



## ML Strategies Update

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## Financial Services Legislative and Regulatory Update

### Leading the Past Week

It was another busy week on the Hill and in the Administration, but it may have been most notable for events from the end of the week that may have only further served to add fuel to revitalized attacks on “big banks.” First, during a massive six-hour hearing about the “London Whale trade,” Chairman Levin received commitments from both regulators and representatives of JP Morgan that taken together, could lead to considerable changes [throughout the industry](#), and certainly served to re-energize proponents of a strong Volcker rule. Later on Friday, the SEC announced that the hedge fund SAC would agree to pay a penalty of **\$616 million dollars** to settle allegations of insider trading, though the settlement doesn’t foreclose additional charges against the members of the fund.

Also last week, Dallas Fed President Richard Fisher, a noted advocate for breaking up the banks, took the somewhat [unprecedented](#) step of speaking before CPAC, the annual conservative gathering in Washington. Despite concerns that Fisher might [rally the crowds](#), according to [published reports](#), he only ended up speaking to a group of 20 people at a sparsely attended event.

However, it wasn’t all bad news, because after a “vigorous debate,” with regulators on both sides of the Atlantic expressing concerns over the complexity of the Basel III global capital rules, Steve Ingves, Chairman of the Basel Committee on Banking Supervision, announced that the Committee will discuss a review of the framework at its March 20<sup>th</sup> meeting. Speaking last week, he said that while some changes being considered include how trading books are supervised, Ingves said “others might necessitate a deeper, longer-term review.”

### Legislative Branch

#### **Senate**

*Senate PSI Report on JPMorgan Trading Loss Finds Evidence of High Risk, OCC Failures*

On March 15<sup>th</sup>, the Senate Permanent Subcommittee on Investigations held a [six-hour long](#) hearing to examine JPMorgan Chase’s “London Whale” trading loss. In advance of the hearing,

the Subcommittee released a [300-page report](#) that offered detailed evidence, including email and telephone transcripts, indicating traders took on greater risk without notifying regulators. In addition to the issues uncovered at JP Morgan, the report was strongly critical of the OCC, saying the agency failed to uncover inappropriate trading activity and tolerated insufficient bank reports. Among other things, the report concluded that federal regulators need to strengthen their derivatives trading regulations and quickly finalize the Volcker Rule. Seeing as the Committee is Chaired by Senator Carl Levin (D-MI), one of the authors of the Volcker Rule amendment, this conclusion is not surprising. What was surprising was that during the hearing Chairman Levin was able to receive assurances from one of JP Morgan's representatives that going forward, the company will link derivatives to specific assets when using them as a hedge. Combining this assurance with promises made by Comptroller Curry, Mr. Levin may put forward a clear path towards achieving his goal of prohibiting portfolio hedging. The hearing was sparsely attended—with only Chairman Carl Levin (D-MI), Ranking Member John McCain (R-AZ) and Senator Ron Johnson (R-WI) in attendance. Chairman Levin called on regulators to strengthen their oversight to keep Wall Street in line and McCain and Johnson accused the bank of embracing “too big to fail” in its business model.

#### *Lawmakers Praise White, Grill Cordray in Nominations Hearing*

On March 12<sup>th</sup>, the Senate Banking Committee met to consider the nominations of Richard Cordray to head the CFPB and Mary Jo White to Chair the SEC. While panel Republicans were, generally speaking, highly laudatory of White, Director Cordray was expectedly grilled on the Bureau's spending and transparency, sending the signal of continued troubles for his confirmation. In an effort to assuage concerns Cordray promised to do everything in his power to enforce consumer protection laws, highlighting the work the CFPB has already done to implement new mortgage rules, broaden public outreach and participation, and reduce compliance burdens. Addressing questions concerning the CFPB's budgetary structure—a major sticking point for Republicans—Cordray said the Bureau has sought to provide detailed financial reporting and said he would consider detailing the agency's budget document before the Senate Appropriations Committee.

While Cordray's nomination may face difficulties, if it is ever fully considered at all, White earned praise from both sides of the aisle. Lawmakers welcomed White's opening comments, which promised to aggressively enforce securities laws and expedite held up Dodd-Frank rulemakings. Senator Tom Coburn (R-OK) said he would “aggressively support” White's nomination and Chairman Tim Johnson (D-SD) said White provided “excellent answers.” In addition to outlining her early priorities for the SEC, White addressed the ongoing concerns over “too big to jail” institutions, saying no bank should be “too big to charge.” The Banking Committee has scheduled the vote on the nominations of White and Cordray for Tuesday, March 19<sup>th</sup>.

#### *Bipartisan Group of Senators Introduce “Jumpstart GSE Reform Act”*

On March 14<sup>th</sup>, Senators Bob Corker (R-TN), Mark Warner (D-VA), David Vitter (R-LA) and Elizabeth Warren (D-MA) introduced the [Jumpstart GSE Reform Act](#) which would prohibit Treasury's sale of preferred shares without Congressional approval as well as other structural reform of the housing finance entities. The bill would also bar any increase in the guarantee fee, which is charged by Fannie Mae and Freddie Mac in order to offsetting other government spending. Following the release of the legislation, a spokesperson for Chairman Tim Johnson (D-SD) indicated the Chairman's support for the bill and that the Banking Committee will consider this bill with another proposal designed to expand refinancing options for home loans guaranteed by the GSEs. FHFA Acting Director Edward DeMarco also lauded the legislation and praised the Senators for their efforts to begin a discussion toward GSE reform.

### *Senate Finance Announces Weekly Tax Reform Meetings*

Beginning March 21<sup>st</sup>, Senate Finance Committee members will conduct weekly meetings on various aspects of comprehensive tax reform. Chairman Max Baucus and Ranking Member Hatch [announced](#) the initiative, saying topics for consideration will include “examining the tax treatment of small businesses and corporate investment; families and children; education expenditures; different types of income and tax structures; international taxation; charitable giving and tax-exempt organizations; and many others.” The Committee’s first meeting will focus on simplifying the tax code for American families.

### *Insurance Agents Bill Introduced*

Last week Senators John Tester (D-MT) and Mike Johanns (R-NE) introduced [legislation](#) to allow insurance brokers and agents to more easily operate across states. They were joined by Representatives Randy Neugebauer (R-TX) and David Scott (D-GA) who introduced a House version of the proposal. The legislation would create the National Association of Registered Agents and Brokers (NARAB) to be a non-profit, independent board comprised of state insurance commissioners and insurance market representatives. After passing background checks in their home states, insurance agents could apply for NARAB membership, allowing them to sell insurance in other states.

### *Senators Continue to Grill Holder of Too Big to Jail Comments*

On March 12<sup>th</sup>, Senators Mark Warner (D-VA) and Bob Corker (R-TN) [wrote](#) to Attorney General Eric Holder requesting additional clarity on recent “too big to jail” comments. The letter requested the Justice Department aggressively prosecute those individuals and banks which break the law, no matter their size. The preceding week, Holder had testified that: “I am concerned that the size of some of these institutions becomes so large that it does become difficult for us to prosecute them when we are hit with indications that if you do prosecute, if you do bring a criminal charge, it will have a negative impact on the national economy, perhaps even the world economy.” Warner and Corker also questioned Holder on whether there exist any “major impediments” to creating a regulatory infrastructure under Dodd-Frank that addresses these issues.

## **House of Representatives**

### *Garrett Introduces SEC Cost-Benefit Bill*

On March 12<sup>th</sup>, Representative Scott Garrett (R-NJ), Chairman of the Financial Services Subcommittee on Capital Markets and Government-Sponsored Enterprises, [re-introduced](#) the SEC Regulatory Accountability Act of 2013 (H.R. 1062). The legislation, which is identical to a bill approved by the Committee last year, would require enhanced economic analysis of requirements and a review of existing regulations. The bill would also require the SEC to clearly identify the nature of the problem that would be addressed before issuing a new regulation. Garrett said it was encouraging that SEC nominee Mary Jo White acknowledged during her testimony before the Senate Banking Committee that the SEC should be trying to better assess the economic impacts of rules. Conversely, Senator Elizabeth Warren (D-MA) took the opposite view to nominee’s perspective, questioning White on the costs of “under-enforcing” regulations.

Also this past week, the Chamber of Commerce released a [report](#) urging financial services regulators to conduct more rigorous cost-benefit analyses. The report, which was drafted by two Ohio State University law professors, finds that “the scale and scope of regulations have made it

even more important, despite the short deadlines, for regulators to ensure they adequately consider the effectiveness and consequences of their proposals.” In light of the D.C. Circuit’s decision regarding the SEC’s Proxy Access Rule, groups such as the Committee on Capital Markets Regulation have warned lawmakers to urge regulators to take proper cost-benefit analysis into account to ensure that Dodd-Frank regulations are upheld.

#### *House Passes Privacy Notice Legislation*

On March 12<sup>th</sup> the House passed H.R. 749, a bill to eliminate requirements imposed by the Gramm-Leach-Bliley Act that financial institutions send annual privacy policy disclosures. Representative Blaine Luetkemeyer (R-MO), sponsor of the legislation, called the bill a simple change which would greatly aid financial institutions by lowering compliance costs. The House passed identical legislation at the end of the 112<sup>th</sup> Congress but the Senate did not take up the legislation before the end of the lame duck session.

#### *House Financial Services Subcommittee Examines Reducing Role of FHA*

On March 13<sup>th</sup>, the House Financial Services Subcommittee on Housing and Insurance held a hearing to compare the private and public housing finance sectors and to examine ways in which to reduce the role of the FHA. Witnesses included: Ken Bjurstrom, Milliman; Nat Shapo; Katten Muchin Rosenman, LLP; Brian Chappelle, Potomac Partners; Steve Stelmach, FBR Capital Markets & Co.; and Teresa Bryce Basemore, Radian Guaranty, Inc. As expected the hearing came out on a partisan basis, with the Chairman of the Subcommittee, Randy Neugebauer (R-TX) saying that the FHA has several advantages over its private competitors, such as artificially low insurance pricing and lower capital reserve requirements, which allows this arm of the government to expand its reach into areas of the market that should not be receiving government support. Ranking Member Michael Capuano disagreed with the Chairman’s analysis, saying the FHA never crowded out private competitors but rather met demand during the financial crisis.

### Executive Branch

#### **CFPB**

##### *Cordray Believes QM Exemption Will Protect Small Lenders*

Speaking at the Independent Community Bankers of America’s annual conference last week, CFPB Director Richard Cordray said that small institutions will likely be held to a different set of new mortgage requirements than large institutions. The Bureau has proposed an exemption for portfolio loans made by small lenders from its new qualified mortgage rule, covering banks with less than \$2 billion in assets. Cordray said the exemption is appropriate as “the traditional lending practices of community banks did not cause the financial crisis.” While the QM rule was finalized in January, the exemption is still in the works. Cordray did not shed light on when a final rule would be issued.

##### *CFPB Issues Proposed Rule for Nonbank Student Loan Providers*

On March 14<sup>th</sup>, the CFPB [proposed a rule](#) to allow the Bureau to supervise certain nonbank student loan servicers. Currently, the CFPB oversees student loan servicing at large banks. The rule would expand this authority to nonbank firms that handle more than 1 million borrower accounts. The Bureau is seeking this expansion in order to evaluate the extent and scope of a number of issues it has identified in the student loan market.

#### **CFTC**

##### *CFTC Contemplating Extending Cross-Border Compliance Deadline*

On March 12<sup>th</sup>, CFTC Commissioner Mark Wetjen said the Commission is considering

extending the July effective date for cross-border derivatives rules. The potential delay was triggered by the European Securities and Markets Authority's recent announcement that EU's implementation timeline could extend into 2014. Speaking at the Futures Industry Association conference, Wetjen said the EU delay is problematic as the agency is already "more than two years past...the deadline prescribed by Congress." Still, the CFTC could "extend the exemptive order" to keep pace with European regulators.

## **FDIC**

### *FDIC Not Planning to Raise Insurance Premiums; On Track to Meet 2020 DIF Standards*

On March 13<sup>th</sup>, the FDIC said it is unlikely to lower insurance premiums soon but also does not see a need for increases in the near future. By 2020 the FDIC is required to ensure that the Deposit Insurance Fund's (DIF) reserve ratio is built to 1.35 percent of insured deposits. Chairman Gruenberg, speaking at the ICBA's convention, said the FDIC is currently above 0.4 percent and "very much on track" to meet requirements by 2020. In 2010 the DIF was over \$20 billion in the red; currently the fund is close to \$33 billion in the black.

## **FHFA**

### *Watt Rumored to Considered as Nominee to Head FHFA*

Last week, the Wall Street Journal reported that Representative Melvin Watt (D-CA) is being considered to replace acting Director Edward DeMarco as the head of the FHFA. While a final decision on the head of the body regulating Fannie and Freddie could come as soon as April, Watt, or any nominee to head the agency, will likely face an uphill confirmation battle due to Republican opposition. In 2010, Republicans blocked the President's first choice, former North Carolina banking commissioner Joseph Smith.

## Upcoming Hearings

On Tuesday, March 19<sup>th</sup> at 10am, in 538 Dirksen, the Senate Banking, Housing and Urban Affairs Committee will meet in executive session to vote on the nominations of: Richard Cordray, to be Director of the Consumer Financial Protection Bureau; and Mary Jo White, to be a member of the Securities and Exchange Commission. Immediately following the vote, the full Committee will meet for a hearing titled "Bipartisan Solutions for Housing Finance Reform?"

On Tuesday, March 19<sup>th</sup> at 10am, in 1100 Longworth, the House Ways and Means Committee will hold a hearing on federal tax provisions that affect state and local government operations and financing.

On Tuesday, March 19<sup>th</sup> at 10am, in 2128 Rayburn, the House Financial Services Committee will hold a hearing on the Federal Housing Finance Agency.

On Tuesday, March 19<sup>th</sup> at 3pm, in 538 Dirksen, the Senate Banking, Housing and Urban Affairs Subcommittee on Securities, Insurance and Investment will hold a hearing titled "Streamlining Regulation, Improving Consumer Protection and Increasing Competition in Insurance Markets."

On Wednesday, March 20<sup>th</sup> at 10am, in 2128 Rayburn, the House Financial Services Subcommittee on Financial Institutions and Consumer Credit will hold a hearing on how federal regulations affect small financial institutions.

On Wednesday, March 20<sup>th</sup> at 10am, in 1300 Longworth, the House Agriculture Committee will mark up seven derivatives bills.

On Wednesday, March 20<sup>th</sup> at 1:15pm, in 1100 Longworth, the House Ways and Means Subcommittee on Select Revenue Measures will hold a hearing to consider proposals to revamp the taxation of financial products.

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