



## ML Strategies Update

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## Financial Services Legislative and Regulatory Update

### Leading the Past Week

The past week could be best described by one word. Chaos. In the House, a scheduled vote on the Helping Sick Americans Now Act, was abruptly pulled from the floor leaving for nearly two days of debate on a bill to protect America's Helium reserves. While last week the Senate was forced to spend the whole week on the Market Place Equity Act, without even being able to vote on amendments or final passage as non-sales tax state Senators used a variety of procedural maneuvers to extend the debate on the issue. This "legislative chaos" also consumed other matters, for example the Brown-Vitter legislation was introduced with four Republican cosponsors at the beginning of the week, however by the end of the week, two of those had withdrawn, and it looked like others were also considering withdrawing their support as well. In spite of all of this chaos, Congress was able to pass a small fix to the sequester to deal with furloughs at the FAA, which will have an immediate impact on what had been a growing problem of flight delays, and perhaps was the most visible component of the impact of the sequester. However, while the majority of the sequester's impacts continue to be seen below the surface, it is [clear](#) that there is effect on the economy. Whether Congress will choose to intervene again to put forward another fix will ultimately depend on the publicity the problem is receiving.

### Legislative Branch

#### **Senate**

#### *Brown-Vitter Officially Unveil Legislation to End "Too Big to Fail"*

On April 24<sup>th</sup>, Senator Sherrod Brown (D-OH) and Senator David Vitter (R-LA) [introduced](#) S. 798, legislation intended to eliminate the concern of "too big to fail" by making it too expensive for banks to get really big. In order to accomplish this goal the legislation would require banks with more than \$500 billion in assets to meet a minimum 15 percent capital ratio and mid-size banks to meet an 8 percent capital ratio. Furthermore, the bill requires banks to hold "pure, loss-absorbing forms of capital," and prohibits subsidiaries of bank holding companies from being able to draw on the capital of their parent bank. In addition, the legislation would limit access to deposit insurance and the Fed's discount window solely to depository institutions (which when

coupled with the Volcker rule would have a significant impact on commercial banks) as well as limit a banks' ability to shift assets and liabilities from nonbanking affiliates in order to "ensure that the safety net begins and ends at the commercial bank."

While large banking institutions have largely criticized the measure and SIFMA called the capital buffer requirements "excessive," not surprisingly the community banking industry has been laudatory of the legislation, especially because the measure contains some "regulatory relief" provisions such as broadening the definition of "rural" lenders that can offer certain products, such as balloon mortgages, and reducing impediments that small banks may face in raising capital or paying dividends. Speaking in support of the legislation, Cam Fine, President of the ICBA, told community bankers that "ICBA strongly supports this legislation" and that there is a regulatory relief section which community banks will like.

#### *Senate Delays Vote on Internet Sales Tax Legislation*

After a week's "debate" on the Senate floor, where non-sales tax state senators, including Finance Committee Chairman Baucus, and likely future Chairman Ron Wyden, prevented both the consideration of amendments, as well as a vote on the underlying bill, the Senate was finally able to vote for cloture and an agreement was reached that final passage would occur on May 6<sup>th</sup>. Interestingly, the final vote for cloture saw 11 Senators switch their votes, as it barely passed the sixty vote threshold (63-30). Although many practical concerns about the legislation were raised against the bill, the majority of the opposition appears to be driven by how the Marketplace Fairness Act (S. 743) would impact small businesses. A point even made by proponents of the legislation, as Bill Hughes, Senior Vice President for Government Affairs at the Retail Industry Leaders Alliance, praised the vote for closure by saying it was "proof that the special treatment of big online businesses at the expense of retailers on Main Street will soon be a thing of the past." Still, opponents of the legislation, ranging from conservatives, members of Congress from non-sales tax states and even large financial institutions worries that this legislation could facilitate state-based transaction taxes, now look to the House, where it is expected to face an uphill battle as it works its way through regular order.

#### *Senate Banking Grills Cordray on CFPB Data Collection in Semi-Annual Review Hearing*

On April 23<sup>rd</sup>, the Senate Banking Committee met to hear testimony from CFPB Director Richard Cordray as part of the Bureau's semi-annual report to Congress. In addition to issues now too common to CFPB oversight hearings, such as the leadership structure of the Bureau, the appropriations process and the Bureau's accountability to prudential regulators and Congress, Senators also focused on recent reports about the CFPB's foray into big data collection. In response to questioning from Ranking Member Crapo (R-ID) about the nature and the use of the data being collected, Director Cordray told lawmakers that the Bureau has no interest in "watching consumers," and that the information is anonymous and necessary for the CFPB to have an understanding of consumers in order to come up with thoughtful regulations expected by Congress.

In addition to extensive discussion of data collection, Mr. Cordray touched on the Bureau's recent mortgage servicer rulemakings, student loan efforts, auto lender findings, and the Bureau's initial enforcement actions against bad actors in the credit card space. Notably, while the Director of the CFPB is required to appear to give the semi-annual report before both the Senate Banking and House Financial Services Committees, Chairman of the House Committee Jeb Hensarling (R-TX) wrote to Cordray to say he will not receive testimony from Cordray as he is not "validly appointed" as Director. Ranking Member Waters (D-CA) quickly pushed back against Hensarling's position on Cordray, saying she will fight to have Cordray appear before the

Committee. Per a [letter](#) to Hensarling on April 23<sup>rd</sup>, Waters told the Chairman that “no court has addressed the legitimacy of the president’s appointment of Director Cordray” and that he has no ground to argue the appointment is invalid.

#### *Senate Republicans Unveil Pension Plan Disclosure Legislation*

On April 23<sup>rd</sup>, Senators Richard Burr (R-NC), John Thune (R-SD), and Tom Coburn (R-OK) introduced the Public Employee Pension Transparency Act (S. 779), which would require public pension plans to disclose to the Treasury Department the methods and assumptions they use to calculate debt, assets, and liabilities. In the House, Representatives Devin Nunes (R-CA), Paul Ryan (R-WI), and Darrell Issa (R-CA) have introduced companion legislation, H.R. 1628. Under the legislation, if the pension plans do not meet the disclosure requirements, they would lose their tax exempt status for certain bonds issued by states and municipalities. The legislation also states that the Federal government will not bail out any current or future shortfall in a state or locality’s pension plan.

#### *Senate Democrats Urge Appellate Court to Reverse Lower Courts on CFTC Position Limits Rule*

On April 22<sup>nd</sup>, nineteen Senate Democrats led by Senator Carl Levin (D-MI) filed a [brief](#) with the U.S. Circuit Court of Appeals for the District of Columbia, calling on the court to reverse a lower court decision invalidating proposed federal regulations limiting speculation on 28 commodities, including crude oil, natural gas, and gasoline. The lawmakers’ letter argues that speculation in these commodities has led to rising prices, which have hurt consumers. The CFTC was directed by the Dodd-Frank Act to propose position limits to address excessive speculation.

### **House of Representatives**

#### *Waters Introduces Legislation to Authorize User-Fees for Investment Adviser Oversight*

On April 19<sup>th</sup>, Ranking Member of the House Financial Services Committee Maxine Waters (D-CA) introduced the Investment Adviser Examination Improvement Act of 2013 ([H.R. 1627](#)). The legislation would give the SEC authority to impose and collect user fees on investment advisors. In a press release announcing the bill, Waters said that, currently, the SEC is only able to conduct exams for about 8 percent of the 11,000 registered advisers. Waters introduced similar legislation in the 112<sup>th</sup> Congress amid conversations over how to proceed with investment adviser oversight. Other proposals considered last Congress included creating a self-regulatory organization (SRO) to oversee advisers, or placing authority in an existing SRO, such as FINRA. Regardless, the SEC has stressed that it continues to have insufficient examination resources and the President’s FY 2014 Budget calls for the agency to add up to 250 new examiners.

#### *Administration Talks to Congress about International Priorities*

On April 24<sup>th</sup>, Treasury Secretary Lew went before the House Appropriations Subcommittee on State, Foreign Operations, and Related Programs to underscore the importance of the Administration’s international priorities. The President’s FY 2014 Budget request includes \$2.89 billion for U.S. investment in multilateral development banks and an increased commitment to the IMF’s quota. In total, the request is \$220 million higher than the FY 2013 continuing resolution spending levels. Lew told lawmakers that “support for the international financial institutions is one of the most cost-effective ways to confront our economic challenges at a time of constrained resources.” Chairman of the Subcommittee, Representative Kay Granger (R-TX), pushed back against additional U.S. commitment to the IMF, saying that the IMF was not created “to bail out industrialized nations that cannot control their spending.”

The same day, the House Financial Services Subcommittee on Monetary Policy and Trade met to hear testimony from Treasury Under Secretary for International Affairs Lael Brainard on the U.S.'s role in the IMF in light of the President's FY 2014 Budget request which included to governance reforms at the IMF and increases the U.S. quota share by about \$63 billion. In response to concerns that taxpayers could sustain losses, Brainard sought to assure the Subcommittee that taxpayers are insulated from any default on loans made by the IMF and that any loss to the U.S. taxpayer would be "difficult because of a number of safeguards."

#### *House Financial Services Committee Examines Impediments to Private Capital in Housing Finance*

On April 24<sup>th</sup>, the House Financial Services Committee met to hear testimony on the effect that the government's role has played in the deployment of private investment capital in the housing finance sector and the secondary mortgage market. Witnesses including, Chris Katopis, Executive Director of the Association of Mortgage Investors; Martin Hughes, President and CEO of Redwood Trust, Inc.; and James Millstein, Chairman and CEO of Millstein & Co, told lawmakers that there is no shortage of private capital but that investors feel crowded out by government-subsidized rates. Millstein told the Committee that until Congress and the Administration "clarify the fate of Fannie Mae and Freddie Mac, the fate of the housing market will remain uncertain for private investors." Witnesses stressed that as part of this clarification, lawmakers should consider structural changes to the mortgage market to provide greater investor protections through standardization, transparency, and enforcement. Notably, Chairman Hensarling (R-TX) sought to tie housing financing reform to Dodd-Frank Act technical fixes, including critiquing the CFPB's ability-to-repay and qualified mortgage (QM) rules as evidence that the financial reforms need improvement to ensure that taxpayers are not the "foundation" of the housing sector.

#### *House Ways and Means Examines Tax Reform and Residential Real Estate*

On April 25<sup>th</sup>, the House Ways and Means Committee met to discuss tax reform related to the housing market and home ownership, including potential changes to the home mortgage interest deduction. The hearing featured testimony from both economists and representatives from the real estate industry. During the hearing, Chairman Dave Camp (R-MI) signaled he was considering a potential transition to a new, unspecified homeownership incentive system and exploring other changes to the popular tax provision. However, others on the committee, including Representative Sander Levin (D-MI), called for caution, noting that many of his constituents have second, yet relatively inexpensive second homes. During the hearing it was disclosed that in 2012, 34 million households claimed a mortgage interest deduction, costing the federal government a total of \$68 billion, with 75% going to households making more than \$100,000 a year. President Obama has proposed limiting the deduction by granting everyone the deduction they would receive in the 28% income tax bracket.

#### *House Ways and Means Advanced Debt Limit Prioritization Legislation*

On April 24<sup>th</sup>, the House Ways and Means Committee voted along party lines, 22 to 14, to advance the Full Faith and Credit Act ([H.R. 807](#)) legislation intended to direct the Treasury to prioritize payment of principal and interest on the debt, in addition to Social Security payments, over all other government spending obligations, should the debt ceiling be reached.

#### *House Oversight Democrats Introduce IFR Monitor Legislation*

As lawmakers continue to probe into the controversial Independent Foreclosure Review (IFR) settlement between Federal regulators and large U.S. banks, Representatives Elijah Cummings (D-MD) and Maxine Waters (D-CA) introduced legislation to create an independent monitor to oversee the settlement. The [Mortgage Settlement Monitoring Act of 2013](#), would require the

independent body to issue reports on the \$9.3 billion settlement reached between 13 large mortgage servicers, the OCC and the Fed and detail banks determined how direct payments would be made and whether banks were writing down principal in harder hit communities or in wealthier communities to fulfill the settlement's terms faster.

#### *Representative Slaughter Seeking Stronger Political Intelligence Rules*

Following significant media attention over the past few weeks about the impact on the market associated with the notice of an increase in Medicare Advantage Rates to a political intelligence firm, Height Securities, Representative Louise Slaughter (D-NY) announced plans to introduce strengthened political intelligence legislation. Slaughter will introduce the legislation with Senator Chuck Grassley (R-IA) to require political intelligence forms to follow a disclosure method similar to registered lobbyists. The two had worked together in the past to get the STOCK Act passed, although a similar provision dealing with registrations for political intelligence firms was stripped out at the last moment.

#### Executive Branch

##### **Federal Reserve**

#### *European Regulators Push Back Against Proposed Enhanced Oversight of Foreign Banks*

Last week, Michele Barnier, European Commissioner for Internal Market and Services, wrote to Federal Reserve Chairman Ben Bernanke criticizing portions of the Fed's [plan](#) for enhanced prudential standards for foreign banks. Barnier's [letter](#) states that the proposal to require higher capital requirements on U.S. subsidiaries of foreign banks could lead to "fragmentation of global banking markets," drive up costs at European banks, and place foreign banks at a competitive disadvantage to their American counterparts. The Fed's proposal is facing pressure from many stakeholders. Barnier's comments follow a [letter](#) from the European Banking Federation, urging the U.S. central bank to rethink the potential impact on cross-border banking activities. In response to Barnier and other critics, a Fed spokesperson defended the proposal, saying that the Fed will carefully consider comments but that the new regulatory framework is intended to address "new risks, create a more consistent regulatory structure for all firms operating in the United States, and promote U.S. financial stability, which is essential for global financial stability."

##### **Treasury**

#### *FSOC Close to SIFI Designations; Releases Annual Report*

In remarks prepared for last week's FSOC meeting, Treasury Secretary Lew said that the Council is close to a decision on what non-banks will be deemed systemically important and subject to additional Federal oversight. "It is critically important that the Council take the time to get the analysis right," said Lew and they "expect to vote on designations of an initial set of non-bank financial companies soon." The same day, Senators Jon Tester (D-MT) and Mike Johanns (R-NE) wrote to Lew, calling on the FSOC to release the SIFI designations for public comments. The letter also encouraged the FDOC to differentiate among industries and to release the metrics used to evaluate the non-banks designated as systemically significant.

At the same meeting, the FSOC released its [annual report](#) highlighting housing finance, cybersecurity, and interest rate benchmarks as issues in need of regulatory action. Specifically, the FSOC recommended that the SEC take additional action to reform the regulation of money market mutual funds and that regulators overhaul the oversight of LIBOR. Speaking at the meeting, SEC Chairman White said that she expects SEC staff will have recommendation "in the near future" that reflect "significant progress" on the treatment of Money Market Funds.

### *SIGTARP Warns Too Big to Fail Still A Reality*

Following on growing rhetoric in government about the need to curtail “too big to fail” banks, on April 24<sup>th</sup> the Special Inspector General for the Troubled Asset Relief Program sent a [report](#) sent to Congress warning that “too big to fail” financial institutions remain a concern and that the government should consider aggressively exercising new orderly liquidation powers in the event of future failures. The report also recommended that regulators be strict in ensuring that living wills submitted by banks have a clear liquidation plan for immediate changes. “To let one of the largest financial firms fail requires regulators to have confidence that they can close down the firm without damaging the economy, and as a nation we are not there yet,” said SIGTARP report. In addition to concerns over ‘too big to fail’ firms and liquidation authority, the report highlighted increases in the number of Home Affordable Modification Program (HAMP) re-defaults, recommending that Treasury work with servicers to develop a warning system to predict missed payments.

### **CFPB**

#### *CFPB Releases Report Highlighting Potential Consumer Abuses in Payday and Deposit Advance Loans*

On April 24<sup>th</sup>, the CFPB released a [report](#) on payday and deposit advance loans finding that loose lending standards, high costs, and risky loan structures may contribute to the sustained use and indebtedness. The report details that payday and deposit advance loans are offered by a small, but growing, number of institutions and are characterized by their small dollar amounts, short repayment schedules, and the requirement that the borrower repay the full amount or give lenders access to repayment through a claim on the borrower’s deposit account. Other key features of these financial instruments are a lack of consideration for a borrower’s ability-to-repay, risky loan structures, and the ease at which these loans become expensive long-term loans. The CFPB noted in a release on the report that it has the authority to examine deposit advance loans at the banks and credit unions it supervises and that the Bureau will continue to analyze the growing online presence of such businesses.

#### *Bureau Issues Proposed Rule to Governing Civil Penalty Fund*

On April 26<sup>th</sup>, the CFPB issued a [proposed rule](#) to establish procedures for the Civil Penalty Fund, which is being created to compensate victims harmed by a person or company that was fined in an enforcement action brought by the Bureau. Under the rule, money in the Civil Penalty Fund will be used to provide compensation to victims in an amount determined by the Bureau. The CFPB also issued a [notice of proposed rulemaking](#) seeking public comment on the management of the Fund.

#### *Bureau Announces Several High Level Staffing Changes*

Last week, the CFPB [announced](#) several personnel changes at the Bureau. Notably, Catherine Galicia, former Senior Counsel on the Banking Committee will serve as Assistant Director for Legislative Affairs. In addition to Galicia, Dan Smith will serve as the Bureau’s first Assistant Director for the Office of Financial Institutions and Business Liaison. Formerly, Smith has served as the Director for Industry and State Relations at Freddie Mac. Interestingly both Galicia and Smith had previously worked as lobbyists in the financial services industry, though not immediately before joining the CFPB. Other staffing changes include Lisa Konwinski, who will serve as the Deputy Associate Director for External Affairs, and Hubert “Skip” Humphrey who will transition from his role as Assistant Director in the Office of Older Americans to remain with the Bureau as a Senior Liaison Officer in charge of building relationships with state, local, public and private organizations.

### **SEC**

### *Chairman White Announces Co-Directors for Office of Enforcement, General Counsel*

SEC Chairman Mary Jo White [announced](#) appointments to the SEC Office of Enforcement on April 22<sup>nd</sup>. White's former colleague Andrew Ceresney and current acting-Enforcement Director George Canellos will serve as co-Directors of the Enforcement Office. Canellos has been serving as acting-Director since January 2013 and also served with both White and Ceresney as Federal prosecutors. White and Ceresney worked together when she headed the Manhattan Attorney's office and at her law firm Debevoise & Plimpton. In addition, Anne Small, Special Assistant to the President and Associate Counsel to the President with the White House Counsel's Office, [has been named](#) as the SEC's General Counsel. Small previously worked at the SEC as Deputy General Counsel for Litigation and Adjudication, helping to oversee enforcement matters, appellate cases, and adjudications.

### *SEC Pressured to Require Disclosure of Corporate Political Contributions*

Last week, a number of Democratic elected officials petitioned the SEC to release a rule which would force publically traded coalitions to disclose to shareholders all their political donations. While the SEC had indicated would be proposed near the end of April, the petition to release the rule has already reached almost 500,000 comments, surpassing all other petitions in the agency's history. In response to growing pressure for a new disclosure rule, House Republicans introduced [H.R. 1626](#), which would prohibit the SEC from issuing rules requiring the disclosure of an issuer's expenditures for political activities. In response, Senate and House Democrats have introduced legislation directing the SEC to require shareholder authorization before a public company may make certain political expenditures (S. 824/H.R. 1734). Stakeholders have noted that the newly confirmed Chairman Mary Jo White will likely be the deciding factor on whether the Commission proceeds with a new rule.

## **CFTC**

### *O'Malia Favors Delay to Cross-Border Derivatives Requirements*

In remarks at the Federal Reserve Bank of New York, Commissioner Scott O'Malia said that it "makes sense" for the CFTC to extend the July 12<sup>th</sup> deadline for when the Commission's derivatives rules begin applying to cross-border transactions. The delay would allow Commissioners to continue to debate what changers should be made to the proposed guidance for cross-border transactions as there is still "no draft final guidance before the Commission." Due to the complexity of the issue, O'Malia stressed that it is perfectly reasonable to suspect the CFTC could miss the July deadline.

## **FDIC**

### *FDIC and OCC Release Guidance to Small Institutions Offering Deposit Advance Products*

On April 25<sup>th</sup>, following the CFPB's report on payday and deposit advance lending, the [FDIC](#) and [OCC](#) released guidance for banks offering advance deposit loans to help ensure that banks are aware of a variety of safety and soundness, compliance, and consumer protection risks posed by deposit advance loans. The guidance highlights a number of supervisory concerns including safety and soundness risk, such as credit risk, third-party risk, and legal risk and compliance and consumer protection concerns. The regulators note that they will continue to closely review the activities of banks that offer or propose to offer deposit advance products, through direct examination of the bank, examination of any third party participating in such transactions under an arrangement with the bank, and review of any licensing proposals involving this activity. The also CFPB has authority to oversee the payday loan market within institutions with more than \$10 billion in assets.

## **International**

### *EU Continues to Debate Merits of Transaction Tax*

Last week, eleven European Union nations sought assurance from the European Commission that their planned financial transaction tax will not increase borrowing costs. In an April 16<sup>th</sup> [document](#) prepared by Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia, and Slovakia, the countries request that the Commission provide data about the potential impact of the transactions tax on repurchase agreements and the “funding cost of the central government and the real economy.” The EU countries estimate that the tax could raise from €30 to €35 billion per year but must still address concerns that the plan could harm the repo market that enables low government borrowing costs through risk hedging. The Treasury has opposed the EU’s attempts to levy a transactions tax, with Treasury Secretary Lew pressing the issue with his European counterparts last month.

### Upcoming Hearings

*The Senate and House will be in Recess this week.*

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