



## ML Strategies Update

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## Financial Services Legislative and Regulatory Update

### Leading the Past Week

Clearly the leading news last week was the Supreme Court's decision holding the Defense of Marriage Act unconstitutional. Additionally, the Senate moved forward, albeit without securing 70 votes, for comprehensive immigration reform. The final passage was 68-32 and now the attention on immigration reform turns to the House, where the Senate passed bill faces [some challenges](#) to becoming law.

This past week the Senate Banking Committee held a hearing on five different nominations including Congressman Mel Watt to be Director of the Federal Housing Finance Authority. This hearing came on the heels of the introduction of a broad, bipartisan bill to reform Fannie and Freddie. It also foretold that, despite how much attention is being paid to how July will be consumed by a nominations fight on the Senate floor, the major policy initiative for the month will focus on housing finance reform. Whether Watt is confirmed by the end of the month, and it is unclear whether he will get through on that timeline or at all, it is our sense that both the House Financial Services Committee and the Senate Banking Committee will spend considerable amount of time focusing on GSE reform and FHFA reform (respectively).

Also facing the Congress when it returns from the July 4<sup>th</sup> recess is how to deal with the Student Loan issue, as the interest rate on new federally issued subsidized student loans are set to double today, from 3.4% to 6.8%.. All of these issues make it look like it is going to be a very busy July in Washington, DC.

### Legislative Branch

#### **Senate**

##### *Corker and Warner Unveil Fannie and Freddie Reform Bill*

On June 25<sup>th</sup>, Senators Bob Corker (R-TN) and Mark Warner (D-VA) introduced the Housing Finance Reform and Taxpayer Protection Act, a bill which would phase out Fannie Mae and Freddie Mac and seeks to insulate the taxpayer against future losses to the housing market. The

[bill](#) establishes a new agency, the Federal Mortgage Insurance Corp. (FMIC), which would replace the Federal Housing Finance Agency (FHFA) within one year of passage. The FMIC would back certain mortgage bonds issued by approved private firms and would only provide backstop insurance after a substantial amount of private capital is exhausted. The legislation also eliminated the affordable housing mandate of Fannie and Freddie, instead creating a Market Access Fund, funded through fees, to maintain access to affordable housing options. A summary of the legislation can be found [here](#).

It is worth noting that shortly after its introduction, Chairman of the Banking Committee Tim Johnson (D-SD) thanked Warner and Corker for their efforts and said that the Committee will begin considering reforms after it deals with separate legislation to bolster the Federal Housing Administration. On the House side, Chairman of the Financial Services Committee Jeb Hensarling has said he prefers a wholly privatized system with no government backstop. Hensarling is expected to introduce a plan to reform Fannie and Freddie before the August recess.

#### *Senate Banking Committee Considers Nomination of Mel Watt, Others*

On June 27<sup>th</sup>, the Senate Banking Committee met to consider the nominations of Representative Mel Watt to be Director of the FHFA, Jason Furman to be the Director of the Council of Economic Advisors, Kara Stein and Michael Piwowar to be SEC Commissioners, and Richard Metsger to be a Board Member of the National Credit Union Administration. Most questions were directed to Representative Watt (D-NC), as Republican Senators expressed skepticism about whether he possesses the required expertise and if he is too political for the position. In addition to defending his qualifications, Representative Watt committed to transitioning the housing finance system to one that is based on private capital with minimizes taxpayer risk. He also said that Fannie and Freddie should only finance QM loans, that he would consider principle reductions policy if asked, and that he would not endorse local government use of eminent domain to seize underwater mortgages. In one of the few questions they received, Kara Stein and Michael Piwowar both endorsed new SEC policies to move away from “neither admit nor deny” in settlement cases.

#### *Senate Banking Committee Holds Hearing on Private Student Loans*

On June 25<sup>th</sup>, the Senate Banking Committee met to conduct a hearing titled “Private Student Loans: Regulatory Perspective.” In their testimony, federal regulators called on banks to offer refinancing options for borrowers that may be struggling to pay off their student debt. While private loans make up a small percentage of overall student debt, witnesses said, their delinquency rates are much higher than those for federal loans, largely because private loans have less flexible terms and higher interest rates. One witness, CFPB Assistant Director Rohit Chopra, warned that growing levels of student debt and rising default rates could pose risks to the broader economy, drawing parallels to the recent mortgage bubble. In his opening statement, Committee Chairman Tim Johnson (D-SD) urged regulators to closely monitor growth in private loan markets that may come should federal student loan rates double on July 1<sup>st</sup>. Other witnesses at the hearing included: John Lyons, Senior Deputy Comptroller for Bank Supervisions Policy at the OCC; Todd Vermilyea, Senior Associate Director at the Fed’s Division of Banking Supervision and Regulation; and Doreen Eberly, Director of Risk Management Supervision at the FDIC.

#### *Warren Prods Sallie Mae on Private Student Loans*

In a [letter](#) sent June 24<sup>th</sup>, Senator Warren wrote to the acting FHFA Director Ed DeMarco requesting information on why Sallie Mae has been able to use a line of credit from the Federal Home Loan Banks (FHLB) estimated at a .23 percent interest rate and then make loans with

rates 25 to 40 percent higher. Warren cautioned that the government sponsorship of FHLB and Sallie Mae “was intended to bolster the banks’ support for the housing market — not be a backdoor way to subsidize highly profitable private student lenders.” Sallie Mae [responded](#) that they receive “virtually all” of its funding for private student loans from Sallie Mae bank, a Utah based subsidiary and that FHLB funds are only used for previously originated Federal Family Education Loan Program loans.

#### *Senate Agriculture Schedules First CFTC Reauthorization Hearing*

On July 17<sup>th</sup>, the Senate Agriculture Committee will hold its first hearing to consider the CFTC’s reauthorization. In conjunction with scheduling the hearing, the Committee published recommendation letters from industry stakeholders and companies on how the Committee should proceed with the reauthorization. While the House has already begun hearing on the Commission’s reauthorization it is unclear if the failure of the Farm Bill will affect timing. The CFTC’s authorization expires in September, but the agency will be able to continue to operate without it.

### **House of Representatives**

#### *House Financial Services Committee Considers Dodd-Frank and Too Big to Fail*

On June 26<sup>th</sup>, the House Financial Services Committee held a hearing examining Title I and Title II of the Dodd-Frank Act to consider whether these provisions achieve their objective of eliminating the need of taxpayer-funded support of large, complex financial institutions. Witnesses included several noted critics of Wall Street, including: FDIC Vice Chairman Thomas Hoenig, Federal Reserve Bank of Dallas President Richard Fisher, Federal Reserve Bank of Richmond President Jeffrey Lacker, and former FDIC Chairman Sheila Bair.

When asked if Dodd-Frank was successful in ending “too big to fail,” Fisher and Lacker both said it had not while Hoenig and Bair said the law provides the tools which will eventually help end the problem. The panel also expressed support for legislation introduced by Senators Sherrod Brown (D-OH) and David Vitter (R-LA) and similar legislation introduced by Representative John Campbell (R-CA) which would impose even greater capital requirements, with Hoenig saying he believes large banks remain “woefully undercapitalized.” While witnesses may have been skeptical, and Chairman Jeb Hensarling (R-TX) expressed belief that Dodd-Frank “codified” too big to fail, Democrats, including Ranking Member Maxine Waters (D-CA) and Representative Carolyn Maloney (D-NY) said the law prohibits the bailouts which characterized the financial crisis.

#### *Ranking Member Waters Continues Panel Series on Future Of the Mortgage Market*

On June 28<sup>th</sup>, Ranking Member of the Financial Services Committee held the second in a series of Minority Panel Discussions on the future of government sponsored entities (GSEs) and the secondary mortgage market. The panel, which discussed sustainable solutions for housing finance reform, featured speakers from the Credit Union National Association (CUNA), the National Association of Realtors, the Independent Community Bankers of America, the Mortgage Bankers Association, the National Multi Housing Council, and the American Securitization Forum. The first panel discussion in the series was in April and covered providing safe and affordable rental and homeownership options and preventing another conservatorship.

#### *House Financial Services Subcommittee Examines HUD’s Moving to Work Program*

On June 26<sup>th</sup>, the House Financial Services Subcommittee on Housing and Insurance met to consider Department of Housing and Urban Development’s (HUD) Moving to Work program. Witnesses, who included representatives of local housing authorities and Matthew Scire, Director of the GAO’s Financial Markets and Community Investment Office, told lawmakers that the

program has been successful in allowing public housing authorities the opportunity to design and test innovative, local strategies aimed at helping residents find employment and become independent. In particular, Subcommittee Vice Chairman Blaine Luetkemeyer (R-MO) called the program an important tool and noted that the Obama Administration has recognized the successes of the program and has publicly called for its ‘substantial expansion.’”

### Executive Branch

#### **Federal Reserve**

##### *Fed Proposes Rule to Gather More Money Market Information*

On June 25<sup>th</sup>, the Federal Reserve proposed a rule that would broaden information it collects on money market instruments. Under the proposal, insured depository institutions with at least \$26 billion in assets and U.S. branches of foreign banks with at least \$900 million in assets would be required to give the Fed daily reports on federal funds transactions, certificates of deposit, and Eurodollar trades. Reports must include the amount, maturity, and interest rate for each transaction. The data would be used by the Fed to help monitor money market conditions, including by calculating average rates across products and tracking trends in aggregate transaction levels. The comment period for the proposal will be open for 60 days.

##### *Fed Will Finalize Basel III Requirements This Week*

The Federal Reserve announced last week that it will hold an open board meeting on July 2<sup>nd</sup> to finalize Basel III capital requirements. The rule, which was first proposed in June 2012 to establish minimum capital requirements for large and small banks, has drawn a significant amount of industry criticism from various stakeholders. In particular, community banks and lawmakers have been vocal in the need for a less stringent, simpler framework for small community banks while other have pushed for additional requirements for the largest banks, including a focus on the leverage ratios.

#### **CFTC**

##### *As Deadline Approaches, Future of Cross-Border Rule Murky As Stakeholders Push for Delay*

As the July 12th deadline for the CFTC’s cross-border regulations quickly approached, last week there was significant discussion of delaying the rules so that they may be significantly overhauled. Negotiations around the cross-border rule, which will govern how U.S. derivatives laws apply to foreign banks, have been simmering for a while, but came into the spotlight on June 25<sup>th</sup> when Commissioner Wetjen indicated he would favor the Commission adopting “interim final guidance” which could continue to be adjusted to reflect industry guidance rather than pushing forward with a final rule. Chairman Gensler, speaking at a Senate Appropriations Subcommittee hearing the same day, pushed back against Wetjen’s proposal, saying the interim final guidance would be the same as a delay and this rule has percolated long enough. Although Gensler has been adamant that the CFTC will finalize guidance by the July 12th deadline, the two Republican Commissioners Jill Sommers and Scott O’Malia have both indicated that they favor a delay.

Those Commissioners at the CFTC are not the only ones who would like to see the rule delayed, as 35 House Democrats wrote to Chairman Gensler and SEC Chair Mary Jo White, urging Gensler to delay the rule and take time to coordinate with the SEC and foreign regulators. The House letter follows on the heels of a letter to Treasury Secretary Jacob Lew sent by six Senate Democrats calling for the CFTC to delay implementation of new cross-border derivative rules, saying CFTC and SEC need to reconcile conflicting policies on how these rules will be applied to banks operating abroad. The letter was signed by Senators Chuck Schumer (D-NY), Kristen Gillibrand (D-NY), Tom Carper (D-DE), Kay Hagan (D-NC), Michael Bennet (D-CO), and Heidi Heitkamp (D-ND).

### *Corzine Reported to be Facing Charges From CFTC*

On June 27<sup>th</sup>, the CFTC [announced](#) that it is suing Jon Corzine, former CEO of MF Global, over the firm's collapse, linking Corzine to the disappearance of over \$1 billion in customer funds during the company's bankruptcy. If found liable as a result of the lawsuit, Corzine could face a ban from participation in the commodity trading in addition to heavy fines. In addition, the case is being said to not give Corzine the opportunity to settle, which could result in a lengthy court battle. A lawyer for Corzine has called the charges "meritless."

### *DC Court of Appeals Upholds CFTC Registration Rules, Cost-Benefit Analyses*

On June 25<sup>th</sup>, the U.S. Court of Appeals for the DC Circuit [upheld](#) CFTC rules requiring that certain advisors to mutual funds and exchange-traded funds register with the CFTC if their commodity trades exceed certain limits. The court reaffirmed an earlier ruling rejecting a suit brought by the Investment Company Institute and the Chamber of Commerce who argued that the rules were redundant and should be thrown out because they were based on a faulty cost-benefit analysis. This ruling is seen as a victory for regulators implementing Dodd-Frank reforms, as cost-benefit analyses used in rulemaking are a popular target for groups seeking to overturn new financial rules in court.

## **CFPB**

### *Bureau Issues Proposed Changes to Mortgage Rules*

On June 24<sup>th</sup>, the CFPB issued [proposed clarifications](#) and slight revisions to its January 2013 mortgage rules. The revisions come as a result of feedback from the industry as to how to implement the new mortgage policies outlined in the January proposal. The changes include:

- Laying out procedures to obtain follow up information on loss-mitigation applications
- Facilitating mortgage servicers' offering of short-term forbearance plans
- Clarifying the financing of credit insurance premiums
- Clarifying the definition of a loan originator
- Revising the effective dates of the loan originator rule and the ban on financing of credit insurance

These changes affect the Ability-to-Repay rule, the mortgage serving rule, and loan originator compensation rule. Comments on the proposed clarifications are due on or before July 22<sup>nd</sup>.

### *CFPB Issues Final Nonbank Oversight Rule*

On June 26<sup>th</sup>, the CFPB finalized a [rule](#) outlining procedures it will use to designate nonbanks for supervision and policies the CFPB will follow to give nonbanks in question a reasonable notice. The Dodd-Frank Act directs the CFPB to supervise nonbanks if they pose risks to consumers. The CFPB notes the rule is not substantive, nor required by the Dodd-Frank Act, and is meant to be a transparent preview of how it intends to use its nonbank authority.

### *SCOTUS to Hear NLRB Recess Appointments Case*

On June 24<sup>th</sup>, the Supreme Court [announced](#) it would consider *Noel Canning v. National Labor Relations Board* which considers whether the President's recess appointment power is valid during a recess that is within a session of the Senate. The Court's decision will likely have major implications for the CFPB as, should the Court rule that the appointments are unconstitutional, Director Cordray's validity will come into greater question. While the NLRB decision would not have immediate implications for the CFPB, it would greatly add to the momentum for the Bureau's critics who could seek to bring a similar case against the agency. However, with Cordray's term expiring at the end of the year, and his re-nomination up in the air, it is possible that the Bureau could be once again without a director before the Supreme Court even rules on the NLRB case. Without a director, the CFPB cannot supervise and regulate nonbanks.

## SEC

### *Court Will Not Issue Stay on Critical Minerals Disclosure Rule*

On June 28<sup>th</sup>, the U.S. Court of Appeals for the District of Columbia declined a request by the American Petroleum Institute (API) and Chamber of Commerce to keep its case open while similar litigation works its way through the district court. Since the losing party at the district level is expected to appeal, API had argued to keep the case open at the Appellate level since the three judge panel was already familiar with the case. The Courts decision this week means that both sides would have to brief an appeal, thus potentially elongating the time period to appellate resolution is achieved. At issue in the case is a Dodd-Frank rule which requires energy and mining companies to disclose payments made to foreign governments.

## International

### *FSB Intends to Name Globally Systemically Important Insurers in July*

On June 24<sup>th</sup>, the Financial Stability Board (FSB) **announced** that in July it will release an initial list of global systemically important insurers (G-SIIs) which will have to undergo additional regulatory and capital requirements, new recovery and resolution standards, and increased group-wide supervision. In addition, the FSB noted that it plans to put forth “straightforward, backstop capital requirements” which will apply to G-SIIs, and their non-insurance subsidiaries, in time for the G20 summit in November 2014.

### *European Commission Financial Transaction Tax Delayed – Legislation Introduced to Nullify it in US*

Despite being intended to enter into force on January 1<sup>st</sup>, a proposal by the European Commission (EC) to tax financial transactions has been delayed by at least an additional six months as EU countries fail to agree on the terms of the new levy. In an update to the Commission’s website, the EC projects that, “if agreement is found before the end of 2013,” and a speedy transition were undertaken by member states, then “this common framework for an FTT could still enter into force towards the middle of 2014.” The news that the FTT will be delayed in Europe comes as Senator Pat Roberts (R-KS) introduced legislation which would block foreign government from collecting taxes on securities transactions by barring the Treasury Secretary from assisting any foreign government in collection of such a tax. Representative Price (R-GA) introduced a companion measure in the House.

## Upcoming Hearings

*The Senate and House will be in Recess for the July 4<sup>th</sup> Holiday.*

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