

# ISSUE BRIEF

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## Financial Regulatory Reform in the House and Senate: A Brief Comparison

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The House passed the Financial CHOICE Act (H.R. 10) in June 2017. The CHOICE Act is a comprehensive financial regulatory reform bill that would replace large parts of the 2010 Dodd–Frank Act. The Senate has not yet passed its own reform bill, but the Senate Banking Committee recently passed the Economic Growth, Regulatory Relief, and Consumer Protection Act (S. 2155) with votes from four Democratic members of the committee.<sup>1</sup> S. 2155 is a more targeted financial-reform bill than the CHOICE Act, but it includes similar versions of approximately 15 CHOICE Act provisions.

A cornerstone of the CHOICE Act is a regulatory off-ramp, a provision that provides regulatory relief to all banks that choose to maintain a higher equity–capital ratio than currently required. Although S. 2155 does not include as broad a regulatory off-ramp as the CHOICE Act, it does include a limited off-ramp for some smaller banks. If Congress can enact a properly designed off-ramp, it will provide significant regulatory relief for financial institutions, help restore market discipline, and move U.S. financial markets in the right direction. This *Issue Brief* provides an overview of the major features of the CHOICE Act and S. 2155.<sup>2</sup>

### Main CHOICE Act Provisions

The core elements of the CHOICE Act represent a major regulatory improvement because they help restore market discipline while reducing regulatory burdens. The bill replaces harmful portions of the Dodd–Frank Act, implements many capital market improvements, and makes several positive changes to the Federal Reserve. The major money and banking components of the CHOICE Act are as follows.

**Providing a Regulatory Off-Ramp.** The regulatory off-ramp (capital election) in Title VI of the CHOICE Act provides regulatory relief to all banks that choose to maintain a higher equity–capital ratio, thus improving their ability to absorb losses, and reducing the likelihood of taxpayer bailouts. Qualifying banks would be exempt from, among other regulations, any federal law, rule, or regulation addressing capital or liquidity requirements, and any of the “heightened prudential standards” implemented by section 165 of Dodd–Frank.

**Repurposing the Financial Stability Oversight Council (FSOC).** Title II of the CHOICE Act takes a major step toward fixing the damage caused by Title I of Dodd–Frank, the section that created the FSOC, a sort of super-regulator tasked with singling out firms for especially stringent regulation. The CHOICE Act effectively transforms the FSOC into a regulatory council for sharing information.

**Replacing Orderly Liquidation with Bankruptcy.** Title II of the CHOICE Act repeals Dodd–Frank’s orderly liquidation authority (OLA) and amends the bankruptcy code so that large financial firms can credibly use the bankruptcy process.

**Repealing the Volcker Rule.** Title IX of the CHOICE Act repeals Section 619 of Dodd–Frank,

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otherwise known as the Volcker rule. The Volcker rule supposedly protects taxpayers by heavily regulating banks' proprietary trading. Long before the 2008 crisis, federal regulators had—and used—the authority to regulate these types of investments.

**Protecting Financial Consumers.** Title VII of the CHOICE Act converts the Consumer Financial Protection Bureau (CFPB) into an enforcement-only agency, and ensures that its director would be removable by the President at will. The CHOICE Act places the new agency under congressional appropriations, and also repeals Dodd–Frank's overly vague “unfair, deceptive, or abusive” consumer protection construct.

## Main Features of the Economic Growth, Regulatory Relief, and Consumer Protection Act

The Economic Growth, Regulatory Relief, and Consumer Protection Act is designed to provide targeted relief in the banking industry. The Senate bill includes several features that would provide significant regulatory relief, and it includes several provisions that are very similar to sections of the CHOICE Act. Two of the main components of S. 2155 are as follows.

**Regulatory Off-Ramp for Risk-Weighted Capital Rules.** S. 2155 includes a trimmed-down version of the off-ramp in the CHOICE Act. The S. 2155 off-ramp only provides relief from risk-weighted capital requirements (as defined in 12 U.S. Code § 5371) for *some small* banks that meet a new leverage-ratio requirement. In general, this regulatory off-ramp applies to banks with total assets of less than \$10 billion. However, the bill authorizes federal regulators to disqualify banks—even those that meet the new leverage ratio—for capital regulation relief based on their *risk profile*.<sup>3</sup>

**Relief from Heightened Standards.** S. 2155 amends the asset threshold for the Federal Reserve to impose more stringent regulations on non-bank financial companies and bank holding companies. The Sen-

ate bill raises the threshold from \$50 billion to \$250 billion, but with major conditions. S. 2155 would still authorize the Fed to “apply any prudential standard” to “any bank holding company or bank holding companies” with total assets of at least \$100 billion. The bill also authorizes the Fed “to tailor or differentiate among companies on an individual basis or by category, taking into consideration their capital structure, riskiness, complexity, financial activities (including financial activities of their subsidiaries), size, and any other risk-related factors that the Board of Governors deems appropriate.” In other words, the Senate bill lifts the threshold to \$250 billion in name only.

## Common Provisions in CHOICE and the Economic Growth, Regulatory Relief, and Consumer Protection Act

Aside from different versions of the regulatory off-ramp, the two bills share nearly 15 similar provisions. A brief description of some of these features follows, and Table 1 provides a summary-level overview of many of the respective features in the two bills.

**Relief from Ability-to-Repay/QM Rules.** Both bills provide relief to banks that hold residential mortgages on their books instead of selling them into the securitization market. S. 2155 provides a qualified mortgage (QM) safe harbor for such banks with less than \$10 billion in total assets, but the CHOICE Act provides a QM safe harbor for all banks that hold mortgages instead of selling them.

**Relief from Home Mortgage Disclosure Act (HMDA) Requirements.** The CHOICE Act provides an exemption from most HMDA requirements to depository institutions that originate less than 100 closed-end mortgages and less than 200 open lines of credit in each of the two preceding years. S. 2155 creates a more limited HMDA exemption for institutions that originate less than 500 closed-end mortgages, and fewer than 500 open lines of credit in each of the two preceding years.

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1. The committee's 12 Republican Senators voted for the measure along with four Democratic Senators. Jim Puzzanghera, “Senate Committee Advances Bipartisan Measure Rolling Back Some Bank Regulations,” *Los Angeles Times*, December 5, 2017, <http://beta.latimes.com/business/la-fi-senate-banking-regulations-20171205-story.html> (accessed December 12, 2017). (As of this writing, S. 2155 has 12 Democratic co-sponsors, some of whom are not on the Banking Committee.)
  2. For a comprehensive analysis of the provisions in the two bills, see Norbert J. Michel, “A Comparison of Two Financial Regulatory Reform Approaches,” Heritage Foundation *Background* No. 3275, <http://www.heritage.org/markets-and-finance/report/comparison-two-financial-regulatory-reform-approaches>, January 2, 2017.
  3. It is impossible to know how regulators will use such discretion, but very few community banks engage in material amounts of the supposedly risky activities singled out in S. 2155. See Michel, “A Comparison of Two Financial Regulatory Reform Approaches.”
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TABLE 1

## Comparing Financial Regulatory Reform Bills (Page 1 of 2)

Provision	House: CHOICE Act	Senate: S. 2155	Heritage Recommendation
<b>Regulatory Off-Ramp</b>	Implements broad off-ramp	Implements limited off-ramp	Provide a broad off-ramp and expand the concept
<b>Risk-Weighted Capital Rules</b>	Broad relief via regulatory off-ramp	Limited relief via regulatory off-ramp	Provide broader relief via regulatory off-ramp
<b>Heightened Prudential Standards</b>	Broad relief via regulatory off-ramp	Limited relief via altered SIFI threshold	Provide broad relief via off-ramp and eliminate SIFI threshold
<b>Volcker Rule</b>	Repeals the Volcker rule	Provides relief to small “traditional” banks	Repeal the Volcker rule
<b>CFPB Reform</b>	Converts CFPB to enforcement-only agency and makes other improvements	No change	Eliminate the CFPB and consolidate enforcement
<b>Ability to Repay/QM</b>	Broad relief for all that hold rather than securitize	Limits relief to banks with less than \$10 billion in assets	Provide broad relief for holding mortgages
<b>Stress Tests and Living Wills</b>	Broad relief via off-ramp and limited relief outside of off-ramp	Limited relief via altered SIFI threshold	Eliminate stress tests and living wills
<b>HMDA Relief</b>	Limited relief with <i>de minimis</i>	More limited relief with alternate <i>de minimis</i>	Provide broad relief via off-ramp
<b>SAFE Act</b>	Levels nonbank/bank employee playing field	Levels nonbank/bank employee playing field	Adopt this policy
<b>Manufactured Home Loan Access</b>	Amends high-cost mortgage and makes one other clarification	Does not amend high-cost mortgage but makes same clarification	Make clarification and eliminate high-cost mortgage concept
<b>Relief from Escrow Requirements</b>	Safe harbor from TILA using \$10 billion threshold if loan is held	Safe harbor from TILA using \$10 billion and <i>de minimis</i>	Provide broad TILA relief via off-ramp
<b>Reduced Reporting Burden</b>	Lowers burden for all well-capitalized banks	Lowers burden for banks with less than \$5 billion in assets	Provide broad reporting relief via off-ramp
<b>Federal Savings Association Charter Fix</b>	Provides blanket fix	Contingent fix with asset threshold and grandfather clause	Provide blanket fix
<b>Small BHC Policy Statement</b>	Raises Fed’s threshold to \$10 billion	Raises Fed’s threshold to \$3 billion	Raise threshold to \$10 billion
<b>Expedited Funds Act Fix</b>	Adds American Samoa and Mariana Islands	Adds American Samoa and Mariana Islands	Adopt this policy

TABLE 1

## Comparing Financial Regulatory Reform Bills (Page 2 of 2)

Provision	House: CHOICE Act	Senate: S. 2155	Heritage Recommendation
<b>Parity for National Exchanges</b>	Extends blue sky pre-emption and includes venture exchanges	Extends blue sky pre-emption but does not include venture exchanges	Extend blue sky pre-emption and include venture exchanges
<b>Alters Federal Involvement in Insurance Regulation</b>	Eliminates FIO, creates new Office at Treasury, protects against usurping state regulation	Creates new Advocacy Committee at the Fed	Eliminate the FIO
<b>Budget Transparency for NCUA</b>	Improves transparency	Improves transparency	Adopt this policy
<b>Exception for Reciprocal Deposits</b>	No change	Amends definition of brokered deposits and implements maximum	Do not amend the definition or implement maximum; improve waiver process
<b>Protections For Veterans' Credit</b>	No change	Protects credit report for vets with delayed VA reimbursement	Protect credit report for vets with delayed VA reimbursement
<b>Muni Bond Change for LCR</b>	No change	Treats all investment-grade muni bonds as Level 2B HQLA	Provide relief via off-ramp
<b>Bank Exam Frequency</b>	No change	Reduces frequency for banks with less than \$3 billion in assets	Provide relief via off-ramp
<b>PACE Loan Regulation</b>	No change	Grants rulemaking authority to CFPB	Do not authorize any federal rules regarding PACE loans

SOURCE: Heritage Foundation research.

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### Relief from Mortgage Licensing Impediments.

Both the Senate and House bills amend the Secure and Fair Enforcement (SAFE) for Mortgage Licensing Act of 2008 so that individuals employed as loan originators can continue working without having to go through a special licensing process when they switch jobs from depository institutions to non-depository institutions. There are no material differences in these sections of the two bills.

**Volcker Rule Relief.** The CHOICE Act entirely repeals the Volcker rule, but the Senate bill creates an

exemption from Volcker for banks with assets not exceeding \$10 billion *and* with total trading assets and liabilities not exceeding more than 5 percent of their total assets.

**Reduced Reporting Burden.** The Senate bill authorizes a shortened call report in the first and third quarters, subject to newly issued regulations, for banks with less than \$5 billion in assets. The CHOICE Act provides the same relief to any size bank provided that it is well capitalized.<sup>4</sup>

4. See Section 38(b) of the Federal Deposit Insurance Act, 12 U.S. Code § 1831o.

## Common Ground for Regulatory Off-Ramp

The S. 2155 regulatory off-ramp is much more limited than the CHOICE Act off-ramp, but the House and the Senate versions are not irreconcilable. For instance, rather than giving the Fed discretion to disqualify banks based on a risk profile, Congress could simply adopt a leverage ratio that accounts for off-balance-sheet exposures, proprietary trading, and derivatives exposures.

Banks that do not undertake such activities would remain unaffected by using such a metric, while banks that do engage in large amounts of such activities will have a more difficult time meeting the off-ramp requirement.<sup>5</sup> Ultimately, the off-ramp approach should be expanded to provide additional regulatory relief to banks that choose to meet even higher equity–ratio requirements.<sup>6</sup>

## Conclusion

In June, the House passed the Financial CHOICE Act, a comprehensive financial regulatory reform bill that would replace large parts of the 2010 Dodd–Frank Act. The Republicans hold a very slim Senate majority, so enacting such a comprehensive reform package is difficult. Nonetheless, the Senate Banking Committee recently passed the Economic Growth, Regulatory Relief, and Consumer Protection Act, a more targeted financial reform bill that has bipartisan support. There is sufficient overlap between the policies in the Senate and House bills that Congress can enact important financial regulatory reforms.

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5. The CHOICE Act does use such a ratio, but there are also other options. See Norbert J. Michel, “Money and Banking Provisions in the Financial CHOICE Act: A Major Step in the Right Direction,” Heritage Foundation *Backgrounders* No. 3152, August 31, 2016, <http://www.heritage.org/markets-and-finance/report/money-and-banking-provisions-the-financial-choice-act-major-step-the>.

6. Gerald P. Dwyer and Norbert J. Michel, “A New Federal Charter for Financial Institutions,” in Norbert J. Michel, ed., *Prosperity Unleashed: Smarter Financial Regulation* (Washington DC: The Heritage Foundation, 2017), <http://www.heritage.org/markets-and-finance/report/new-federal-charter-financial-institutions>.

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