits on banks to engage in proprietary trading, a/k/a the "Volcker Rule," are established. Sen. Dodd has limits on banks trading in financial securities using their own funds, something proposed by former Federal Reserve Chairman Paul Volcker and supported by the Obama administration. S. 3217 would require regulators to implement it after further study.

## Other Unresolved Issues that may be Addressed on the Conference Level

A number of other issues were not resolved by the Senate and may be considered in Conference. Attempts, for example, may be made to weaken the derivatives language (as noted above), as well as to strengthen the Volcker Rule by making it mandatory; a measure will also be entertained taking apart Fannie Mae and Freddie Mac. It is on the Conference level where one of the best opportunities lies to affect passage financial regulatory reform.

## Summary

Time is running out on action in Congress on financial regulatory reform. As discussed, final congressional passage is considered very likely and the legislation is then expected to go to the President for his anticipated signature. The Public Policy & Infrastructure Practice remains available to provide counsel on all lobbying matters related to this and other key legislation pending before Congress

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