

Regulatory reform in the USA: From words to deeds

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Since Donald Trump took office in 2017, the United States has embarked on a process of easing and recalibration of its financial regulation. While this process will not entail a dismantling of its regulatory framework, it is certainly the largest overhaul made since the last financial crisis.

The reforms promoted by the government, which have their genesis in a series of reports prepared by the Treasury Department, have materialised through two channels: legislative changes (which require congressional approval), and regulatory changes (which only need the approval of the competent regulators).

Within the first group we find the recent bill approved by Congress on 22 May with the agreement of both parties. This law does not reverse the Dodd-Frank Act (the main regulation which emerged after the crisis), but it does mean softening the regulatory burden, particularly for smaller banks, and certain benefits for medium and large entities. For example, smaller banks will benefit from an exemption from the Volcker Rule (that is, one that prohibits, among other things, proprietary trading, or the trading of financial assets on their own behalf). In addition, the threshold of assets to qualify for enhanced supervision (which implies stricter conditions in terms of contingent capital requirements or resolution plans) amounts to US\$50 billion to US\$250 billion, although the Federal Reserve may submit this regime stricter to banks with more than US\$100 billion in assets. These new limits will also serve to determine which entities will be subject to stress tests. Finally, the regulation also proposes changes likely to benefit larger banks, such as the recognition of certain municipal bonds that will be used for calculations for the purpose of compliance with liquidity requirements.

Although this legislative change has entailed an important shift in terms of regulation, the reform has not been as disruptive as the Republican Party wanted (otherwise it would not have had the support of the Democratic Party). For example, the authority of the Consumer Financial Protection Bureau, the Volcker Rule for larger banks, and the Orderly Liquidation Authority (OLA) have been left intact.

There are also purely regulatory changes promoted by the competent agencies. A clear example of this is the proposal published by the Federal Reserve to modify the Volcker Rule. The objective is to simplify it, adapting the requirements to the situation of each entity. For example, the requirements are modified depending on the size of each bank's trading portfolio. Thus, financial entities with a significant trading portfolio will be subject to a comprehensive compliance programme, while banks with a reduced portfolio will be subject to a presumption of compliance. It should be mentioned, in any case, that this last group of banks would only represent 2% of the total activities in the sector.

In short, the proposed changes will facilitate compliance with the Volcker Rule, and will not entail a return to the pre-crisis world: proprietary trading will continue to be prohibited. Even Lael Brainard, a member of the Board of Governors of the Federal Reserve appointed by the Obama administration, has supported the changes, acknowledging that they will make it more efficient.

In this way, the Trump administration is fulfilling its promise to review financial regulation in the United States. So far, the regulatory changes put in place seem to be following the principle of proportionality, mainly reducing the burden on smaller institutions, although they will also, as we stated earlier, benefit the larger banks. While improving efficiency and recalibrating the requirements of the regulatory framework are laudable objectives, it is important to emphasise that it is vital we do not fall into a deregulatory spiral that could lead to a new financial crisis. The undesirable consequences of regulation must be analysed and solved, but high regulatory standards must always prevail. The global rules agreed upon in international forums must be respected, to prevent the undermining of financial stability and the level playing field among banks.

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