

P.R.I.M.E. Finance

Panel of Recognized International Market Experts in Finance

Regulatory Reform: Prospects for Growth and Regulatory Cooperation



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Lookback: 2017 Regulatory Initiatives

Derivatives and Securities

- Focus on cross border regulatory harmonization of international rules under a principles-based framework.
- Push for harmonization of US interagency rules for derivatives and securities at and including:
 - Securities and Exchange Commission (SEC)
 - Commodity Futures Trading Commission (CFTC)
 - Prudential regulators: Federal Reserve Board (Fed), Office of the Comptroller of Currency (OCC), Federal Deposit Insurance Corporation (FDIC)
 - Department of Treasury
- Administration Chief of Staff announced regulatory freeze pending review.
- Require robust economic analysis of rules: Conduct a retrospective review of all rules implemented under the Dodd-Frank Act and make any necessary amendments or modifications to such rules.
- Hold corporations, corporate executives, and other individuals and entities accountable for violating federal law.



Lookback: Presidential Executive Orders

Core Principles for Regulating the Financial System

- (a) Empower Americans to make independent financial decisions and informed choices in the marketplace, save for retirement, and build individual wealth;
- (b) Prevent taxpayer-funded bailouts;
- (c) Foster economic growth and vibrant financial markets through more rigorous regulatory impact analysis that addresses systemic risk and market failures, such as moral hazard and information asymmetry;
- (d) Enable American companies to be competitive with foreign firms in domestic and foreign markets;
- (e) Advance American interests in international financial regulatory negotiations and meetings;
- (g) Restore public accountability within Federal financial regulatory agencies and rationalize the Federal financial regulatory framework.



US Update 2018: A Regulatory Reform Agenda

- Over the past year, the Trump Administration and Congress have moved forward with a broad program of regulatory reform designed to enhance American competitiveness
- The reforms have particularly focused on the financial and energy industries
- American reforms are occurring at a moment when regulations in many other advanced economies are becoming somewhat stricter, which allows us to contrast the trends and likely consequences for competitiveness



Financial Regulators Ease Costs of Compliance

- After receiving new Chairmen and Commissioners, both the SEC and my former agency, the CFTC, have taken steps to ease compliance costs for regulated entities
- SEC Chairman Clayton has proposed simplifications to Regulation S-K disclosure requirements
- CFTC Chairman Giancarlo has delayed plans to reduce swap *de minimis* thresholds in order to consider the economic costs and benefits
- The CFTC also delayed some swap variation margin requirements by six months to give market participants more time to prepare



Reforms to OTC Derivatives Regulations: Cost Benefit Approach

- The CFTC's statutory authority over swaps markets have increased its purview over financial derivatives (notably including interest rate swaps and broad-based indices of credit default swaps market), and shares jurisdiction over security-based swaps with the SEC.
- In 2011, the CFTC Inspector General found CFTC failed to use cost benefit analysis in a variety of rule makings in connection with the Dodd Frank Act.
- The IG concluded the analyses were inadequate and that the economists were not given enough input or recognition into the analyses.
- Require that all CFTC rulemakings and guidance be accompanied by a cost benefit analysis
 - Consider strengthening through Executive Order (recall Reagan's 1981 executive order) or through legislation requiring cost benefit analysis.



Financial Reforms: Removing Costs that Render Institutions “Too Small to Succeed”

- Following Dodd-Frank, US banks consolidated at an alarming rate to achieve regulatory economies of scale
- The US Senate has been advancing a bipartisan reform designed to exempt small banks with less than \$10 billion in assets from the most costly portions of Dodd-Frank, including the controversial Volcker Rule
- The Senate proposal would also exempt banks with assets under \$250 billion from systemically-risky status, reducing costs from capital requirements and stress testing requirements



Financial Reforms: Rescinding and Delaying Cures that Are Worse than the Disease

- In November 2017, Trump and Congress used the Congressional Review Act to nullify a CFPB rule that banned some financial institutions from using mandatory arbitration clauses, noting that Treasury found that trial lawyers benefitted more than consumers from the rule
- The Department of Labor's Fiduciary Rule requiring financial advisers to act as clients' fiduciaries was partially delayed in November 2017 as the DoL considers the economic costs and benefits of the rule, which may include a substantial reduction in financial adviser services offered



Energy Reforms: Reducing Costs without Eliminating Oversight

- In 2017, the EPA announced its intent to rescind the controversial greenhouse gas-focused Clean Power Plan and issued an advanced notice of proposed rulemaking seeking public comment on less costly replacements.
- The EPA/Army Corps of Engineers rescinded the expansion of the Clean Water Act's definition of covered waters and limited it to navigable waters.
- Implementation of the Interior Department's methane venting and flaring rule was delayed as the department considered the economic costs and benefits.



Ongoing American Regulatory Reform Efforts

- One-in, two-out: In 2017, three new regulations were added, while 67 existing regulations were removed, more than meeting Trump's ongoing 2:1 goal
- More than 1,500 pending rules were withdrawn or delayed
- Many delayed rules were delayed in order to be modified to account for changes implied by detailed cost-benefit analysis, which is ongoing at many agencies and departments



US: Renewed Focus on Principles Based Oversight of Securities and Derivatives

- Work with US Congressional leadership to revise the Dodd Frank Act and formulate a new regulatory regime that better protects American consumers and investors and promotes economic opportunity, growth, and stability.
- Push for harmonization of inter- and intra-agency rulemakings, guidance, and other interpretive orders required by Title VII of Dodd-Frank to reduce compliance burdens and improve oversight.
- The CFTC has ongoing and active rule implementations that it promulgated in concert with the prudential regulators, most notably the Volcker Rule and its Margin on Uncleared Swaps rulemaking.
- CFTC has authority to provide no action relief to entities negatively impacted by these rules, and to the extent necessary, in coordination with International regulatory counterparts, the Fed and other prudential regulators.

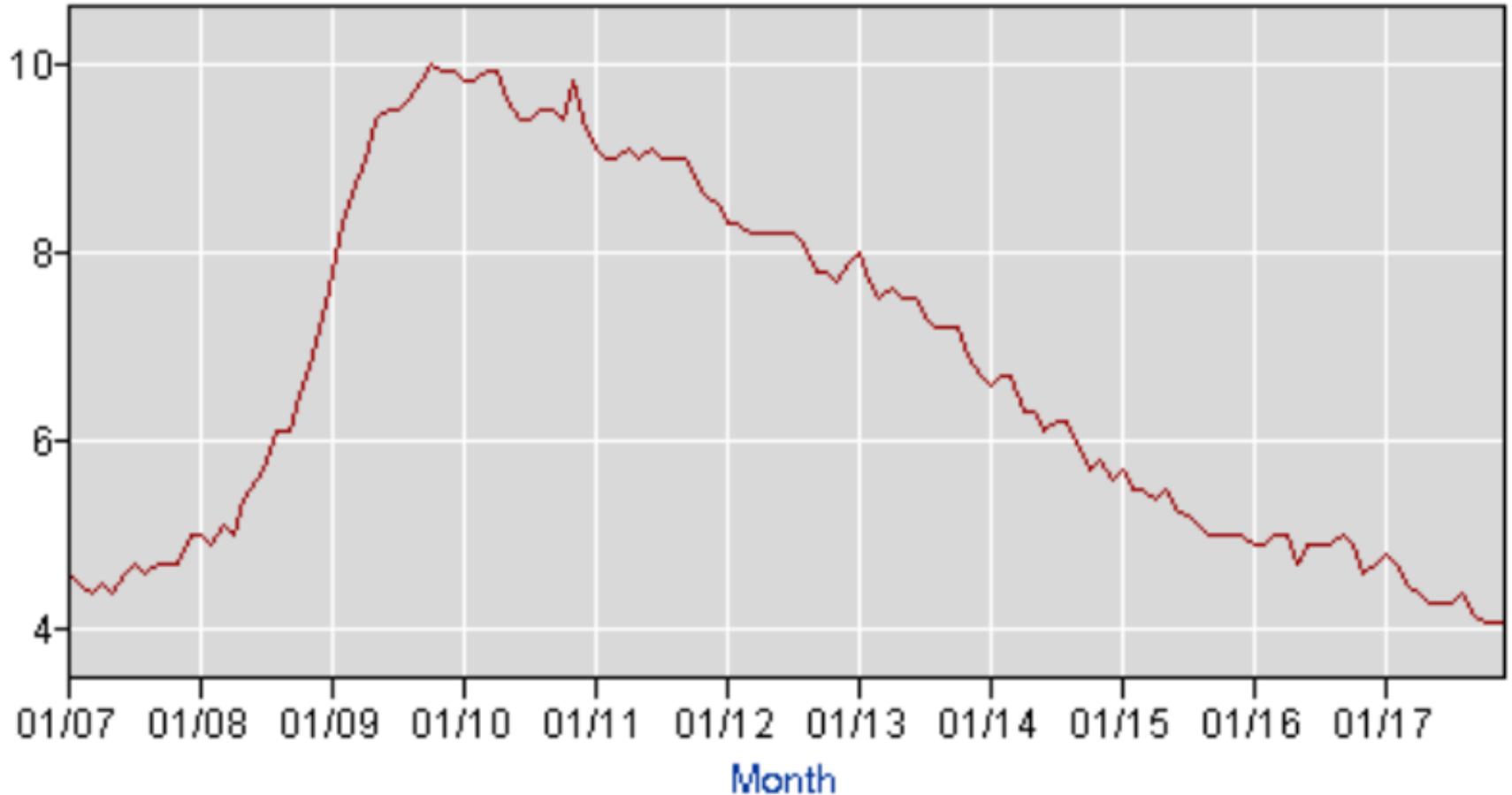


Regulatory Reform and Economic Growth

- The deregulatory environment has coincided with rapid improvements in labor force participation rates and a reduction in the unemployment rate to 4.1%
- Wage growth has started to pick up after years of concern that job growth wasn't resulting in more take-home pay for workers
- Stock markets have hit record highs
- A combination of a growth-oriented regulatory framework and the recent pro-capital creation tax reform to incentivize more future investment at the margins



Unemployment Rate Continues Tightening

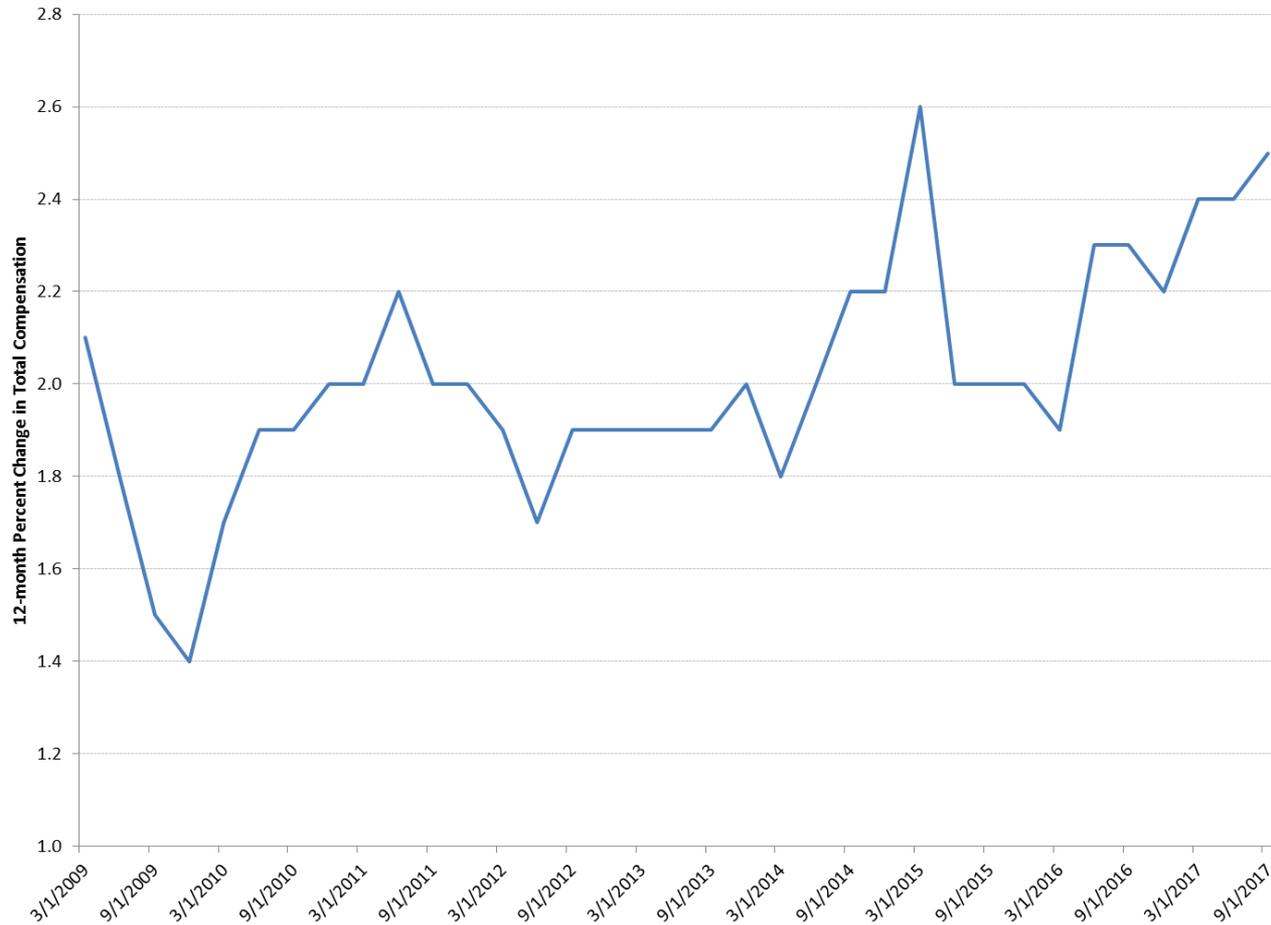


Source: Bureau of Labor Statistics, "Unemployment Rate"



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12-Month Wage Growth Picks Up



Source: Bureau of Labor Statistics, "Employment Cost Index (NAICS)"



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S&P 500 Stock Index Hits Record Highs



Source: Yahoo Finance



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International Context

- MiFID II and PRIIPs: European regulators' new disclosure and transparency rules run to over 1.4 million paragraphs
 - Expected to shrink spending on research,
 - Limit Europeans' ability to buy US ETFs and closed-end funds unless US funds comply with documentation requirements, and
 - Create substantial compliance costs for European traders
- Brexit: Introduces uncertainty regarding the long-term compliance expectations for UK financial entities
- Europe positioning may create competitive advantages for US financial markets as reforms take hold



International Harmonization

- It is to be hoped that the US example spurs European policymakers and regulators to harmonize their regulatory requirements with US requirements
- Absent harmonization, firms can be expected to engage in regulatory arbitrage where possible, and regulatory costs and deadweight losses can be expected elsewhere
- Ensuring that American and international financial markets and energy markets are open to international investment is key to ongoing global prosperity and rising consumer sentiment



“America First” Not Inconsistent With Globalization

- A forward focus on removing barriers to competition embedded in regulation and international agreements
 - International agreements that were perceived to disadvantage US companies will be revisited
- An emphasis on promoting US business interests at home and abroad and the US workforce
 - Return to robust economic growth
 - Return to full employment and good paying jobs for American workers



PRIME Finance Experts Leading the Way

- PRIME Finance Experts play a role in informing regulators on the impact of regulation on markets and contracts
 - Participate in market and product advisory committees
 - Provide public comments on pending rules and regulations
 - Provide supporting legal expertise and economic analysis to formal and rigorous cost benefit studies that consider global impact of rules and rule changes
- PRIME Finance Experts provide training and educational content to regulators, judges, and lawmakers
- PRIME Finance Experts can provide a forum for bringing regulators together and a means to resolve differences and seek regulatory harmonization



Further Questions?

- National Economic Research Associates, Inc. (NERA) is a global firm of experts dedicated to applying economic, finance, and quantitative principles to complex business and legal challenges;
- We bring academic rigor, objectivity, and real world industry experience to bear on issues arising from competition, regulation, public policy, strategy, finance, and litigation;
- NERA has a commitment to deliver unbiased findings, and a reputation for quality and independence.



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