Revisiting Dodd-Frank

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PROBLEM

Drafted and enacted in response to the 2007–2009 financial crisis, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) became law in 2010.[1] Dodd-Frank's drafters hoped the law would repair the flaws in the financial system that had so painfully manifested themselves during the financial crisis. Rather than addressing the regulatory failures that led to the crisis, Dodd-Frank's core solution was to shift decision-making from the private sector to regulators—the same regulators whose lapses had contributed to the crisis. Dodd-Frank has been costly in the short term, as any major regulatory overhaul would be. The financial industry and regulators have poured countless hours and dollars into implementing the new law. Of greater concern than these short-term implementation costs are Dodd-Frank's potential long-run costs. Rather than averting crises, Dodd-Frank's rejiggering of the financial system has created the preconditions for a future crisis, while inhibiting economic growth and dynamism.

SOLUTION

Reinstituting precrisis financial regulation is not the answer. The precrisis financial regulatory system was broken, but Dodd-Frank is not the proper repair kit. The current rationale for financial regulation is misguided. A piece-by-piece assessment of Dodd-Frank to see what should be repealed is important, but it is not enough. To be effective, financial regulation also needs a perspective shift—a shift away from the current regulator-centric approach to a regulatory system that is grounded in the superior ability and incentives of market participants to collect, process, and act on information. An effective regulatory system pun-

1. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

ishes fraud, holds the institutions and people who take risks responsible for any resulting losses, avoids nonregulatory social objectives, forecloses bailout opportunities, embraces creative destruction, presumptively fosters innovation, and removes roadblocks to competition in the financial system.

EXPLANATION

Dodd-Frank is a sprawling law, many pieces of which are unrelated to any financial crisis—past or future. What unifies the disparate pieces is an unquestioning faith in regulatory omniscience and broad grants of power to these infallible regulators. The law calls on regulators to step in where the rest of us—individuals, firms, and nongovernmental institutions—are supposedly destined to fail, namely, to identify and address all systemic and a wide array of nonsystemic risks. In giving such heavy responsibilities to regulators, Dodd-Frank's drafters overlooked the fact that precrisis regulators missed risks and that precrisis regulatory design contributed to the buildup of risk. By giving regulators an outsized role, Dodd-Frank suppresses the market's intrinsic disciplining mechanisms and builds bailout expectations. Revisiting Dodd-Frank thus requires a marked change in perspective—a shift away from the comforting but ineffective "entrust the financial system to the skilled hands of the all-knowing regulators" approach to financial regulation, as well as a piece-by-piece substantive overhaul.

SHIFTING THE REGULATORY PERSPECTIVE

Dodd-Frank favors regulatory discretion over market-based regulation. It empowers regulators to use their discretion to make risk-management decisions for companies and individuals, who would otherwise respond to direction from their shareholders, customers, and creditors. Dodd-Frank not only embraces more prescriptive microprudential regulation for individual financial institutions, but it also adds another regulatory layer designed to target ill-defined and elusive "systemic risk." This so-called macroprudential regulation allows government lawyers and economists to overrule a financial institution's decisions—even if those decisions are legal and appropriate for the individual firm—for fear that they might endanger the broader financial system.

Financial regulators thus become central planners charged with carefully balancing the interests and risk-taking of all market participants, ensuring that firms do not fail, keeping the financial system functioning smoothly, and managing firms' relationships with one another. This form of regulation

turns regulators into allocators of credit: regulators decide who gets financed and who does not, which, in turn, affects how the economy develops, which consumer and business needs are met, and where innovation occurs.

Regulators, driven by an evolving understanding of the inscrutable "systemic risk," override the clear market signals through which consumers and Main Street businesses communicate their needs to financial service providers. Macroprudential regulation also displaces the market mechanisms that signal impending trouble at a financial company or in a financial sector. Regulators, who rely on imperfect, delayed information, try to foresee and forestall problems. The customers, shareholders, and creditors, who have access to more immediate information and would otherwise be monitoring the firms with which they interact, instead get the message not to worry. Regulators' very public and costly efforts at managing the financial system and keeping risk-taking in check blunt market discipline and train market participants to look to the government for solutions. With deposit insurance and assurances of federal oversight in place, how often do you check your bank's balance sheet?[2] When the next financial crisis comes, the calls for government bailouts will be even louder than they were in the last crisis.

The next crisis is likely to be worse than the last because Dodd-Frank concentrates so much power in the hands of a few regulators. If these powerful regulators make mistakes, exercise poor judgment, or miss a key market development (all of which are inevitable because they are human), the consequences will be far-reaching. Every firm that has reordered its business to satisfy a regulatory directive will find itself in trouble if that directive proves unsound. And once a crisis happens, widely applicable regulatory mandates, such as liquidity rules, could intensify it. By contrast, if firms and individuals retain decision-making authority, their errors will be contained and firms will not walk in lockstep with one another.

That the framers of Dodd-Frank embraced enhanced regulatory authority and discretion as the answer in the heat of the crisis is perhaps understandable. The crisis hurt many people, and policymakers wanted to prevent similar harm in the future. In the years since the crisis, however, research has shown that regulatory errors lay at the heart of the crisis. Regulatory decisions drove firms and individuals to make poor choices that they otherwise would not have made. For example, Stephen Matteo Miller has demonstrated that regulation created

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2. Anat Admati asked this question on David Beckworth's Macro Musings podcast. David Beckworth, "Macro Musings 40: Anat Admati on Debt, Equity, and Financial Instability," Mercatus Center at George Mason University, January 16, 2017.

a demand by financial institutions for mortgage-related, structured products by classifying them as safer than the underlying mortgages.[3] Arnold Kling and Russell Roberts likewise point to the government's inadvertent contributions to the financial crisis through misguided regulatory and housing policies.[4] Lawrence White has highlighted the role that credit rating agency regulation—which forced firms to rely on government-credentialed credit rating agencies and kept competitors out—played in the crisis.[5]

This research demonstrates the false promise of a top-down approach that relies on regulators to identify and address risks. While neither regulators nor markets perfectly rein in bad behavior, markets hold those who make mistakes more promptly and mercilessly to account—if the government does not stand in the way—than regulators can. To raise money, a firm needs to show investors that it has a plan to make money. And to make money, a firm needs to provide something people want. The market will walk away from firms that fail on either of these counts. Regulators have difficulty obtaining and processing information, but price signals readily transmit information among market participants.[6] Moreover, individuals and firms rapidly and rationally adjust their behavior—without the need for regulatory intervention—in response to these signals.[7] But under the current regulatory framework, regulators *do* intervene to drive financial firms' behavior.

A new perspective should guide the new approach to financial regulation: regulation sets broad parameters within which market participants have freedom to act, as long as they bear the consequences of their actions. There is a role

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3. See Stephen Matteo Miller, "The Recourse Rule, Regulatory Arbitrage, and the Crisis" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, forthcoming). See also "Stephen Miller on the Recourse Rule and the Financial Crisis," YouTube video, June 3, 2015, https://www.youtube.com/watch?v=LwsMbz8yQ-8.
4. Arnold Kling, *Not What They Had in Mind: A History of Policies that Produced the Financial Crisis of 2008* (Arlington, VA: Mercatus Center at George Mason University, 2009); Russell Roberts, *Gambling with Other People's Money: How Perverted Incentives Caused the Financial Crisis* (Arlington, VA: Mercatus Center at George Mason University, 2010). See also Peter J. Wallison, *Hidden in Plain Sight: What Really Caused the World's Worst Financial Crisis and Why It Could Happen Again* (New York: Encounter Books, 2015).
5. Lawrence J. White, "An Assessment of the Credit Rating Agencies: Background, Analysis, and Policy" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, September 2013); Lawrence J. White, "A Brief History of Credit Rating Agencies: How Financial Regulation Entrenched This Industry's Role in the Subprime Mortgage Debacle of 2007–2008" (Mercatus on Policy, Mercatus Center at George Mason University, Arlington, VA, October 2009).
6. F. A. Hayek, "The Use of Knowledge in Society," *American Economic Review* 35, no. 4 (1945): 519–30.
7. See, for example, Alex Tabarrok, "A Price Is a Signal Wrapped Up in an Incentive," Marginal Revolution University, accessed January 16, 2017.

for regulators to establish clear ground rules, monitor the markets, and punish fraud, but decision-making, and the attendant responsibility for bad decisions, should be left to market participants. Market participants respond to price signals, which function well as a guide for individual and firm decisions, as long as regulators do not dampen competition, obstruct innovation, or subsidize activities or industries. Private ordering can address many problems without resort to regulatory intervention. When regulation is necessary, it should be rooted in solid economic analysis[8] and notice-and-comment rulemaking.[9] Regulatory enforcement likewise should be grounded in due process and informed by economic analysis.[10] And supervision, while an important component of the regulatory system, must not become an opaque and easily abused substitute for rulemaking or enforcement.

SUBSTANTIVE REFORM

A change in perspective cannot be effectuated without revisiting Dodd-Frank and other financial regulation on the books. Most of Dodd-Frank's provisions place responsibilities on regulators that they cannot fulfill, albeit not for lack of good intentions, creative thinking, and hard work. Dodd-Frank is divided into 16 titles covering a wide array of subjects.[11] To ensure that regulators are not asked to do the impossible and taxpayers are not asked to pay for mistakes, each of these titles must be reformed.

Title I is devoted to systemic risk. Its key features include the establishment of the Financial Stability Oversight Council (FSOC) and the Office of Financial Research (OFR) and the introduction of formalized systemic risk identification and regulation. The FSOC brings together the heads of other financial

8. See, for example, Jerry Ellig and Vera Soliman, "Is Regulatory Impact Analysis of Financial Regulations Possible?," in *Reframing Financial Regulation: Enhancing Stability and Protecting Consumers*, ed. Hester Peirce and Benjamin Klutsey (Arlington, VA: Mercatus Center at George Mason University, 2016); Jerry Ellig, "Improvements in SEC Economic Analysis since *Business Roundtable*: A Structured Assessment" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, December 2016); Hester Peirce, "Economic Analysis by Federal Regulators," *Journal of Law, Economics & Public Policy* 9, no. 4 (2013): 569–613; Abby McCloskey and Hester Peirce, "Holding Financial Regulators Accountable: A Case for Economic Analysis" (American Enterprise Institute, Washington, DC, May 2014).
9. Hester Peirce, "Regulating through the Back Door at the Commodity Futures Trading Commission," *Harvard Journal of Law and Public Policy*, Federalist Edition 2, no. 2 (2014): 321–93.
10. J.W. Verret, "Economic Analysis in Securities Enforcement: The Next Frontier at the SEC," *University of Cincinnati Law Review* 82, no. 2 (2013): 491–504.
11. For an overview of Dodd-Frank, see Hester Peirce and James Broughel, eds., *Dodd-Frank: What It Does and Why It's Flawed* (Arlington, VA: Mercatus Center at George Mason University, 2012).

regulators, state regulators, and an insurance expert to identify systemically important financial institutions, activities, and so-called financial market utilities.[12] The identified institutions and activities are subject to additional regulation, particularly from the Board of Governors of the Federal Reserve System (Fed). The FSOC also is empowered to make recommendations to other financial regulators. The OFR's job is to standardize financial data collection, collect data from other financial regulators and from financial institutions, perform research, and measure financial system risks.

The FSOC's most valuable function—one that has traditionally been performed by the President's Working Group on Financial Markets (PWG)—is to bring together financial regulators to discuss issues of common interest. The FSOC, which is more formal than the PWG, could be retained to facilitate interagency discussions, assessments of the financial system, and analyses of the costs and benefits of multiagency regulatory initiatives. Even if the FSOC is retained for these purposes, the FSOC's other functions—identifying systemically important institutions and activities and recommending courses of action for other regulators—should be eliminated to avoid distracting from and hindering the FSOC's role in fostering regulatory cooperation and information sharing. The OFR, which has a problematic design and a nebulous mission,[13] could be disbanded, and its data standardization remit could be transferred to the FSOC. The OFR has commissioned some interesting research, but research on systemic risk and other financial markets issues will occur with or without OFR involvement.[14] In any case, markets are likely better at tracking systemic risk than regulators, who receive, process, and transmit information less efficiently and comprehensively than markets.[15]

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12. For a discussion of the FSOC's SIFI designations, see Hester Peirce, "Gaining and Shedding Dodd-Frank's 'Systemically Important Financial Institution' (SIFI) Label," in *Legal Risk Management, Governance and Compliance: Interdisciplinary Case Studies from Leading Experts*, ed. Stuart Weinstein and Charles Wild (Globe Law and Business, 2016), 33–61.
13. For a brief overview of some of these concerns, see Hester Peirce, "Dodd-Frank's Office of Financial Research Is an Affront to Privacy," *RealClearMarkets*, April 19, 2012.
14. In addition to academic interest in the subject of financial stability, the Fed has a division devoted to financial stability. Specifically, the division "identifies and analyzes potential threats to financial stability; monitors financial markets, institutions, and structures; and assesses and recommends policy alternatives to address these threats. In addition, the division fosters broader understanding of financial stability issues by undertaking longer term research, primarily in banking, finance, and macroeconomics." Board of Governors of the Federal Reserve System, "Financial Stability," January 30, 2017.
15. See Matthew Beville, Dino Falaschetti, and Michael J. Orlando, "An Information Market Proposal for Regulating Systemic Risk," *University of Pennsylvania Journal of Business Law* 12, no. 3 (2010): 849–98.

For financial firms that regulators deem too big to fail, Title II of Dodd-Frank allows regulators to bypass bankruptcy in favor of a resolution process run by the Federal Deposit Insurance Corporation (FDIC). Specifically, Title II empowers the FDIC, after a government finding that default is on the horizon and there is "no viable private sector alternative," to take over nonbank financial institutions (an area in which the FDIC lacks any particular expertise) and allows the agency to borrow from the Treasury to fund the resolution.[16] Introducing uncertainty about whether, where, by whom, and how a financial firm's failure will be managed undermines sound risk management by financial institutions and their counterparties. A better approach would be to amend the bankruptcy code to make it workable for large financial companies.[17] In addition to or instead of Dodd-Frank's requirement that financial companies prepare living wills, other actions can be taken in advance to make failure less likely and more manageable.[18]

Title III of Dodd-Frank eliminates the Office of Thrift Supervision, an agency that need not be resuscitated. That title also makes permanent a temporary increase in the deposit insurance coverage cap from $100,000 to $250,000 per depositor.[19] Academic research shows that government-provided deposit insurance undermines financial stability.[20] For that reason, a revision of Dodd-Frank should go in the opposite direction and substantially decrease coverage levels. The average household has far less than $100,000 in deposits and therefore would be unaffected by such a change. Alternatives to FDIC insurance

16. See Paul H. Kupiec, "Title II: Is Orderly Liquidation Authority Necessary to Fix 'Too Big to Fail'?," in *The Case against Dodd–Frank: How the "Consumer Protection" Law Endangers Americans*, ed. Norbert J. Michel (Washington, DC: Heritage Foundation, 2016), 60–61.
17. See, for example, Emily Kapur, "The Next Lehman Bankruptcy," in *Making Failure Feasible*, ed. Thomas Jackson, Kenneth E. Scott, and John B. Taylor (Stanford, CA: Hoover Institution Press, 2015).
18. See, for example, Garett Jones, "The Rise of Bail-Ins and the Quest for Credible Laissez-Faire Banking," in *Reframing Financial Regulation*, ed. Peirce and Klutsey; Peter J. Wallison, "Title II of Dodd-Frank," in *Reframing Financial Regulation*, ed. Peirce and Klutsey.
19. During the crisis, the cap was temporarily raised to $250,000. Federal Deposit Insurance Corporation, "Emergency Economic Stabilization Act of 2008 Temporarily Increases Basic FDIC Insurance Coverage from $100,000 to $250,000 per Depositor," October 7, 2008.
20. For a discussion of the literature, see Thomas L. Hogan and Kristine Johnson, "Alternatives to the Federal Deposit Insurance Corporation," in *Reframing Financial Regulation*, ed. Peirce and Klutsey, 60. See also William J. Luther and Thomas L. Hogan, "The Implicit Costs of Deposit Insurance," in *Journal of Private Enterprise* 31, no. 2 (2016): 1–13; William J. Luther and Thomas L. Hogan, "Deposit Insurance Is Not Fair" (working paper, 2015), available through SSRN; William J. Luther and Thomas L. Hogan, "Deposit Insurance Is Not Free" (Mercatus on Policy, Mercatus Center at George Mason University, Arlington, VA, December 2012).

include privately administered or provided insurance.[21] Particularly in combination with simpler, higher capital requirements,[22] such an approach could do more for financial stability than expanding FDIC deposit insurance.

Title IV of Dodd-Frank requires hedge fund and certain other private fund advisers to register with the Securities and Exchange Commission (SEC).[23] The resulting influx of private fund advisers has diverted SEC examiners away from funds that serve a far greater number of less sophisticated investors. Concerns about diversion are particularly acute given the inability of the SEC to examine investment advisers regularly. Although many advisers are likely to remain registered even if the requirement is eliminated, allowing advisers the option of deregistering would enable the SEC to redirect its resources to areas of greater need. Title IV also imposes extensive reporting requirements on private fund advisers to meet federal systemic risk regulators' needs. The Form PF arguably has fallen short of expectations,[24] so it could be eliminated or modified to make its information more useful to regulators. Title IV tightened the accredited investor definition, which determines who can invest in certain nonpublic securities offerings, by excluding investors' primary residences. Narrowing the universe of accredited investors harms the economy and investors by artificially constraining the flow of capital and investors' options. To foster economic growth and investor autonomy, reform instead should allow more investors to qualify as accredited.[25]

Title V of Dodd-Frank covers insurance. Although Title V leaves the existing state regulatory system intact, it (along with the systemic designations of Title I) opens the door to federal regulation of insurance. Title V creates the Federal Insurance Office, which has the ability to nudge state regulators through, for example, reports and so-called covered agreements with international regu-

21. Hogan and Johnson discuss alternatives to FDIC insurance. Hogan and Johnson, "Alternatives to the Federal Deposit Insurance Corporation."
22. Stephen Matteo Miller, "On Simpler, Higher Capital Requirements," in *Reframing Financial Regulation*, ed. Peirce and Klutsey, 35; James R. Barth and Stephen Matteo Miller, "Benefits and Costs of a Higher Leverage Ratio" (Mercatus Working Paper, Mercatus Center at George Mason University, February 2017).
23. For a discussion of Title IV, see J.W. Verret, "Revisiting Title IV: Why Mandatory SEC Registration for Hedge-Fund Advisers Is Not Necessary," in *The Case against Dodd-Frank*, ed. Michel.
24. Office of Financial Research, "Asset Management and Financial Stability," September 2013.
25. See, for example, Hester Peirce, "Statement of Dissent from the Investor Advisory Committee Recommendation Regarding Accredited Investor Definition," US Securities and Exchange Commission, February 9, 2015; J.W. Verret, "Time for a Trump/Reagan Revolution at the SEC," *The Hill*, December 13, 2016.

lators.[26] There are good reasons for contemplating a federal charter option for an industry that is increasingly national in character.[27] But an optional federal charter might lay the groundwork for a federal bailout.[28] A better option—an approach that builds on states' expertise in insurance regulation—might be to allow state competition in chartering under which an insurance company would need only one state charter to operate nationally.[29]

Title VI of Dodd-Frank expands the Fed's powers to regulate systemic risk associated with large financial institutions and introduces the so-called Volcker Rule to ban banks from proprietary trading and private fund ownership. Expanded Fed oversight and new activity limits do not effectively address the problems that caused distress throughout the financial system during the crisis; financial institutions failed not because of proprietary trading but because of government-induced holdings of the highly rated securitization tranches.[30] Rather than solving problems manifested during the financial crisis, Title VI introduces new ones.

The Volcker Rule could make financial institutions less stable. Although the intention of the Volcker Rule—stopping banks from trading with deposit insurance backing—is commendable, there are better ways to address this problem, including requiring banks to be well capitalized.[31] Forcing banks to forgo the benefits of diversification by narrowing the activities in which they are engaged may actually weaken the banks and make them more vulnerable to risk.[32] Indeed, the history of banking is littered with examples of the problems

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26. For a discussion of the potential federalization of insurance regulation under Dodd-Frank, see Hester Peirce, "Title V and the Creeping Federalization of Insurance Regulation," in *The Case against Dodd-Frank*, ed. Michel; Hester Peirce, "Insurance Regulation in the Dodd-Frank Era" (Policy Brief No. 2015-PB-02, Networks Financial Institute, Indiana State University, Terre Haute, IN, March 2015).
27. For a discussion of the optional federal charter, see the AEI book on optional federal chartering. Peter J. Wallison, ed., *Optional Federal Chartering and Regulation of Insurance Companies* (Washington, DC: AEI Press, 2000).
28. Scott E. Harrington, "Insurance Regulation and the Dodd-Frank Act" (Policy Brief No. 2009-PB-01, Networks Financial Institute, Indiana State University, Terre Haute, IN, March 2011).
29. See Henry N. Butler and Larry E. Ribstein, "A Single-License Approach to Regulating Insurance" (Faculty Working Papers 154, Northwestern University School of Law, Chicago, IL, 2008). See also Hester Peirce, "Title V and the Creeping Federalization of Insurance Regulation."
30. Miller, "The Recourse Rule, Regulatory Arbitrage, and the Crisis."
31. See Stephen Matteo Miller and J.W. Verret. "No Need for Title VI with Simpler, Higher Capital," in *The Case against Dodd–Frank*, ed. Michel. See also Hester Peirce and Robert Greene, "Rethinking the Volcker Rule" (Mercatus on Policy, Mercatus Center at George Mason University, January 2013).
32. As J.W. Verret has explained, restrictions on the commodities activities of banks raise similar concerns. J.W. Verret, "How the Price of Beer Cans Led to a Politicized Proposal from the Fed," *The Hill*, October 12, 2016.

caused by arbitrary regulatory lines on bank activities and geographic reach.[33] While it limits diversification in some areas, the Volcker Rule could cause financial institutions as a group to move into new types of risk-taking.[34] Regulators and banks have struggled to implement the Volcker Rule in a way that does not cut off legitimate market making and hedging and does not impair liquidity.[35]

As augmented by Title VI,[36] the Fed's power over holding companies and subsidiaries across the financial industry raises concerns about homogenized regulation. Because the Fed's remit has expanded to include nonbanks, all financial institutions—baked into the same mold by the Fed—will increasingly share vulnerability to regulatory mistakes by the Fed and market events.[37] An error made by the Fed will affect not only banks and bank holding companies, but the whole financial industry landscape.[38] In revisiting Title VI of Dodd-Frank, policymakers should consider whether the Fed's role in monetary policy conflicts with its regulatory and supervisory roles and creates undue temptation for the central bank to use its monetary policy tools to cover up regulatory mistakes.[39]

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33. For a detailed discussion, see Charles W. Calomiris and Stephen H. Haber, *Fragile by Design: The Political Origins of Banking Crises and Scarce Credit* (Princeton, NJ: Princeton University Press, 2014); Michael D. Bordo, Angela Redish, and Hugh Rockoff, "Why Didn't Canada Have a Banking Crisis in 2008 (or in 1930, or 1907, or . . .)?," *Economic History Review* 68, no. 1 (2015): 218–43. For a short summary, see Stephen Matteo Miller, "The Path to 'Too Big to Fail': How We Got Holding Companies and Left Market Discipline Behind," *U.S. News and World Report*, December 19, 2016.
34. See, for example, Hester Peirce, "The Volcker Rule Increases the Likelihood that Banks Will Default," *RealClearMarkets*, March 26, 2014. As the op-ed notes, the benefit-cost analysis for the Volcker Rule warned, for example, of a potential "change in the composition of the banks' portfolio of government agency securities." Office of the Comptroller of the Currency, "Analysis of 12 CFR Part 44," accessed February 3, 2017, https://web.archive.org/web/20140321144523/http:/www.occ.gov/topics/laws-regulations/legislation-of-interest/volcker-analysis.pdf.
35. See, for example, Vern McKinley, "After the Crisis: Revisiting the 'Banks Are Special' and 'Safety Net' Doctrines" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, June 2015), 34–39. A recent Fed study found that the Volcker Rule has adversely affected corporate bond liquidity. Jack Bao, Maureen O'Hara, and Alex Zhao, "The Volcker Rule and Market-Making in Times of Stress" (Finance and Economics Discussion Series 2016-102, Board of Governors of the Federal Reserve System, Washington, DC, September 2016).
36. For an illustration of the expansion, see Hester Peirce and Robert Greene, "The Federal Reserve's Expanding Regulatory Authority Initiated by Dodd-Frank," Mercatus Center at George Mason University, November 13, 2013.
37. See Mark Calabria, Norbert Michel, and Hester Peirce, "Reforming the Regulators," in *Prosperity Unleashed: Smarter Financial Regulation* (Washington, DC: Heritage Foundation, forthcoming).
38. For a discussion of these and other problems with the Fed's regulatory approach, see Hester Peirce, "Legislation to Reform the Federal Reserve on Its 100-Year Anniversary" (Testimony before the House Financial Services Committee, Mercatus Center at George Mason University, Arlington, VA, July 10, 2014).
39. Ibid.

Under Titles VII and VIII of Dodd-Frank, regulators establish a new regulatory framework for over-the-counter derivatives (swaps) and the clearinghouses that now manage many of these contracts. Derivatives are financial contracts that derive their value from something else, such as a commodity, a bond, an interest rate, or a currency. They help financial and Main Street companies to manage risk and are also valuable sources of information to individuals, firms, and regulators.[40] Dodd-Frank mandates that central clearinghouses act as seller to every buyer and buyer to every seller in standardized swap transactions, and it also requires that these transactions be traded on exchange-like platforms.[41] Because of the size and complexity of the affected derivatives markets, this is an ambitious and dangerous undertaking. While central clearing moves some risk out of large financial firms, it introduces new risks for these firms, their customers, and the broader financial system.[42] Clearinghouses are inherently difficult to manage properly, and the introduction of government clearing mandates only complicates risk management.[43] Given that virtually all of the major financial institutions now interact with clearinghouses in at least one and usually more capacities, a clearinghouse misstep or a market event that causes the clearinghouse to collect additional margin to protect itself could spark a crisis. A better approach would drop the clearing mandate and allow market participants to decide when to use a clearinghouse.[44] Regardless of where clearing occurs, regulators should be able to see what is happening in these markets,[45] which Title

40. For a discussion of the role that derivatives play in the economy, see Bruce Tuckman, “In Defense of Derivatives: From Beer to the Financial Crisis” (Policy Analysis No. 781, Cato Institute, Washington, DC, September 29, 2015).
41. The focus on derivatives was driven by an incomplete understanding of the problems American International Group experienced during the crisis. See, for example, Hester Peirce, “Securities Lending and the Untold Story in the Collapse of AIG” (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, May 2014). In any event, the tailored nature of AIG’s swap transactions would have precluded them from being centrally cleared.
42. See, for example, Craig Pirrong, “The Inefficiency of Clearing Mandates” (Policy Analysis No. 665, Cato Institute, Washington, DC, July 21, 2010). Professor Craig Pirrong, an early skeptic of mandatory clearing, explains that “fundamental economic considerations suggest that a clearing mandate is likely to reduce market efficiency and pose its own systemic risks in a world where information is costly.”
43. See generally Hester Peirce, “Derivatives Clearinghouses: Clearing the Way to Failure,” *Cleveland State Law Review* 64, no. 3 (2016): 589–660, and sources cited therein.
44. See, for example, Hester Peirce and Vera Soliman, “Rethinking the Swaps Clearing Mandate,” in *Reframing Financial Regulation*, ed. Peirce and Klutsey.
45. Despite claims to the contrary, prior to Dodd-Frank, regulators did have information about these markets. See, for example, Norbert J. Michel, “Fixing the Dodd-Frank Derivatives Mess: Repealing Titles VII and VIII,” in *The Case against Dodd-Frank*, ed. Michel. Dodd-Frank improved the SEC’s and CFTC’s view into these markets.

VII reporting requirements may be able to achieve. In contrast, the clearing and trading mandates at the heart of the title fundamentally change these important markets by introducing new risks that are not fully understood.[46] Policymakers should modify Title XVI, which relates to the tax treatment of derivatives, as needed to reflect the changes in clearing and trading mandates.

Title VIII, an outgrowth of the clearing mandate of Title VII, should be modified to focus on coordination of principles-based regulatory oversight of clearinghouses, rather than on systemic designations. Title VIII allows regulators to prescribe special regulation for designated clearinghouses and other so-called financial market utilities (a term that implies intense regulatory control) and firms engaged in designated payment, clearing, or settlement activities. Title VIII therefore gives regulators a free hand to reshape a large swath of financial firms through the imposition of new "risk management standards," a term that the statute defines broadly.[47] Title VIII also allows the Fed to grant special privileges—including the ability to set up accounts at the Fed, the ability to earn money on Fed balances, and borrowing privileges—to designated financial market utilities.[48] Title VIII, following the lead of Title I, causes the firms that deal with clearinghouses and other financial market infrastructure firms to look to government regulators to oversee these entities and address any problems. A natural outgrowth of regulators' displacement of private monitoring and discipline is an expectation that the Fed will step in to bail out these entities if they fail. Bolstering this expectation is Title VIII's establishment of the avenues (Federal Reserve accounts and services) through which such bailouts could be carried out.[49] To avoid bailouts, the special designations of and privileges for clearinghouses and the broad regulatory delegations in Title VIII should be eliminated.

Title IX of Dodd-Frank addresses a large number of topics, most within the SEC's purview. The title warrants piece-by-piece consideration so that effective provisions can be retained. For example, expanding the SEC's ability to engage in investor testing is a useful rulemaking tool, particularly in combination with the

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46. CFTC Commissioner J. Christopher Giancarlo makes specific recommendations for modifying swaps trading rules. Christopher Giancarlo, "Reconsidering the Dodd-Frank Swaps Trading Regulatory Framework," in *Reframing Financial Regulation*, ed. Peirce and Klutsey.
47. See Dodd-Frank § 805.
48. Clearinghouses, for example, are opening accounts at the Federal Reserve. Katy Burne, "Clearinghouses Park Billions in New Fed Accounts," *Wall Street Journal*, November 23, 2016.
49. For a discussion of Title VIII, see Norbert J. Michel, "Fixing the Dodd-Frank Derivatives Mess," in *The Case Against Dodd-Frank*, ed. Michel, 131; Peirce and Broughel, eds., *Dodd-Frank: What It Does and Why It's Flawed*, 91–98; Daniel M. Gallagher, "Bank Regulators at the Gates: The Misguided Quest for Prudential Regulation of Asset Managers: Remarks at the 2015 Virginia Law and Business Review Symposium," US Securities and Exchange Commission, April 10, 2015.

agency's new emphasis on rigorous economic analysis.[50] The Investor Advisory Committee and the Investor Advocate serve a useful role in advising the SEC, but the agency's five commissioners should bear ultimate responsibility for the agency's agenda and actions. Less clear is the need for the investor ombudsman, a position that Dodd-Frank created, but whose duties seem to overlap with the SEC's preexisting Office of Investor Education and Advocacy.

The SEC has not taken regulatory action under Title IX's provisions related to the duties that broker-dealers and investment advisers have toward their clients. A recent rulemaking by the Department of Labor may have effectively superseded those provisions and thus undermined the ability of the SEC—the primary governmental regulator of retail investors' relationship with their brokers—to effectively regulate in this area.[51] To ensure consistency, Congress should consider constraining the Department of Labor's regulatory authority under the Employee Retirement Income Security Act to eliminate potential conflicts with SEC rules.[52]

Title IX also deals with the SEC's relationships with self-regulatory organizations (SROs) such as the stock exchanges and Financial Industry Regulatory Authority (FINRA). Although Dodd-Frank's procedural changes to speed consideration of SRO rulemakings may have helped on the margins, any Dodd-Frank rewrite should focus on bigger issues related to the propriety of the role SROs play given their nongovernmental status and nontransparent methods.[53] As part of the reconsideration of the role of SROs in financial regulation, FINRA's arbitration process warrants review. However, research on the value of arbitration provisions in other contexts[54] should give the SEC pause before it acts on its Title IX authority to override mandatory arbitration clauses in private contracts.

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50. Ellig, "Improvements in SEC Economic Analysis." For comparison, see Jerry Ellig and Hester Peirce, "SEC Regulatory Analysis: 'A Long Way to Go and a Short Time to Get There,'" *Brooklyn Journal of Corporate, Financial & Commercial Law* 8, no. 2 (2014): 361–437.
51. See, for example, Daniel M. Gallagher, Commissioner, US Securities and Exchange Commission, Comment Letter to Thomas Perez, Secretary, Department of Labor, July 21, 2015.
52. See, for example, Calabria, Michel, and Peirce, "Reforming the Regulators," in *Prosperity Unleashed: Smarter Financial Regulation*.
53. For a discussion of some of these issues, see Hester Peirce, "The Financial Industry Regulatory Authority: Not Self-Regulation after All" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, January 2015). See also Daniel M. Gallagher, "US Broker-Dealer Regulation," in *Reframing Financial Regulation*, ed. Peirce and Klutsey; David Burton, "Reforming FINRA" (Report, Heritage Foundation, Washington, DC, February 2017).
54. Jason Scott Johnston and Todd Zywicki, "The Consumer Financial Protection Bureau's Arbitration Study: A Summary and Critique" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, August 2015).

Title IX includes a number of enforcement-related provisions. Some of these—such as permitting collateral bars for different types of SEC registrants—have contributed to the SEC's ability to protect investors, but others have raised due process concerns.[55] For example, Dodd-Frank expanded the SEC's authority to impose penalties in administrative proceedings—enforcement cases run through the SEC's in-house tribunal rather than a federal court. After making active use of its authority, the SEC has faced a number of challenges to the legality of its administrative proceedings.[56] To address due process concerns, policymakers might consider retracting the expanded penalty authority in Dodd-Frank and adding protections for subjects of administrative proceedings. The infamous Madoff Ponzi scheme highlighted the valuable role that whistleblowers can play in rooting out fraud.[57] In response, Dodd-Frank established a new program for rewarding and protecting SEC whistleblowers. While this program (and a similar one at the CFTC) has generated useful information and should be retained, certain elements—particularly mandatory minimum payouts and permissible circumvention of internal reporting channels—should be studied in the light of the agencies' experience with their whistleblower programs.[58]

Title IX addresses credit ratings, which contributed to the crisis by masking asset risks and dissuading market participants from engaging in their own due diligence. Dodd-Frank took the positive step of requiring the removal of mandates to use credit ratings from statutes and regulations; these government mandates encouraged financial institutions to rely blindly on credit ratings.[59] Another part of Title IX, however, counteracts the positive effect of removing rating mandates. Title IX created a new credit ratings bureaucracy within the SEC, which encourages reliance on ratings and the government regulators that oversee them.[60] Title IX also gives the SEC authority to establish a system to assign credit ratings, which would further solidify the dependence of the credit rating industry on the SEC's seal of approval and accordingly diminish the incentive for ratings users to make their own assessments of the rating agencies.

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55. To the extent the SEC has exercised its collateral bar authority retroactively, due process concerns also exist. See, for example, Gregory Bartko v. Securities and Exchange Commission, Case No. 14-1070, --- F.3d ---, (D.C. Circuit, January 17, 2017).
56. See, for example, Bandimere v. SEC, No. 15-9586, 2016 WL 7439007, --- F.3d --- (10th Cir., December 27, 2016); Raymond J. Lucia Cos., Inc. v. SEC, 832 F.3d 277 (D.C. Cir. 2016).
57. Harry Markopolos, *No One Would Listen: A True Financial Thriller* (Hoboken, NJ: John Wiley & Sons, 2010).
58. Hester Peirce, "Blowing the Whistle on Whistleblowers," *RealClearMarkets*, September 26, 2012.
59. White, "An Assessment of the Credit Rating Agencies."
60. Peirce and Broughel, eds., *Dodd-Frank: What It Does and Why It's Flawed*, 102–103.

In addition to reforming credit ratings, Title IX attempts to improve securitization by requiring securitizers to retain "skin in the game." The "skin-in-the-game" problem was created by the Recourse Rule, which was finalized in late 2001 to encourage securitization but discourage risk-taking.[61] By setting risk-weighted capital requirements for securitizations according to credit ratings, the Recourse Rule pushed banks to hold the highest-rated tranches, which suffered catastrophic losses during the crisis.[62] In any event, the final rules are complex and riven with exceptions, including one for securities backed by Fannie Mae and Freddie Mac. A better approach, particularly in light of Dodd-Frank's provisions strengthening disclosure and representations and warranties, would allow risk retention to be a matter of private contract. More fundamentally, non-risk-based capital requirements could diminish the incentive to securitize assets.[63]

Another major objective of Title IX is to expand the SEC's role in managing how companies are governed. The provisions requiring companies to allow shareholders nonbinding votes on executive compensation and golden parachutes, independence requirements for compensation committees, and proxy access authorization[64] fall into this category. Rather than eliminating competition among states in corporate chartering by federalizing corporate law, policymakers should look for ways to enhance competition, including allowing corporations to select charters that are tailored to their business model or industry.[65] In revising this portion of Title IX, policymakers should take a close look

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61. For a detailed discussion of the Recourse Rule, see Jeffrey Friedman and Wladimir Kraus, *Engineering the Financial Crisis: Systemic Risk and the Failure of Regulation* (Philadelphia: University of Pennsylvania Press, 2011).
62. For a discussion of why banks involved in securitizing assets held the highest-rated tranches, see Isil Erel, Taylor Nadauld, and René Stulz, "Why Did Holdings of Highly Rated Securitization Tranches Differ So Much across Banks?," *Review of Financial Studies* 27, no. 2 (2014): 404–53. Miller, "The Recourse Rule, Regulatory Arbitrage, and the Crisis," shows that it was the largest securitizing banks that increased their holdings of the highest-rated tranches the most, which explains why the largest banks featured prominently during the crisis.
63. See, for example, Thomas L. Hogan, Neil Meredith, and Xuhao Pan, "Evaluating Risk-Based Capital Regulation" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, January 2013); Arnold Kling, "Risk-Based Capital Rules," in *Reframing Financial Regulation*, ed. Peirce and Klutsey. See also Miller, "The Recourse Rule, Regulatory Arbitrage, and the Crisis," which shows that after the Recourse Rule was finalized, large securitizing banks increased their holdings.
64. For a discussion of proxy access, see Bernard S. Sharfman, "What Theory and Empirical Evidence Tell Us about Proxy Access" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, August 2016).
65. See, for example, J.W. Verret, "Uber-ized Corporate Law: Toward a 21st Century Corporate Governance for Crowdfunding and App-Based Investor Communications," *Journal of Corporation Law* 41, no. 4 (2016): 101–43.

at the related issue of the degree to which regulation has caused undue reliance on proxy advisers.[66]

The social disclosure provisions in Titles IX and XV of Dodd-Frank merit reconsideration. These provisions burden and distract both the SEC and issuers without clear benefit for the investors that pay for them. They require companies to make disclosures related to arbitrary employee compensation ratios, conflict minerals, resource extraction, and mining. In addition to forcing the SEC to regulate outside of its traditional bailiwick, these provisions have had harmful consequences.[67] The SEC's disclosure requirements more traditionally have served investors by providing them material information related to corporate value maximization.[68]

Title IX contains a section on municipal securities, which should be an important area of focus for the SEC because of the size of the market and the heavy participation by retail investors. The particular changes made by the statute warrant reconsideration with an eye toward identifying the problems in this market and assessing whether Dodd-Frank's solutions are working and when additional legislative changes are needed. Among other things, policymakers should review the structural changes to the Municipal Securities Rulemaking Board made by Dodd-Frank and the new municipal adviser registration regime.[69] Any review should take into account events since the passage of Dodd-Frank, including the Puerto Rican debt crisis[70] and the SEC's enforcement activity against municipal debt issuers.

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66. James K. Glassman and J.W. Verret, "How to Fix Our Broken Proxy Advisory System" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, April 2013); James K. Glassman and Hester Peirce, "How Proxy Advisory Services Became So Powerful" (Mercatus on Policy, Mercatus Center at George Mason University, Arlington, VA, June 2014).
67. For a discussion of some of these harms, see David Burton, "How Title XV Mandated Disclosures Harm, Rather than Protect, Investors," in *The Case Against Dodd-Frank*, ed. Michel; Dominic P. Parker and Bryan Vadheim, "Resource Cursed or Policy Cursed? US Regulation of Conflict Minerals and Violence in the Congo," *Journal of the Association of Environmental and Resource Economists* 4, no. 1 (2017): 1–49. See also Peirce and Broughel, eds., "Title XV: Requirements for Nonfinancial Companies," in *Dodd-Frank: What it Does and Why It's Flawed*, 153.
68. J.W. Verret, "The Securities Exchange Act Is a Material Girl, Living in a Material World: A Response to Bebchuk and Jackson's 'Shining Light on Corporate Political Spending,'" *Harvard Business Law Review* 3, no. 1 (2013): 453–71.
69. Peirce and Broughel, eds., *Dodd-Frank: What It Does and Why It's Flawed*, 105–6.
70. See, for example, Marc D. Joffe and Jesse Martinez, "Origins of the Puerto Rico Fiscal Crisis" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, April 2016); J.W. Verret, "Draft Bill for Puerto Rico Will Only Hurt the Island," *The Hill*, April 8, 2016; J.W. Verret and Marc Joffe, "Should Puerto Rico Be Allowed to Restructure Its Debt? A Mercatus Debate" (Policy Brief, Mercatus Center at George Mason University, Arlington, VA, April 2016).

Title X of Dodd-Frank established the Bureau of Consumer Financial Protection (CFPB) to regulate providers of consumer financial products and services. The structure of the CFPB and its actions have raised questions about its legitimacy and constitutionality. The CFPB's structure—a single director who is removable only for cause, funded but not overseen by the Fed, granted extraordinary discretion in interpreting its statutes—makes it uniquely independent from accountability.[71] In light of these bureaucratic peculiarities, the Court of Appeals for the DC Circuit recently held that the CFPB's design is unconstitutional.[72] As might be expected for an agency that answers to no one, the CFPB has taken actions that raise concerns about due process, jurisdictional overreach, and research integrity.[73] A commission structure, congressional appropriations, a more rigorous economic analysis requirement, and a narrower jurisdiction would help to moderate the CFPB's actions and make them more consistent over time, which would in turn provide welcome predictability to regulated entities and their customers and investors.[74] Eliminating the CFPB and transferring its appropriately narrowed responsibilities[75] to the other banking agencies and the Federal Trade Commission may be necessary given that the CFPB's bad habits—developed over half a decade—could be difficult to root out. Title X also includes the controversial Durbin

71. Todd Zywicki, "The Consumer Financial Protection Bureau: Savior or Menace?," *George Washington Law Review* 81, no. 3 (2013): 856–928.
72. PHH Corp. et al. v. Consumer Financial Protection Bureau, No. 15-1177 (D.C. Cir., Oct. 11, 2016).
73. See, for example, Todd Zywicki, "Assessing the Effects of Consumer Finance Regulations" (Testimony before the Senate Committee on Banking, Housing, and Urban Affairs, Law & Economics Center, George Mason University School of Law, Arlington, VA, April 5, 2016); Hester Peirce, "Increasing the Effectiveness of the Bureau of Consumer Financial Protection in Protecting Consumers" (Testimony before the Financial Institutions and Consumer Credit Subcommittee of the House Financial Services Committee, Mercatus Center at George Mason University, Arlington, VA, May 21, 2014); Hester Peirce and Vera Soliman, "Disclosure of Consumer Complaint Narrative Data" (Public Interest Comment, Mercatus Center at George Mason University, Arlington, VA, September 10, 2014); Johnston and Zywicki, "The Consumer Financial Protection Bureau's Arbitration Study"; Thomas W. Miller Jr., Todd Zywicki, and Brian Knight, "Comment on the CFPB's Rule on Payday, Vehicle Title, and Certain High-Cost Installment Loans" (Public Interest Comment, Mercatus Center at George Mason University, Arlington, VA, October 7, 2016).
74. Brian Knight, "Court Rulings Bruise Consumer Financial Protection Bureau's Authority," *The Hill*, May 2, 2016.
75. Among other things, the new authority should clearly circumscribe jurisdictional reach, avoid the ill-defined term "abusive" acts and practices introduced by Dodd-Frank, and limit consumer data collection. See, for example, Hester Peirce, "CFPB Knows Abuse When It Sees It," Expert Commentary, Mercatus Center at George Mason University, March 29, 2012; Zywicki, "Assessing the Effects of Consumer Finance Regulation."

Amendment, which should be reconsidered in light of evidence that it has not helped consumers as intended.[76]

Title XI makes changes to the Federal Reserve's governance and its emergency lending authority. On the governance side, Title XI creates a new vice chairman for supervision, a position that has not yet been filled. If the Federal Reserve retains its regulatory and supervisory powers, the position should be retained and filled to establish some measure of accountability for the Fed's exercise of these authorities. Title XI also changes the way in which the Federal Reserve district bank presidents are chosen. Concerns about potential conflicts of interest are better addressed by not asking the Federal Reserve to engage in regulatory policy and credit allocation, the areas in which the conflicts arise.[77] In making reforms in this area, policymakers should consider the important insights that the district banks, which maintain relationships with banks and businesses throughout the United States (and outside of Washington, DC), have on monetary policy.[78]

With respect to emergency lending, Title XI mandates some public transparency in emergency lending and limits the Fed's authority in Federal Reserve Act section 13(3) by requiring that such lending be broadly available—not targeted to a single company.[79] The Federal Reserve's implementing rule chafes against these new restrictions by reserving for the Fed as much latitude as possible to engage in emergency lending.[80] The objectives of section 13(3) are better met through standard monetary policy tools that provide system-wide liquidity,

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76. Todd J. Zywicki, Geoffrey A. Manne, and Julian Morris, "Price Controls on Payment Card Interchange Fees: The US Experience" (Financial Regulatory Research Program White Paper 2014-2, International Center for Law and Economics, Portland, OR, 2014).
77. See Lawrence H. White, "Ending the Federal Reserve's Overreach into Credit Allocation" (Testimony before the Subcommittee on Monetary Policy and Trade of the House Financial Services Committee, Mercatus Center at George Mason University, Arlington, VA, March 12, 2014), 5–6. Professor White explains, "Potential conflicts of interest can be entirely avoided while retaining the FRB member banks' desirable indirect input into monetary policy via the FRB presidents only by removing the Fed entirely from credit allocation. If the Fed gives no institution favored credit allocation treatment in the form of a bailout or concessionary loan, it does not matter which institutions are represented on an FRB's board of directors."
78. Dino Falaschetti and Chad Reese, "Come Together, over the Fed?," *The Hill*, March 3, 2015. The authors explain that "better aligning the incentives of monetary policy-makers with productive policy objectives could establish a stronger first line of defense against monetary mischief."
79. See James Broughel, "Fed Transparency and Bailouts," in *Dodd-Frank: What It Does and Why It's Flawed*, ed. Peirce and Broughel, 120–33.
80. Extensions of Credit by Federal Reserve Banks, 80 Fed. Reg. 78959 (proposed December 18, 2015). For some of the concerns with the Federal Reserve's approach, see, for example, comments by J.W. Verret, summarized in Martin Neil Baily and John B. Taylor, eds., *Across the Great Divide: New Perspectives on the Financial Crisis* (Stanford, CA: Hoover Institution Press, 2014), 371.

rather than directing aid to specific companies.[81] Policymakers should consider additional actions to regularize monetary policy, including bounded discretion, meaningfully increased transparency, and subjecting the Fed's actions to a market check.[82]

Title XII seeks to increase "access to mainstream financial institutions," but it does this by subsidizing bank lending to low- and moderate-income individuals. A preferable approach would be to expand unsubsidized private lending by lowering regulatory and litigation obstacles.[83] Eliminating or reforming the CFPB, which—along with other legal and regulatory developments—has heightened the legal risk of engaging with low- and moderate-income customers (or at least restructuring it to facilitate accountability), would help.[84] Also helpful in this regard would be a mandate to regulators to provide the flexibility necessary to accommodate innovation in the customer financial services space, rather than using rules and enforcement actions as a signal to would-be innovators that serving low- and moderate-income consumers carries with it heightened legal liability. Lowering regulatory barriers to entry and reducing the regulatory privileges enjoyed by incumbent financial institutions are two ways to invite innovators to offer consumer financial services to underserved populations.[85]

Titles XIII and XIV represent missed opportunities to deal with housing finance. Title XIII generates a report on housing finance reform, but no actual housing reform. Title XIV makes extensive changes in the rules governing mortgage lending, including new rules for mortgage originators and the new qualified

81. See Norbert J. Michel, "Title XI Does Not End Federal Reserve Bailouts," in *The Case against Dodd-Frank*, ed. Michel, 173–74.
82. See, for example, David Beckworth and Joshua R. Hendrickson, "Nominal GDP Targeting and the Taylor Rule on an Even Playing Field" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, October 2016); Alexander William Salter, "An Introduction to Monetary Policy Rules" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, December 2014); Mercatus Center, "Monetary Rules for a Post-Crisis World," September 7, 2016; Scott Sumner, "A Market-Driven Nominal GDP Targeting Regime" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, July 2013).
83. See, for example, Thomas W. Miller Jr. and Harold A. Black, "Examining Arguments Made by Interest Rate Cap Advocates," in *Reframing Financial Regulation*, ed. Peirce and Klutsey; Todd J. Zywicki, "Market-Replacing versus Market-Reinforcing Consumer Finance Regulation," in *Reframing Financial Regulation*, ed. Peirce and Klutsey.
84. See, for example, Brian Knight, "Court Rulings Bruise Consumer Financial Protection Bureau's Authority." See also Brian Knight, "Risks to Innovative Credit Posed by Emerging Regulatory and Litigation Trends" (Mercatus on Policy, Mercatus Center at George Mason University, Arlington, VA, January 2017).
85. Brian Knight, "Regulating FinTech: Creating a Regulatory Regime that Enables Innovation While Providing Appropriate Consumer Protection" (Reply Comment, Mercatus Center at George Mason University, Arlington, VA, May 12, 2016).

mortgage rules that heighten liability for mortgages disfavored by policymakers.[86] The new layer of regulatory complexity is expensive and burdensome, but it may not be effective at reducing defaults.[87]

Neither Title XIII nor Title XIV tackles the difficult but core issue of ending the government's involvement in housing finance. Market discipline does not kick in when taxpayers are on the hook for sloppy underwriting, so poor mortgage practices will persist until the government backstop is gone. Rather than relying on the federal government to set mortgage standards, reforms in this area would make the private market responsible for financing mortgages and establishing and enforcing proper underwriting standards.[88] Although certain types of mortgages, such as 30-year fixed mortgages, might be less common and more expensive in a privatized housing finance market, other types of mortgages likely would emerge.[89]

CONCLUSION

Repealing Dodd-Frank entails rethinking the prevailing perspective on financial regulation and making specific, substantive changes. Dodd-Frank relies on regulators to run the financial system by elevating their judgment over the decisions of the individuals and firms with access to the best, most up-to-date information and with the most at stake. Financial reform should restore decision-making and the consequences of those decisions to their rightful place, and it should allow regulators to be regulators, not central planners. Substantively, the complexity of Dodd-Frank should give way to simple, well-enforced rules that lower barriers to competition, accommodate innovation, and eliminate both the expectation and possibility of bailouts. Only then will the financial system effectively and safely serve consumers, businesses, investors, and the economy.

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86. For a more comprehensive discussion of Title XIV, see Mark A. Calabria, "Title IX Subtitle D and Title XIV: Likely to Increase Cost of Mortgage Credit and Increase Foreclosures," in *The Case against Dodd-Frank*, ed. Michel.
87. Ibid., 190.
88. For a discussion of potential approaches to reforming housing finance, see Satya Thallam, ed., *House of Cards: Reforming America's Housing Finance System* (Arlington, VA: Mercatus Center at George Mason University, 2012).
89. See, for example, Michael Lea and Anthony Sanders, "Do We Need the 30-Year Fixed-Rate Mortgage?" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, March 2011).

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