

**RSC Policy Brief:**  
**Overview of The Wall Street Reform and Consumer Protection Act**  
*December 4, 2009*

H.R. 4173, which is scheduled for floor consideration beginning next week, will radically change the way markets function and vastly expand the federal government's regulation of the free market. This bill may have as big of an impact on the economy as a government takeover of health care or the creation of a national energy tax. Although Democrats argue this is necessary to address the problems plaguing the economy, the legislation will not create a single private-sector job, and this bill will not fix the problems of the economic crisis. Instead, at every turn, this bill expands government bureaucracy and red tape. It hurts small businesses, preventing them from bringing the country out of this economic morass. What follows are highlights of the 1279 page bill. The RSC will send out a Legislative Bulletin for the bill next week.

**Consumer Financial Protection Agency (CFPA) – Title IV of H.R. 4173:**

- The bill creates a new “consumer” agency (see [here](#) for a previous RSC Policy Brief on the CFPA) paid for by taxing financial companies for examinations and enforcement, and siphons off 10% of the Federal Reserve's expenses.
- The CFPA would have unlimited authority to regulate any financial product that could potentially be unfair, deceptive, or abusive to a consumer. This is a floor, not a ceiling, and states would be able to impose tougher standards.
- The CFPA is designed to be an equal to the prudential regulators; however, prudential regulation and consumer protection cannot be separated without harming the consumer and increasing the risk to the financial system.
- The legislation carves out banks under \$10 billion and credit unions under \$1.5 billion in assets from the examination and enforcement provisions; however, the CFPA can act if it feels the regulators are not moving swiftly enough to protect consumers.
- The CFPA would not just apply to traditional financial services. Any business which provides loans, credit, or repayment plans would be regulated. Examples include: doctors and hospitals, student loans, defined-benefit pension plans, merchants and retailers, realtors, consumer credit reporting agencies, telephone service providers, advertising agencies, publishers, and cable and satellite TV companies.

**Systemic Risk and Bailouts – Title I of H.R. 4173:**

- The bill authorizes a new Financial Services Council, made up of existing regulators, to decide which companies are “too big to fail.” The Council is also authorized to determine which companies should be bailed out (i.e. resolved). This determination can be made prospectively, without the need for exigent circumstances.

- The bill gives the Federal Reserve unlimited and unchecked authority to regulate “too big to fail” companies at will with no standard measure for regulation. Areas of regulation include capital requirements (risk weighted and countercyclical), limiting interactions between a company and their counterparties, and any other standard the Federal Reserve deems appropriate.
- Once the Council decides to bail out a financial company, the FDIC takes over and winds down these companies. This gives the FDIC unlimited authority to make loans, guarantee debt and obligations, sell or transfer assets, and remove management.
- It creates a pre-funded, \$150 billion bailout fund which, is paid for by all financial institutions with assets over \$50 billion and hedge funds over \$10 billion. An additional \$50 billion can be borrowed from the Treasury. This is a new tax the FDIC can levy on financial companies. There is no limit on how big a “too big to fail” company has to be to be resolved.

### **Over-the-Counter (OTC) Derivatives – Title III of H.R. 4173:**

- It establishes a new regulatory structure for OTC derivatives. This includes mandatory clearing or exchange trading for “standardized” transactions. This term is not defined in the bill, but is generally determined to mean a derivative that can be cleared.
- It requires margin and capital to be posted for non-standard trades not made on an exchange or through clearing. Margin is the collateral a company must deposit to cover the credit risk of the broker or counterparty.
- It places a huge burden on all companies (including many small businesses) who use OTC derivatives to hedge their risks on commodity prices, interest rates, foreign currency fluctuations, and more. These new requirements will siphon capital and liquidity away from job creation and business expansion.

### **Executive Compensation – Title II of H.R. 4173:**

- Consists of the House-passed executive compensation bill from July 2009 ([H.R. 3269](#)).
- This title requires publically traded companies to hold a non-binding shareholder vote on compensation levels for executives.
- This title requires public companies to report compensation to federal regulators who would be able to approve or disapprove of compensation agreements. It also allows federal regulators to determine if the compensation packages are aligned with the company’s risk management.

### **Investor Protection Act (IPA) – Title V, Subtitle C of H.R. 4173:**

- IPA is a grab-bag of reforms requested by the Securities and Exchange Commission (SEC), Public Company Accounting Oversight Board (PCAOB), and Securities Investor Protection Commission (SIPC).
- IPA makes several SEC-requested amendments to the Sarbanes-Oxley Act and the Securities Investor Protection Act. These would be the first changes to these acts since the early 2000s and the early 1970s respectively; however, no hearings were held to look into free market reforms of these acts.
- An amendment (Rep. Garrett) was added to permanently exempt non-accelerated filers with public float under \$75 million from complying with Sarbanes-Oxley Section 404 requirements. These reporting requirements are a major expense for small businesses. Chairman Frank has announced his intention to change or remove this bi-partisan amendment.

- The bill removes mandatory pre-dispute arbitration agreements from federal securities law and existing investor contracts.
- Even with the SEC's track record of failure to prevent massive fraud (the Madoff Ponzi scheme and Stanford Group fraud, for example), the legislation doubles the SEC's budget to \$2.5 billion over the next 5 years.
- The bill allows the SEC to levy a new tax on investment advisors for their compliance examinations. The SEC has an abysmal record of examining investment advisors. In any given year, the SEC only examines 10% of 11,000 advisors.
- The bill attempts to harmonize the fiduciary duty standard for investment advisors and broker-dealers.

#### **Credit Rating Agency Reform – Title V, Subtitle B of H.R. 4173:**

- It allows the SEC to review credit ratings issued by Nationally Recognized Statistical Rating Organizations (NRSRO) so they follow documented internal controls and manage conflicts of interest when determining credit ratings.
- For the first time, it opens credit rating agencies up to liability from any individual who may feel misled by a rating. This is a boon for trial lawyers.
- The bill also includes a Republican proposal to change the designation to National Registered Statistical Rating Organization. Importantly, Democrats are looking to remove this provision from the final bill.

#### **Federal Insurance Office (FIO) – Title VI of H.R. 4173:**

- It establishes a new FIO in the Department of the Treasury which is responsible for monitoring systemic risk in the insurance industry. It permits the FIO to negotiate international agreements related to insurance.

#### **Private Pools of Capital – Title V, Subtitle A of H.R. 4173:**

- It requires private advisors at hedge funds and private equity firms managing assets over \$150 million to register with the SEC. Venture capital firms are exempted.
- It establishes new data collection and reporting requirements for these companies which may interfere with confidential and proprietary information.

#### **Federal Reserve Audit:**

- The Financial Services Committee adopted an amendment by Rep. Paul to require audits of the Federal Reserve.

#### **Staff Contacts:**

Brad Watson [brad.watson@mail.house.gov](mailto:brad.watson@mail.house.gov) 202-226-9719, RSC

Ellen Gwaltney [Ellen.Gwaltney@mail.house.gov](mailto:Ellen.Gwaltney@mail.house.gov) 202-225-0530, Rep. Tom Price