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After a Decade, What is Settled About Dodd-Frank?

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In a statement that has been more honored in the breach than the observance, Justice Louis Brandeis once noted that "it is usually more important that a rule of law be settled than that it be settled right."[1] July 21, 2020 will be the 10th anniversary of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank). Enacted in President Obama's first term, its provisions called for significant rulemaking by the federal banking agencies. The first rulemakings were not immune from criticism, and after the 2016 election, Congress trimmed certain Dodd-Frank provisions in the Economic Growth, Regulatory Relief and Consumer Protection Act of 2018 (EGRRCPA). In addition, in a series of rulemakings that drew dissents, the federal banking agencies have, in the last few years, cut back on the reach of many of their initial Dodd-Frank regulations. With a presidential election looming, it is appropriate to ask what parts of the Dodd-Frank scheme for the nation's banks are finally settled after a full decade, and what may be subject to yet further change.

We should start with the principal changes to Dodd-Frank affecting wholesale banking since 2016. Five of the most significant ones are: (i) the tailoring of the Section 165 enhanced prudential standards for large bank holding companies;[2] (ii) the revisions to the proprietary trading and private funds provisions of the Volcker Rule;[3] (iii) the simplification of minimum capital rules, with the so-called "Stress Capital Buffer" (SCB) becoming the most important constraint for many banking organizations;[4] (iv) the shift by the Financial Stability Oversight Council (FSOC) away from designating systemically significant nonbank companies (Nonbank SIFIs);[5] and (v) reduction in required margin for bank-affiliate derivative contracts.[6]

These modifications to the pre-2017 Dodd-Frank regulatory regime have not had unanimous support at the regulators. In particular, Federal Reserve Board (Federal Reserve) Governor Lael Brainard and Federal Deposit Insurance Corporation (FDIC) Director Martin Gruenberg have published dissents to many of them, as well as dissents on other changes. It is quite possible that both regulators would play important roles in a Democratic Administration in 2021. On one view, everything could be up for grabs in a new Administration.[7] There are, however, reasons to believe that this will not be the case because of certain legal constraints as well as the practical experience of the regulators themselves in the first six years after the statute's enactment.

First are the requirements of administrative law and procedure. Nothing has spawned litigation in recent years so much as new Administrations changing regulations from their predecessors. Under existing precedent, the federal banking agencies are permitted to change their existing policies as long as they provide a reasoned explanation for the change.[8] When an agency changes its existing position, it need not always provide "a more detailed justification than what would suffice for a new policy created on a blank slate,"[9] but the agency must at least "display awareness that it is changing position" and "show

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that there are good reasons for the new policy."[10] Moreover, in explaining its changed position, an agency must also be cognizant that longstanding policies may have "engendered serious reliance interests that must be taken into account."[11]

Changes to each of the five significant areas described above would therefore require reasoned rulemakings. Under this requirement, one could see different regulations faring differently. With respect to the simplification of capital requirements and the SCB requirement, this regulation has the advantage of only recently having been finalized. It is only with the Federal Reserve's 2020 CCAR results that banks subject to the SCB have received their buffers, following a rulemaking process that began in April 2018. Although Governor Brainard dissented from the final SCB rule, it seems likely that several years' experience with the SCB rule in practice would help the Federal Reserve make a more reasoned justification for changing it.

As for the Volcker Rule, there the banking agencies face a different challenge. The revisions to the Volcker regulations that were finalized in 2019 and 2020 came after many years' experience, with the agencies justifying the changes in large part based on that experience. For example, the original approach to proprietary trading, under which there was a presumption of trading for transactions within 60 days, but no time at which the presumption finally disappeared, clearly proved difficult to implement as a practical matter. So too, the banking agencies considered closely, and rejected, the so-called "accounting prong" approach to proprietary trading in the 2018-2019 rulemaking, for inappropriately capturing long-term investments.[12] A similar approach prevailed with respect to Volcker fund issues like foreign excluded funds, where the agencies offered a detailed justification for why the exclusion would promote U.S. financial stability. Changes to margin requirements for bank-affiliate swaps similarly came after several years of "actual supervisory experience" with the prior regulation.[13]

The Section 165 tailoring rule, to which Governor Brainard and Director Gruenberg dissented, seems to be a potentially different story. Unlike the Volcker Rule – or the revision to the swaps margin rule, for that matter – it is not a revision of a rule finalized prior to 2016, where the federal banking agencies have based a change in approach in part on their experience under the original regulations. And the tailoring rule was finalized in 2019, which means that the federal banking agencies will have somewhat more experience with its being in effect than the SCB. As such, it seems to be more of a candidate for revision, although even here the agencies could wish for some additional time to pass in order to bolster justifications any changes.

A second tempering factor could be the agencies' own experience in the early years of Dodd-Frank. The best example here is the experience with FSOC designations of Nonbank SIFIs. Four such companies were designated: General Electric Capital Corporation (GE Capital), AIG, MetLife, and Prudential. Upon designation, such companies became subject to Federal Reserve supervision, as well as heightened regulatory requirements. The Federal Reserve, however, proposed heightened regulatory requirements for only one of the four, GE Capital, deciding to defer any attempts to regulate the insurance industry. In addition, MetLife successfully challenged its designation in federal court on the ground that the FSOC had arbitrarily misapplied its own designation regulation, and AIG and Prudential successfully sought de-designation after modifying their businesses. Inasmuch as the primary regulatory authority responsible for regulating and supervising Nonbank SIFIs was unable to construct a working paradigm for such companies, it is difficult seeing a return to the early days of Dodd-Frank and additional designations under a Democratic Administration. This principle applies as well to the Volcker Rule – it is a provision directed at the nation's largest, most sophisticated banks, and the regulatory record in its first years, where the federal banking agencies applied heightened standards to all banks with more than $50 billion in assets, was clearly one of biting off well more than one could chew.

For the foregoing reasons, it seems at this writing that more of Dodd-Frank may now be settled that one might think initially. Regulators under a new Administration may be confined "from molar to molecular motions," in the words of Brandeis' colleague Justice Holmes. In addition to the tailoring rules mentioned above, it is possible that new regulators could act at the margins to require large banking organizations to maintain more capital – such as by continuing to limit share repurchases and placing more stringent restrictions on dividends if the economy does not recover quickly enough from COVID-19. But even a significant return to the early days of Dodd-Frank does not seem to be in the picture, absent a new financial crisis.

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[1] *DiSanto v. Pennsylvania*, 273 U.S. 34, 42 (1927) (dissenting opinion).

[2] 12 C.F.R. § 252 *et seq.*

[3] *Id.* § 248 *et seq.*

[4] 85 *Federal Register* 15,576 (March 18, 2020).

[5] 84 *Federal Register* 71,740 (December 30, 2019).

[6] 85 *Federal Register* 39,754 (July 1, 2020).

[7] A new Administration would have a new Comptroller of the Currency, a new Director of the Bureau of Consumer Financial Protection (given that Dodd-Frank's termination "for cause" standard was held unconstitutional), and, as a result, would soon have a majority position on the FDIC Board. As for the Federal Reserve, there are currently two open seats on its Board of Governors; nominations to those positions are pending only. It is quite possible, therefore, that a Democratic President could appoint a majority of the Federal Reserve fairly swiftly.

[8] *See, e.g., National Cable & Telecommunications Assn. v. Brand X Internet Services*, 545 U. S. 967, 981–982 (2005).

[9] *FCC v. Fox Television Stations, Inc.,* 556 U. S. 502, 515 (2009).

[10] *Id.*

[11] *Id.* at 515-516 ("In such cases it is not that further justification is demanded by the mere fact of policy change; but that a reasoned explanation is needed for disregarding facts and circumstances that underlay or were engendered by the prior policy.").

[12] 84 *Federal Register* 84,974, 84,975 (November 14, 2019).

[13] 85 *Federal Register* 39,754, 39,760 (July 1, 2020).