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## **Financial Services Legislative and Regulatory Update**

### Leading the Past Week

While Washington and the country were mainly focused on the troubles surrounding the implementation of the Affordable Care Act (ACA), other areas of the federal government tasked with implementing the President's other signature law – Dodd-Frank – were having a bit more success. Last week, regulators moved ahead with several aspects of the Dodd-Frank Act, including new clearinghouse standards and additional stress test requirements. However, one area where the roll out has not gone as smoothly is the Volcker Rule. With the nominee for CFTC chair announced this week, it seems that the impetus to get a draft of the final rule out may have gained steam. Despite the interest by some to move forward, there are clear bumps in the road ahead. For example, it was [reported](#) that Securities and Exchange Commission (SEC) Commissioner Michael Piwowar will not support a “final or interim final rule without first re-proposing” the Volcker Rule, a position similar to fellow Republican Commissioner Dan Gallagher, though with a full slate at the SEC, Chairwoman White would have enough votes to pass if her two fellow Democratic Commissioners hold. Though there may be dissent among those that must vote on a final Volcker Rule, regulators are expected to release a draft as soon as this week – though we've been [close before](#).

### Legislative Branch

#### **Senate**

*Yellen Hearing Appears to Show Smooth Sailing for Nominee – [Media Focused on Other Things](#)*

On November 14<sup>th</sup>, Vice Chairman of the Federal Reserve (Fed) Janet Yellen appeared before the Senate Banking Committee for her confirmation hearing for her nomination to serve as Chairman of the Federal Reserve Board. Following the hearing, the general consensus was that Yellen sailed through, with Republicans taking a much softer line of questioning than expected. In her prepared testimony, and then during the question and answer session, Yellen touched on a number of high level issues before the Fed including its quantitative easing policy, where she noted that the Fed would not reduce its “monetary accommodation” or its reliance on unconventional policy tools such as asset purchases until the strength of the economy improves. Interestingly, the most “controversial” element of the

hearing may have come from her response to a Democratic Senator's question, when in response to a question from Senator Kay Hagan (D-NC), Yellen responded that believes the Fed can address concerns with the push out rule without repeal and that the Fed will release rules addressing these concerns later this year. Initially, some interpreted the Vice Chairwoman's remarks to mean that a "fix" to the controversial swaps push out rule could be in the works, but subsequently, it came to be seen that was not the case.

The Senate Banking Committee is expected to vote on Yellen's nomination as early as this week. While Yellen is expected to be easily approved by the Committee, the timing for a vote by the full Senate is more in flux. Senator Rand Paul (R-KY) has said he will put a hold on Yellen's nomination until the Senate considers an Audit the Fed proposal originally crafted by his father, former U.S. Representative Ron Paul. Senator Ted Cruz (R-TX) has also said he will support holding up Yellen's confirmation in order to get a vote on the audit legislation. This maneuver is unlikely to create a real road block, but it could create some procedural headaches. Current Chairman Bernanke's term doesn't expire until the end of January and it seems, at this point, that Yellen will be confirmed before then.

#### *Senate Banking Committee Receives Semi-Annual Report from CFPB Director Cordray*

On November 12<sup>th</sup>, the Senate Banking Committee heard from Director Cordray who spoke about Consumer Financial Protection Bureau's Semi-Annual Report to Congress. During the hearing, Cordray made it clear that he believes the vast majority of institutions are prepared to comply with the QM rule which takes effect in January 2014, and he sees little reason to delay the rule. He went on to add that in the early months after the rule has gone into effect, the CFPB will be looking for good faith efforts at substantial compliance. Senator Crapo and other Senators from both parties continued to question Director Cordray on privacy and security concerns over the CFPB's big data collection. Director Cordray explained that the big data the CFPB collects is non-identifiable and focuses on macro trends in the market. He said that privacy and security regarding the personally identifiable information voluntarily provided to the CFPB by consumers through the consumer complaint program is of the utmost importance. Senator Warren (D-MA) and Senator Moran (R-KS) both asked about the CFPB's efforts to regulate auto-lending market, though coming at their questions from different perspectives. While Warren praised the CFPB for its actions, Senator Moran questioned why the Bureau was trying to [impose new regulations on auto financing](#) outside of a traditional rulemaking procedure. Cordray noted that although the Bureau released its guidelines in March, it had scheduled an open forum to discuss the issue. (see below for more on this event).

#### *Finance Stakeholders Urge Congress to Pass Cybersecurity Legislation*

On November 13<sup>th</sup>, the American Bankers Association, the Financial Services Roundtable, and SIFMA wrote to the Senate, urging Congress to pass cybersecurity legislation that would allow the financial services sector and the government to share more information on threats. The [letter](#), sent to Chairman and Ranking Member of the Senate Select Committee on Intelligence Diane Feinstein (D-CA) and Saxby Chambliss (R-GA) notes that, while Congress waits to pass legislation to "enhance cross-sector sharing, our adversaries are not bound by the same restriction and thus regularly share tools and techniques to attack our nation." While cyber legislation currently remains stalled in the Congress, as financial institutions continue to be on the front line of these battles, this is an issue that should be of continued interest.

#### *GAO Releases Report on Government Support for Too Big to Fail Banks*

In response to a request made by Senators Sherrod Brown (D-OH) and David Vitter (R-LA), on November 14<sup>th</sup> the Government Accountability Office (GAO) released its first [report](#) on whether large banks receive a subsidy from being “too big to fail.” The report, which outlines the assistance that large banks received during the financial crisis, found that these banks were able to borrow at below-market interest rates because of a perception of a government backstop. The GAO will be publishing a follow-on report due out in early 2014 to further examine whether implied government support has created a funding advantage, and it is rumored that this second report will be even more critical of big banks. In response to the report, Brown said that the GAO’s findings underscore “the need to pass our legislation to ensure that these types of bailouts will not happen in the future by imposing sensible capital requirements.” While Senator Brown and others continue to seek a legislative solution, it is worth noting that the market is also moving away from “too big to fail”, as Moody’s announced on November 15<sup>th</sup> that four large banks, Goldman Sachs, JPMorgan Chase, Morgan Stanley, and Bank of New York Mellon, would be downgraded based on the conclusion that they would no longer be bailed out should a crisis occur.

#### *FINRA Updates Arbitration Database Following Congressional Concerns*

On November 12<sup>th</sup>, the Financial Industry Regulatory Authority (FINRA) responded to [comments](#) by Senator Ed Markey (D-MA) calling on the self-regulatory organization (SRO) to improve its processes for tracking and removing unscrupulous brokers from the industry. In response to these concerns, FINRA [updated](#) its online database, “BrokerCheck,” for consumers to investigate broker-dealers and financial advisers. Announcing the update, FINRA Vice President for Registration and Disclosure Derek Linden said that “investors using BrokerCheck will encounter a more user-friendly interface that allows them to quickly find information that can help them decide if an investment professional is right for them.” Although Senator Markey commended FINRA for taking positive steps, clearly he wasn’t satisfied by FINRA’s actions, as he labeled them “cosmetic changes don’t disguise the fact that the information BrokerCheck provides to investors is incomplete.”

### **House of Representatives**

#### *House Financial Services Committee Approves Banking Bills*

On November 14<sup>th</sup>, the House Financial Services Committee approved five pieces of [legislation](#) designed to support investment company growth and relax regulations for smaller institutions. Among the bills considered by the Committee was [H.R. 3468](#) which would expand the National Credit Union Share Insurance Fund. Another bill aimed at small business investment was [H.R. 3329](#), approved by voice vote, which would apply rules on formation and expansion of small bank holding companies with high debt levels to companies with assets up to \$1 billion, assuming they do not conduct overly risky nonbanking activities. However, the Committee spent much of the markup considering [H.R. 1800](#), which would build on the Jumpstart Our Business Startups (JOBS) Act to relax some financing rules for business development companies. Also approved were measures to create a simplified SEC registration system for mergers and acquisition brokers and a bill to increase the minimum tick size of emerging growth companies.

#### *House Subcommittee Weighs Reauthorization, Tweaks to TRIA*

On November 13<sup>th</sup>, the House Financial Services Subcommittee on Housing and Insurance held a hearing on the reauthorization of the Terrorism Risk Insurance Act (TRIA). As with the previous hearings on TRIA, lawmakers were generally supportive of the program, although Republicans reiterated a desire to increase the role of private capital and the private market in the program. Among the other proposals mentioned by lawmakers and witnesses include: lowering the federal cap, increasing

the triggering threshold, creating additional copays, and creating some sort of bond market or other financial instruments for bundling terrorism risk insurance. Another proposal that was floated, but which did not receive much support, was moving away from government recoupment and toward upfront premiums paid to the Treasury by industry. Witnesses, including representatives from Lloyd's of London, the reinsurance industry, and economic experts, across the board supported a long-term five to ten year reauthorization of TRIA—albeit with various alterations. Democrats pushed back against the Republican desire to move toward a private market, citing risk modeling difficulties and coverage issues should TRIA be allowed to sunset or dramatically overhauled. Subcommittee Chairman Neugebauer (R-TX) said that this is likely the last pre-legislative hearing on TRIA and that moving forward the Subcommittee will work to provide clarity to the industry.

#### *House Financial Services Subcommittee Examines International Models of Central Banking*

On November 13<sup>th</sup> the House Financial Services Subcommittee on Monetary Policy and Trade met to examine the central banks of other advanced economies, focusing on their governance, policy tools, and their successes and failures in implementing monetary policy. Witnesses included: Desmond Lachman, American Enterprise Institute; Athanasios Orphanides, Massachusetts Institute of Technology; John Makin, American Enterprise Institute; and Adam Posen, Peterson Institute for International Economics. There was much discussion of the Fed's dual mandate of maximizing employment and minimizing inflation. Specifically, Mr. Posen pointed to concerns that the Fed's persistent low interest rates, caused by the constraint of the dual mandate, could lead to asset bubbles. In addition, reflecting on a quote by former Fed Chairman Paul Volcker that the Fed will fall short if it is asked to do too much, Subcommittee Vice Chairman Bill Huizenga (R-MI) said that a focus on employment "has diverted the Fed's attention from the more important issue of low inflation" which, he argued, should be the Fed's sole focus.

#### Executive Branch

##### **CFTC**

#### *Massad Nominated to Lead CFTC*

On November 12<sup>th</sup>, President Obama announced he will nominate the Assistant Secretary for Financial Stability Timothy Massad to be Chairman of the Commodity and Futures Trading Commission (CFTC). Massad has served at the Treasury since 2011, heading the Administration's effort to wind down the Troubled Asset Relief Program (TARP). The Senate appeared to have mixed reactions to the pick, as Chairman Johnson noted his support for Massad, by saying he is "exactly the type of leader the CFTC needs," while conversely, Massad received an unenthusiastic response from a number of liberal Democrats. Senator Sherrod Brown, a member of the Senate Agriculture Committee that will vet Massad's nomination, said he was unsure that Massad would "continue reforms initiated by Chairman Gensler" and be aggressive in implementation of derivatives rules. In addition to a lukewarm reception from Congress, the same day as the announcement nineteen agriculture industry groups [wrote](#) to the White House and to the Senate Agriculture Committee urging the nomination of a CFTC Commissioner with "a genuine background and experience in agricultural commodity futures markets."

#### *CFTC Strengthens Cross-Border Guidance*

In an [advisory](#) released November 15<sup>th</sup>, the CFTC clarified guidance for cross-border derivatives rules. The advisory makes clear that foreign banks, no matter their affiliation with a U.S. company, must meet with the rules and regulations prescribed by the Dodd-Frank Act if the swaps trades in questions are being facilitated by someone in the U.S. The guidance also applies to transactions arranged between foreign banks and other foreign entities. The clarification is in response to concerns raised about

skirting the CFTC's cross-border rules for derivatives. Speaking on the advisory, Chairman of the House Agriculture Committee Frank Lucas (R-OK) called the agency "irresponsible" for "overnight" changing regulations that market participants had thought concrete.

#### *Additional Clearinghouse Standards Finalized*

On November 15<sup>th</sup>, the CFTC voted unanimously to finalize [standards](#) governing large clearinghouses that are considered to be systemically important. The rule requires clearinghouses that have been designated by the Financial Stability Oversight Council (FSOC) as systemically important to have a "prearranged and highly reliable funding arrangement" to support their collateral. According to a release on the vote, the rule also includes "substantive requirements relating to governance, financial resources, system safeguards, special default rules and procedures for uncovered losses or shortfalls, risk management, additional disclosure requirements, efficiency, and recovery and wind-down procedures."

### **SEC**

#### *Exchanges and SROs Agree on SEC Recommendations for Trading Disruption*

On November 12<sup>th</sup>, exchange operators and their self-regulatory organizations (SROs) announced they have reached "general agreement on certain recommendations and preliminary implementation timetables in response to the September 12, 2013 meeting between leaders of the equities and options exchanges, FINRA, the Depository Trust & Clearing Corporation (DTCC) and Options Clearing Corporation and SEC Chair Mary Jo White." The SROs have been working with SEC staff on recommendations to strengthen resilience, performance, disaster recovery, and governance of critical infrastructure in the exchanges as a response to a three-hour Nasdaq trading disruption in August. Speaking on the recommendations, Mary Jo White said she hopes they will lead to elimination of trading glitches and facilitate discussions of further structural changes to the U.S. financial sector. White, acknowledging that no technology is perfect, outlined a "zero tolerance" policy at the SEC to market disruptions such as the Nasdaq glitch that prompted discussions.

### **FDIC**

#### *FDIC Releases Stress Test Scenarios*

On November 12<sup>th</sup>, the Federal Deposit Insurance Corporation (FDIC) [released](#) economic scenarios for use by large financial institutions with more than \$10 billion in the stress tests required by the Dodd-Frank Act. The tests include baseline, adverse, and severely adverse scenarios that reflect economic activity such as unemployment, exchange rates, prices, income, and interest rates. The FDIC is working with the Federal Reserve and the OCC in developing and distributing the scenarios. The Fed released stress test scenarios on November 1<sup>st</sup> and released additional market shock data for stress test use on November 12<sup>th</sup>.

### **CFPB**

#### *CFPB Holds a Forum on Auto Finance*

On November 14<sup>th</sup>, nearly eight months after it issued its guidance for the industry, the CFPB held a forum about possible discrimination in the auto finance market. At the forum, industry representatives expressed concerns over the March bulletin's flat fee proposal in which auto loan markups would no longer be discretionary. CFPB officials made it clear that the flat fee proposal included in the bulletin was just an example and that they are open to any alternative compensation models that both limit fair lending risk and are economically sustainable, though they struggled to outline other acceptable alternatives. Another point of contention between industry and the Bureau dealt with the CFPB's

statistical methodology. Industry representatives argued that the use of proxies were inaccurate, while CFPB officials defended their methodology as reliable and in line with common practices, though failed to offer any insight into the math that serves as the foundation for their analysis.

#### *Bureau Releases Online Database of Housing Counselors*

On November 8<sup>th</sup>, the CFPB launched a [tool](#) to assist consumers in finding local housing counseling agencies to answer questions and concerns. The tool is meant to complement requirements that lenders provide a list of nearby housing counselors to those applying for a mortgage. Lenders can choose to build their own lists or use the CFPB's tool which shows consumers the closest Department of Housing and Urban Development (HUD)-approved counselors.

## **OCC**

#### *OCC Publishes Guidance for Bankers on Independent Consultants*

On November 12<sup>th</sup>, the Office of the Comptroller of the Currency (OCC) released [guidance](#) on how and when independent consultants should be used in enforcement actions. The guidance comes in response to pressure from lawmakers who have criticized the OCC for relying too heavily on outside consultants to oversee the review of foreclosure errors by banks. Among the concerns voiced by lawmakers include conflicts of interest between the banks being investigated and the consultants and the high cost of consultants. The OCC's guidelines are intended to help banks ensure consultants are independent, with the necessary resources and qualifications. The guidance makes clear that this guidance only applies to the use of consultants to address significant violations, and not when the OCC requires a bank to hire an outside firm. Senator Sherrod Brown (D-OH), one of the lawmakers who critiqued the OCC's reliance on consultants, [called on](#) the OCC to "vigorously enforce these standards to ensure that consultants serve the public, not the banks that hire them."

## **FHFA**

#### *Fannie and Freddie Will Continue to be Profitable, Groups Request Congress Avoid Raising Fees*

On November 13<sup>th</sup>, Moody's Investor Services released a report finding that Fannie Mae and Freddie Mac will continue to reap profits for the coming few years. As profits continue, taxpayers are close to breaking even in the bailout that the two government sponsored entities (GSE) received in September 2008. The same day, a group of housing industry stakeholders [wrote](#) to lawmakers requesting that Fannie Mae and Freddie Mac's fees not be raised as an offset in a budget deal. The letter, sent by the Mortgage Bankers Association, National Association of Realtors, American Bankers Association, and others, asks Congress not to use housing as a piggy bank for a budget deal. In 2011, Congress raised the GSEs' fees by 10 basis points to fund payroll tax relief.

## **International**

#### *FSB Updates List of Globally Systemically Important Banks*

On November 11<sup>th</sup>, the Financial Stability Board (FSB) [released](#) an updated list of global systemically important banks (G-SIBs), using a methodology developed by the Basel Committee on Banking Supervision (BCBS). The list is broken into five categories of institutions based on how much capital they are required to hold. Due to the annual assessment conducted as part of the update, some large banks, including Citigroup and Deutsche Bank will be required to hold less capital than originally proposed by regulators last year. Announcing the changes, FSB said the updates "reflect the combined effects of data quality improvements, changes in the methodology and changes in underlying systemic importance."

### Miscellaneous

#### *Bitcoin for use in Federal Elections Delayed*

With both the Senate Homeland Security and Government Affairs Committee and the Senate Banking Committee separately set to hold hearings on virtual currency this week, it is worth noting that late last week the Federal Election Commission (FEC) announced it would delay a vote on final rules related to the use of Bitcoin as a way of contributing to candidate for federal office. There are currently three draft proposals before the FEC that would allow campaigns to collect but not spend Bitcoins and it is unclear when the FEC will meet to finalize its decision on this issue.

#### *New York Considers Licensing for Virtual Currency*

On November 14<sup>th</sup>, the New York State Department of Financial Services [released](#) a notice of intent to explore virtual currencies, including a potential “BitLicense.” A BitLicense would be specific to virtual currency transactions and activities, which would include anti-money laundering and consumer protection requirements for licensed entities. The move comes as entrepreneurs who support a greater deployment of the BitCoin currency appear to be moving forward with bringing the virtual currency mainstream. This includes Circle, [bringing](#) Raj Date, one of the first hires at the CFPB, on a board member to help advise on regulatory compliance.

### Upcoming Hearings

On Monday, November 18<sup>th</sup> at 3:00pm in 342 Dirksen, the Senate Homeland Security and Government Affairs Committee will hold a hearing title, “Beyond Silk Road: Potential Risks, Threats and Promises of Virtual Currencies.”

On Tuesday, November 19<sup>th</sup> at 10am in 538 Dirksen, the Senate Banking, Housing and Urban Affairs Committee will hold a hearing titled “Housing Finance Reform: Fundamentals of Transferring Credit Risk in a Future Housing Finance System.”

On Tuesday, November 19<sup>th</sup> at 10am in 2128 Rayburn, the House Financial Services Subcommittee on Oversight and Investigations will hold a hearing on disparate impact theory.

On Tuesday, November 19<sup>th</sup> at 1:30pm in 2128 Rayburn, the House Financial Services Subcommittee on Housing and Insurance will hold a hearing on implementation of the Biggert-Waters Flood Insurance Act of 2012.

On Tuesday, November 19<sup>th</sup> at 2pm in 538 Dirksen, the Senate Banking, Housing, and Urban Affairs Subcommittee on Financial Institutions and Consumer Protection will hold a hearing on regulating financial holding companies and physical commodities.

On Tuesday, November 19<sup>th</sup> at 3:30pm in 538 Dirksen, the Senate Banking, Housing and Urban Affairs Subcommittee on National Security and International Trade and Finance will hold a hearing on virtual currency.