WebMemo

Published by The Heritage Foundation

No. 3320
July 21, 2011

Dodd–Frank: One Year Later

By Diane Katz

Today marks the one-year anniversary of the Dodd–Frank Wall Street Reform and Consumer Protection Act. It comes in at some 2,300 pages, so it should surprise no one that dozens of regulatory deadlines have been missed, and a multitude of agencies are months behind in their rulemaking schedule. It is certainly fair to question, then, how the bureaucrats and technocrats who cannot get the rules written can possibly manage the vast and roiling markets over which they now rule.

They cannot—at least not successfully. And a principal reason is that their colossal regulatory edifice teeters on the faulty premise that the economic crisis was a consequence of too little regulation—as opposed to misguided housing policies and twisted tax and regulatory incentives. Thus, Dodd–Frank and its 243 separate rulemakings (by 11 different federal agencies) are an ill-conceived attempt to reduce financial risk by constraining banks, credit unions, mortgage brokers, investors, accountants, and myriad other financial products and services.

In so doing, Congress has expanded the powers of the very regulatory behemoths that were supposed to protect us from financial calamity last time around. Yet the torrent of regulation does nothing to tame Fannie Mae and Freddie Mac—major contributors to the financial crisis.

Failure Is the Only Certainty. Dodd–Frank's results to date have been less than stellar to say the least. With few of the rules actually finalized, financial firms now inhabit a regulatory purgatory of sorts, while billions of dollars are funneled into expanding the size of government.

Ironically, Dodd–Frank supporters claim the monstrous regulatory rollout was intended to inject certainty into a market made jittery by the 2008 crisis. The uncertainty is now worse than ever—and nothing beats uncertainty for inhibiting investment and job growth.

Meanwhile, the unemployment rate stands at 9.2 percent. The budget deficit tops $1.3 trillion, and federal debt has hit the ceiling at $14 trillion. Consumer spending is tepid, wages are stagnant, and prices for energy and food are rising.

President Obama actually complains of lobbyists and lawyers "trying to undo the progress that we've made." But try as he might to demonize bankers, the President's misreading of public sentiment will come back to haunt him. Americans, for the most part, understand that punishing success is a losing proposition. The public is far more frustrated that his Administration has rewarded failure by lavishing billions of tax dollars on mismanaged banks.

More Risk, Not Less. In reality, placing new burdens on financial institutions and their custom-

This paper, in its entirety, can be found at:
http://report.heritage.org/wm3320

Produced by the Thomas A. Roe Institute for Economic Policy Studies

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002–4999
(202) 546-4400 • heritage.org

Nothing written here is to be construed as necessarily reflecting the views of The Heritage Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

ers will actually increase risks to the financial system. For example, slashing bank fees for processing debit transactions will only increase the costs of other forms of credit. Indeed, banks are hiking fees on credit cards, checking accounts, and cash machines. Even Federal Reserve Chairman Ben Bernanke is worried, telling lawmakers: "There are good reasons to be concerned.… It's going to affect revenue of small issuers. And it could result in some smaller banks being less profitable or even failing."

Absent congressional action, the finance sector faces considerable hurdles. The Commodity Futures Trading Commission has yet to finalize radical derivatives regulations that Commissioner Scott O'Malia fears may distort financial markets, limit access to capital, and increase costs for commercial end-users, putting further strains on the already struggling economy. Even worse, rules that have been issued may be revised. According to Commissioner Bart Chilton, "We had a very steep learning curve, so I think some proposals weren't as good as many of us would have liked."[1]

The housing market remains stagnant, yet federal regulators are crafting rules that would exacerbate matters. The proposed Qualified Residential Mortgage (QRM) rule could have the effect of requiring many home buyers to have at least a 20 percent down payment in order to qualify for a best interest rate mortgage. In addition to making it more difficult for qualified consumers to obtain loans, the proposed regulation would preserve Fannie Mae and Freddie Mac, whose collapse has already cost taxpayers in excess of $150 billion. It would also further concentrate mortgage lending in the largest financial institutions.

Stalled on Derivatives. The Financial Stability Oversight Council has yet to finalize the criteria it will apply to determine which bank-holding companies will qualify as "systemically important" and thus subject to particular regulatory scrutiny. (Dodd–Frank supposedly did away with "too big to fail," but simply renamed the concept "systemically important" for the purposes of making bailouts a permanent fixture of federal fiscal policy.) Absent the council's determination, financial firms will likely wait months to find out how much capital they must keep on hand and the asset limits they may leverage.

Over at the Consumer Financial Protection Bureau (CFPB), a battalion of auditors is busily gathering intelligence on most every type of financial firm and preparing regulatory attacks under existing laws. Fortunately, President Obama's dithering over a director means the CFPB will mark its first anniversary today with narrowed powers. Until a director is in place, the CFPB is statutorily barred from imposing new regulations.

Dodd–Frank Will Stunt Economic Growth. Two dozen bills are pending in Congress to rescind or reform various elements of Dodd–Frank. Some are more worthy than others. But the law's unparalleled powers, unless checked, will curtail the availability of credit and capital for consumers and businesses alike, both of which are sorely needed to nurture economic growth.

—Diane Katz is Research Fellow in Regulatory Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation.

1. Deborah Solomon, "Commodity Cop Getting Grief From All Sides," *The Wall Street Journal*, July 19, 2011.