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## FINANCIAL SERVICES LEGISLATIVE AND REGULATORY UPDATE

April 23, 2012

### Leading the Past Week

Welcome back as Congress returned from the recess and almost immediately deviated away from the sense of bipartisan accomplishments secured before the break and instead opted to move closer towards the electoral “silly season.” Perhaps no better example of this could be seen from the competing tax bills that each body passed -- the so-called Buffet Rule in the Senate and a small tax proposal in the House – each with about the same chance of being considered and enacted by the other chamber. However, while Congress may have initiated the slow crawl towards gridlock and legislative stasis, the Administration continues to push out its implementation of the Dodd-Frank Act, with the past week providing excellent examples of how lobbying efforts to impact the implementation have been successful. First, with the various regulatory bodies responsible for implementing the Volcker Rule announced a delay until 2014 for US firms to become compliant with the rule. At the same time, the SEC and CFTC finally came out with their rules defining who will be judged a “swap dealer” and a “major swap participant” while carving out a significant *de minimis* exemption that may blunt the overall impact of the rule.

### Legislative Branch

#### **Senate**

##### *Senate Rejects Buffett Rule:*

In a 51-45 party line vote, the Senate rejected the Buffett rule. It was not expected that the 60 votes needed to break the filibuster on the bill to raise the effective tax rate on millionaires would materialize; however, the failure of the measure has set the stage for an election dominated by rhetoric around taxing the rich. In fact, many believe the Buffett Rule—with its relatively small impact on the deficit, \$47 billion over ten years—was always more about campaign strategy than it was about tax policy. Even as the Buffet Rule was set to fail, top Obama Administration economic policy officials took the stage to defend the spirit behind the

measure. Challenging Mitt Romney's proposals and record, Treasury Secretary Geithner told ABC's *This Week* that the rule was "part of a very comprehensive, detailed, long-term fiscal program that would bring our deficits down to a sustainable level."

*Senate Republicans Join Legal Challenge of Obama Recess Appointments:*

On April 17<sup>th</sup>, Senate Majority Leader Mitch McConnell (R-KY) announced Senate Republicans will file an amicus brief in the court case to challenge the recess appointments to the National Labor Relations Board. In response to the challenge, a White House spokesperson said the Administration "confident that the president's authority to make recess appointments will be upheld by the courts."

## **House of Representatives**

*House Financial Services Committee Advances Deficit Cutting Legislation:*

On April 18<sup>th</sup>, the House Financial Services Committee approved legislation that would cut the deficit by \$35 billion while preventing automatic cuts to defense and other discretionary spending. As part of the House budget resolution adopted in March, six committees were each instructed to pursue measures to reduce the deficit. The Financial Services Committee's deficit reduction measures consisted of four proposals: 1) eliminating the Home Affordable Modification Program, a TARP-funded program to aid homeowners with loan modifications; 2) placing the CFPB under the normal appropriations process; 3) reauthorizing the National Flood Insurance Program for five years with reforms; and 4) repealing the Office of Financial Research. The deficit package now goes to the House Budget Committee for inclusion in the appropriation process; however, Senate Democrats have already vowed not to advance the March House Budget in addition to refusing to open the Dodd-Frank Act to changes.

*House Ways and Means Examines Potential Changes to Retirement Tax Incentives:*

On April 19<sup>th</sup>, the House Ways and Means Committee met to examine changes to tax incentives for retirement plans and retirement savings as a part of comprehensive tax reform, including simplification of incentives, increasing participation in incentive programs and better targeting incentives. The panel of experts overwhelmingly favored methods such as auto-IRAs, auto-enrollment, and auto-escalation as means of increasing retirement savings. The panel also generally supported Representative Neal's (D-MA) bill, the Automatic IRA Act of 2012 (H.R. 4049). Additionally, the panel agreed that any methods to increasing saving in younger generations, to increase financial literacy and to provide broad coverage options are crucial.

Although various budget deficit reduction proposals, including the Simpson-Bowles plan, called for significant reductions in the amount of retirement incentives in the code, the Committee appears to be approaching changes to the retirement tax incentive scheme from an approach of 'do no harm.' All five panel members stressed that the current retirement system is generally working fairly well and that Congress would do wrong to eliminate tax incentives for retirement savings. While approximately 33 percent of Baby Boomers still fear they will not have the appropriate means to retire, these numbers are significantly improved over recent years—in spite of the economic downturn. A common theme of the hearing was the lack of plans and options at small employers. One witness stressed that this shortfall is due to business

uncertainty, not tax code complications. Other proposals put forth by lawmakers and panelists were preservation of employee stock ownership plans (ESOPs), improved rollover options, targeted and electronic delivery of retirement account information, and additional annuity options to further lifetime income.

## Executive Branch

### **Federal Reserve**

#### *Regulators Delay Implementation/Enforcement of Volcker Rule for Two Years:*

After months of speculation around the fate of the Volcker Rule, regulators confirmed on April 19<sup>th</sup> that US banks will have until at least July 21, 2014 to comply with the rule's proprietary trading and investment crackdown. Seeking to assuage fears over compliance, and in the face of realizations that the five agencies responsible for jointly implementing the rule would be hard pressed to issue a final rule before the July 21<sup>st</sup> effective date, the Fed affirmed last week that regulators will use "the full 2-year period provided by the statute to fully conform its activities and investments, unless the Board extends the conformance period." The move is being described as an effort to calm industry fears over compliance with rules that lack clarity. Representative Barney Frank (D-MA) called the Fed's announcement "an appropriate and reasoned approach to the implementation of this important provision," continuing, while it remains important for regulators to adopt a rule by July 21<sup>st</sup>, "the two-year period during which the banks will have to come into compliance with the rule will allow a reasonable time for them to make their necessary changes, and will give the regulators the chance to deal with any particular issues that arise from the experience of implementation."

### **SEC**

#### *SEC Adopts Definitions of Swap Dealer, Major Swap Participant:*

On April 18<sup>th</sup>, the SEC unanimously voted to adopt final definitions for security based 'swap dealers' and 'major swap participants' which will be subject to registration, capital, margin and business conduct requirements under the Dodd-Frank Act. The final rules are substantially different from the proposed definitions and include higher *de minimis* thresholds for swap dealers, a new phase-in period, and a requirement for SEC staff to review the definitions in context of the security based swap market when the new plan is in place. The adopting release estimated that fewer than 50 entities may seek to initially register as swap dealers and that entities are not required to register until the SEC has adopted final registration requirements.

Under the new definitions, a security based swap dealer is one that meets one of four criteria: 1) it holds themselves out as a dealer in security-based swaps; 2) it makes a market in security-based swaps 3) it regularly enters into security-based swaps with counterparties as an ordinary course of business for their own account; or 4) it engages in activity causing them to be commonly known in the trade as a dealer or market maker in security-based swaps. The new rule also would specify that the term "security-based swap dealer" does not include a person who enters into security-based swaps for their own account "not as a part of a regular business."

Although, the CFTC originally said firms would be counted as swap dealers if they traded more than \$100 million in swaps over a 12-month period, the rule as announced increased the *de*

*minimis* exemption up to \$8 billion for most asset classes as an initial phase-in, however, that threshold could eventually be dropped to \$3 billion, or even changed further depending on future SEC action.

The final definitions are part of a joint rulemaking with the CFTC. Security based swaps, those under the SEC's authority, account for only 5 percent of the \$600 trillion over-the-counter market. As such, the SEC anticipated the majority of swaps under its jurisdiction will be credit default swaps based on a single, company, government or borrower. The SEC/CFTC rules are parallel but not identical. For more on the final CFTC rule, see below.

## **CFTC**

### *CFTC Adopts Swap Dealer Definition:*

On April 18<sup>th</sup>, in a 4 to 1 vote, the CFTC adopted a final rule to define 'swap dealer,' 'major swap participant' and those entities that will be considered dealers and subject to additional capital and regulatory requirements. Like the SEC rule, the CFTC rule has changed substantially over the December 2010 proposal, including a de minimis exception and a phase-in period. The CFTC rule includes a phased-in de minimis threshold of \$8 billion. This threshold will exist for two and one-half years after data starts to be reported to swap data repositories, and then the CFTC will prepare a study of the swap markets, including data and information that becomes available about the de minimis threshold. Nine months after the completion of this study, the Commission may end the phase-in period, or propose new rules to change the de minimis threshold (either up or down). If the Commission doesn't take any action, the phase-in period will automatically terminate five years after the data starts to be reported to swap data repositories.

Similar the SEC definitions, the CFTC used the four criteria established by Dodd-Frank, including: 1) entities that hold out as a dealer; 2) a market maker in swaps; 3) entities that regularly enter into swaps with counterparties; or 4) entities engaging in activity "causing itself to be commonly known" as a dealer. The rule also provides additional guidance on what the terms "holding out," "commonly known," and "not a part of regular business" mean.

The final rule defines major swap participant as: a party that maintains a "substantial position" in any of the major swap categories, excluding positions held for hedging or mitigating commercial risk and positions maintained by certain employee benefit plans; a party whose outstanding swaps create "substantial counterparty exposure" and present systemic risk; and any "financial entity" that is "highly leveraged relative to the amount of capital such entity holds," is not subject to capital requirements established by a prudential banking regulator, and maintains a "substantial position" in any major swap category.

### *Chamber, ICI Sue CFTC to overturn Rule Requiring Dual Registration for Commodity Pool Operators:*

On April 17<sup>th</sup>, the Chamber of Commerce and the Investment Company Institute filed suit against the CFTC in the US District Court of the District of Columbia with the goal of overturning an agency rule that requires dual registration of investment company advisers already regulated by the SEC or other agencies. The rule in question, adopted in October 2011,

rescinds a 2003 exclusion that allowed some entities that would otherwise be classified as commodity pool operators to avoid CFTC registration. The CFTC recently revoked this exclusion so that it no longer applied for 40 Act Funds if they traded on a pooled basis and were also overseen by another regulator. The lawsuit is the second challenge to CFTC rules this year, with an International Swaps and Derivatives Association and the Securities Industry and Financial Markets Association challenge to position limits rules still pending.

## **CFPB**

### *Industry and Consumer Groups Team Up to Caution Against Narrow Qualified Mortgage Standard:*

On April 16<sup>th</sup>, a diverse group of over 30 organizations, spanning affordable housing groups, homebuilders, real estate professionals and others, wrote to the CFPB warning the Bureau against developing overly narrow qualified mortgage (QM) standards. The [letter](#) argues that overly prescriptive QM rules would limit the availability of mortgage credit, especially among middle- and low-income borrowers. The signees argued a narrowly defined QM standard would increase the products in the non-QM market, increasing the risk of litigation and ability to repay violations. Groups that signed onto the letter included: the American Bankers Association, the National Community Reinvestment Coalition, the National Association of Realtors, the National Housing Conference, the National Association of Home Builders, and Independent Community Bankers of America.

### *CFPB Announces Intention to “Tackle” Discriminatory Lending:*

On April 18<sup>th</sup>, the CFPB said it would begin to use its full authority to enforce the ‘disparate impact’ standard in order to ensure lending practices that may appear legitimate do not result in discrimination. Speaking on the announcement, Director Cordray said “even intentional discrimination can be difficult to identify and that consumers often do not know it is happening. But conduct that may seem benign – what the lawyers call ‘facially neutral’ actions – can create effects that are just as devastating for those marginalized communities.” The disparate impact standard was originally set by the Department of Justice in 1994 and has since been upheld in courts. The CFPB said in its [compliance bulletin](#) they will specifically look enforcement at banks and nonbanks in all the consumer credit areas it has authority over, such as mortgages, student loans, credit cards and auto loans.

### *Industry Pushed for Legislative Fix to Protect Privileged Information at CFPB:*

Despite efforts underway at the CFPB to ensure the protection of privileged information shared with the Bureau, industry associations continue to maintain the only solution is a statutory fix. While the Bureau recently announced a proposed rule to deal with this issue, a joint letter from the Clearing House Association, the American Bankers Association, the Consumer Bankers Association, and the Financial Services Roundtable industry was released this week where the associations pressed for a legislative fix, calling it the “clearest and most appropriate way to protect any privileges applicable to information provided to the Bureau.”

The House has already approved a legislative fix, H.R. 4014, which would amend the Federal Deposit Insurance Act to ensure information provided to the CFPB is protected. The measure has considerable support in both Chambers; however, it may face hurdles in the Senate as

lawmakers have objected on the grounds that other areas of the CFPB and Dodd-Frank Act should be open to amendments as well and Director Cordray has endorsed the legislation. However, it is unclear whether Congress will be able to enact the legislation in the near future.

*CFPB Planning to engage with Industry on Compliance and Supervisory Issues:*

The CFPB is planning two industry discussions to review key industry concerns such as the CFPB's plans for the future of compliance and supervision, interagency cooperation and coordination and opportunities to join the supervision team at the Bureau. The first discussion will be April 27<sup>th</sup> in Cleveland, Ohio followed by a May 4<sup>th</sup> meeting in New York City.

**White House**

*Obama Moves to Address Excessive Speculation in Oil Markets:*

On April 17<sup>th</sup>, President Obama announced a \$52 million proposal designed to strengthen federal supervision of oil markets, increase penalties for market manipulation and prod regulators to increase the amount of money energy traders must back their transactions with. Presenting the initiative in a Rose Garden address, Obama said: "We can't afford a situation where speculators artificially manipulate markets by buying up oil, creating the perception of a shortage, and driving prices higher, only to flip the oil for a quick profit." Republicans were quick to depict this as a political ploy, with presumptive nominee Mitt Romney releasing a statement hours after the President's speech charging that attacking speculators will not lower gas prices, and Speaker Boehner noting that despite all of the tools currently available to the Administration it had yet to even bring a case of illegal market manipulation.

**DOL**

*Labor Encouraging Lifetime Income Options:*

On April 16<sup>th</sup>, in remarks before the National Institute on Retirement Security, Phyllis Borzi, Assistant Secretary for the Employee Benefits Security Administration, said DOL is encouraging employers with 401(k) plans to offer more options than just lump-sum withdrawals. Borzi said DOL is hoping to "encourage people to offer various kinds of lifetime income streams, and more importantly, to encourage those workers when offered those choices ... to be willing to elect them." These options include traditional lifetime income streams, annuities or other financial products all with the end goal of decreasing the chances people will outlive their savings.

Borzi's remarks come soon after the Treasury and DOL jointly issued two proposed rules and two revenue rulings to expand retirement income solutions. On top of the February joint initiatives, DOL intends to issue guidance on lifetime income in the near future. On the recent and upcoming retirement initiatives, said Kathryn Ricard, senior vice president of retirement policy for the ERISA Industry Committee said lawmakers and regulators should be flexible when crafting these regulations, paying more attention to fixing the "problem you see now and [to] keep coming back to fix the problems that occur later."

**OCC**

*OCC Head Pledges Support to Small Business Lending*

On April 17<sup>th</sup>, in his first speech as the head of the Office of the Comptroller of the Currency, Thomas Curry promised to continue the OCC's support of small business lending through appropriate supervision. Curry stressed that small businesses are still having a harder time than larger firms in the wake of recession due to tight loan demand continue to hamper growth of community banks. Demand for credit will increase as the economic recovery strengthens; however, small national banks and federal thrifts are still recovering more slowly said Curry.

### UPCOMING HEARINGS

On Tuesday, April 24<sup>th</sup> at 10am, in 538 Dirksen, the Senate Banking, Housing and Urban Affairs Committee will hold a hearing titled "The Collapse of MF Global: Lessons Learned and Policy Implications."

On Wednesday, April 25<sup>th</sup> at 10am, in 538 Dirksen, the Senate Banking, Housing and Urban Affairs Subcommittee on Housing, Transportation, and Community Development will hold a hearing titled "Helping Responsible Homeowners Save Money Through Refinancing."

On Wednesday, April 25<sup>th</sup> at 10am, in 215 Dirksen, the Senate Finance Committee will hold a hearing titled "Tax Reform: What It Means for State and Local Tax and Fiscal Policy."

On Wednesday, April 25<sup>th</sup> at 10am, in 210 Cannon, the House Budget Committee will hold a hearing titled "Replacing the Sequester."

On Wednesday, April 25<sup>th</sup> at 10am, in 2128 Rayburn, the House Financial Services Subcommittee on Capital Markets and Government Sponsored Enterprises will hold an oversight hearing titled "Oversight of the U.S. Securities and Exchange Commission."

On Wednesday, April 25<sup>th</sup> at 10am, in 1100 Longworth, the House Ways and Means Subcommittee on Human Resources will hold a hearing titled "Moving From Unemployment Checks to Paychecks: Implementing Recent Reforms."

On Wednesday, April 25<sup>th</sup> at 2pm, in location TBD, the House Financial Services Subcommittee on Financial Institutions and Consumer Credit will hold a hearing on mobile payment services

On Thursday, April 26<sup>th</sup> at 10am, in 215 Dirksen, the Senate Finance Committee will hold a hearing titled "Tax Filing Season: Improving the Taxpayer Experience."

On Thursday, April 26<sup>th</sup> at 10am, in 2128 Rayburn, the House Financial Services Subcommittee on Financial Institutions and Consumer Credit will mark up pending legislation.

On Thursday, April 26<sup>th</sup> at 10am, in 2359 Rayburn, the House Appropriations Subcommittee on Financial Services and General Government will hold a hearing on proposed Fiscal Year 2013 Financial Services Appropriations.

On Thursday, April 26<sup>th</sup> at 2:30pm, in 342 Dirksen, the Senate Homeland Security and Governmental Affairs Subcommittee on Oversight of Government Management, the Federal Workforce and the District of Columbia will hold a hearing titled “Financial Literacy: Empowering Americans to Prevent the Next Financial Crisis.”