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Trump's Deregulation Agenda: 4 Things For City Attys To Know

By **Mark Taylor**

Law360, London (February 3, 2017, 11:29 PM GMT) -- The mooted deregulation of robust U.S. financial laws under President Donald Trump has triggered panic in a stuttering European banking sector still reeling from the Brexit shock.

Before Trump's surprising victory in November's U.S. election, Europe's leaders had planned to ease requirements on bloc banks suffering malaise as their U.S. rivals flourished, but Trump's win and his subsequent promise to "dismantle" the Dodd-Frank Act has appeared to hand Wall Street further advantage.

While paring back Dodd-Frank could pave the way to "the most favorable environment for financial institutions since the financial crisis," said Edward Chan, financial services partner at Linklaters LLP, "it will raise even more questions for the regime in Europe and future negotiations on Britain's departure from the EU."

Here, legal experts weigh in on four things British banks should keep in mind under the Trump administration's approach to financial reform.

Dodd-Frank Won't Be Completely Killed

Trump signed an executive order Friday directing federal agencies to review Dodd-Frank for possible revisions to eliminate significant parts of regulatory controls he claimed stifled U.S. banks following the financial crisis.

But while changes are sure to come, lawyers are skeptical Dodd-Frank will be completely dismantled.

There is certainly an emphasis in Congress on reducing regulatory burdens and aiding the flow of capital now that the Senate, the House of Representatives and the White House are all in Republican hands, said John Collins, government affairs partner at Steptoe & Johnson LLP in Washington, D.C.

But getting a total repeal of Dodd-Frank through Congress "would be very difficult for a variety of reasons," said Bruce Bennett, leader of Covington & Burling LLP's financial services group in New York.

"Our sense is, in the overall hierarchy of priorities the new president has, this isn't at the top," he added.

Those priorities include tax reforms and undoing the Affordable Care Act, or Obamacare, according to Collins.

“No one is certain what will happen regarding changes to bank regulations,” Collins said, though he predicted that any regulatory rollback that is achieved would have little effect outside the U.S.

“Consider what is doable in the Senate, which is generally relief for regional and community banks, and much of that is on the retail side which would not affect most European banks with U.S operations,” he added.

Changes Are Likely Coming to the Volcker Rule

The Volcker Rule was a late addition to Dodd-Frank and covers a ban on banks trading on their own accounts. The net result was a mass fleeing of top proprietary traders from the largest U.S. banks into the hedge fund sector. Trump hopes killing it will boost U.S. liquidity and reverse the brain drain.

“We have seen speculation about the possible dismantling or altering the Volcker Rule, and this is an area that will be watched closely in Europe,” said Peter Green, financial services partner at Morrison & Foerster LLP in London.

“The rule was a unilateral U.S.-led initiative forming part of Dodd-Frank,” he said. “In the U.K., we have the ring-fencing rules which have a similar effect to Volcker in some areas, but there is as yet no equivalent to Volcker within the EU.”

He said it was unlikely to be seen as an overly provocative act but will be important to monitor.

“The concept makes sense — we don't want the banks playing with house money to do aggressive proprietary trading,” Bennett said. “The concern now is we have a consequence where liquidity in the debt capital markets has eroded significantly, because even though there is a market making exception in the Volcker Rule regulations it’s hard to work with.”

He said banks have really stepped away and there are few players wanting to step in, and the unintended consequence is a drag on U.S. markets.

“Whilst in one respect you can see elements of Wall Street would be advantaged by deregulation, it should also be remembered that banks have spent a lot of time and money getting ready to comply with the current international framework,” Green said.

“It can't be assumed all banks would be hugely supportive of changes that then require more restructuring of their businesses and systems and lead them to incurring more administrative costs,” he added.

He said the sentiment of many in the industry is that they would benefit from a period of stability where the existing rules bed down.

“Asking senior execs at the largest banks if they could choose between Congress dialing back Volcker or regulatory capital, they would vote for regulatory capital in a heartbeat,” Bennett said. “They have already built out Volcker compliance, they jettisoned businesses that didn’t comply, so it’s not as if they can flip a switch and go back.”

US Attitudes to Basel III Might Be Shifting

The Group of Central Bankers and Heads of Supervision, which oversees the Basel Committee on Banking Supervision, had been due to approve long-awaited reforms to the Basel III accord — which bankers informally call Basel IV — on Jan. 8, but now expect the Basel Committee to complete the highly contentious changes "in the near future" instead.

The reforms aim to stop taxpayers from bailing out financial institutions on the verge of collapse, but they have infuriated bankers who say the changes damage their ability to promote growth by lending to the wider economy.

The European Commission has been vocally opposed to the Basel revisions and has the backing of Europe's financial sector that it is strangling growth and would further weaken liquidity.

Dodd-Frank requires the banking regulators to put in place capital and other prudential enhancements required under the 2010 Basel III international banking accords, ensuring the U.S. is closer to Basel than the European sector.

But Republican congressman Patrick McHenry, a vice chairman on the House Financial Services Committee, sent a strongly worded letter to Federal Reserve Chair Janet Yellen last week stating the U.S. should explicitly not follow the Basel standards.

Bennett said that in some aspects the EU implementation of Basel III favored EU financial institutions more than the U.S. approach. "There were components of the U.S. rule that were more stringent," Bennett said. "There were complaints by the larger U.S. banks that this disparity in fact created advantages for European Union banks."

Relaxing capital requirements would almost certainly result in a U.S. advantage.

"Basel III is a major issue in Europe, and if there were plans by the new U.S. administration to roll back elements of Basel III to the extent it applies to U.S. banks, particularly in relation to significant financial institutions, that would likely provoke a substantial reaction," Green said.

There is no clear indication that the protectionist Trump administration will take this action, Green said, but as it is an area of international accord it would be a significant move away from global standards.

"I'd agree that at this point there is more concern in Europe than among U.S. regulators over the Basel Accord," Collins said. "Adjustments can be made by U.S. regulators, recognizing that certain frameworks are useful but can be improved without hampering supervision."

He said Trump's regulatory appointments would likely indicate change on the horizon but he did not expect a deviation from "the basic emphasis on safety and soundness."

The European Commission Is Against Deregulation

Last year, Michael Theurer, member of European Parliament's economic and monetary affairs committee, said the election of Trump, in addition to the U.K.'s Brexit vote, triggered a wave of anti-banking populism which threatened to undermine previous regulatory work.

"The European Parliament does not want to start a period of deregulation," he said. "We wanted to draw the right consequences from the financial crisis and we see after the Brexit we have managed to create a secure system."

A European Commission source told Law360 Friday there was “no appetite or desire” to follow Trump’s path, which could result in the U.K. stuck between the U.S. and EU when it finally leaves the bloc.

“From a European perspective it is pretty much a waiting game,” Green said.

There is continuing concern about what happened in the wake of the financial crisis, and banks and regulators do not want to see similar problems repeat, lawyers said.

“The U.S. institutions are doing pretty well, they have improved their systems and capital positions, so any significant changes to capital requirements is not something that will be done any time soon,” Collins said.

--Additional reporting by Evan Weinberger, Carmen Germaine and William Shaw. Editing by Rebecca Flanagan and Brian Baresch.
