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Dodd-Frank: Navigating a Complicated Financial World

Center Forward Basic
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Overview

Dodd-Frank, officially called the Dodd-Frank Wall Street Reform and Consumer Protection Act (Public Law 111-203), is major legislation signed by President Obama in July 2010, designed in the aftermath of the "Great Recession" of 2007-2009.

This wide-sweeping legislation affects nearly every aspect of the U.S. financial system, from the operations of banks, investment, private equity and hedge fund firms to the administration of mortgages and credit cards. Given recent discussions about reforming pieces of this legislation (most notably from the Trump Administration in a recent executive order), this Basic outlines some of the main components of the law.

Roots of the Legislation

President Obama, with a Democratic-led Senate and House, took the lead in drafting this massive legislation. In the final vote, no Republicans voted for the legislation in the House, and only three Republicans did so in the Senate. As such, the outcome has always been viewed as highly partisan and in the crosshairs of many Republican lawmakers. The legislation is named after former Senator Chris Dodd, then chairman of the Senate Banking Committee and former Representative Barney Frank, then chair of the House Financial Services Committee. *Please see our "Resources" sidebar for a link to the full text of the legislation.*

What Dodd-Frank Did

Some of the major items in Dodd-Frank include:

- **Financial Stability Oversight Council (FSOC):** The FSOC is "charged with identifying risks to the financial stability of the United States; promoting market discipline; and responding to emerging risks to the stability of the United States' financial system." It's members include the Board of Governors of the Federal Reserve System, Commodity Futures Trading Commission, Federal Deposit Insurance Corporation, Federal Housing Finance Agency, National Credit Union Administration, Office of the Comptroller of the Currency, Securities and Exchange Commission and the Consumer Financial Protection Bureau. It is chaired by the Treasury Department.
- **Consumer Financial Protection Bureau (CFPB):** The CFPB greatly expanded the government's role in regulating and punishing companies deemed to have harmed consumers. This covers activities by banks, payday lenders, credit reporting agencies and debt collectors to name a few. They regulate a variety of fees paid by consumers, including credit, debit, general

Key Facts

Due to the financial crisis that led to the "Great Recession" of 2007-2009, the global economy lost $15 trillion dollars and the Dow Industrial Average dropped over 50 percent.

Dodd-Frank, among other things, did the following: created the Financial Stability Oversight Council, the Consumer Financial Protection Bureau, and the Federal Insurance Office; established the "Volker Rule", stricter regulation of derivatives; established "stress tests" for banks; increased supervision of credit rating agencies; and, expanded whistleblower protections.

In early February 2017, the Trump Administration issued an executive order asking federal agencies to identify laws and regulations that may negatively impact America's financial system.

bank and mortgage underwriting fees. The CFPB also works to educate consumers about a variety of financial products like mortgages.

- **Federal Insurance Office (FIO):** Housed within the Treasury Department, the FIO "has the authority to identify issues or gaps in the regulation of insurance that could contribute to a systemic crisis in the insurance industry or broader US financial system."
- **The "Volker Rule":** One of the most contentious pieces of the legislation and named after former Federal Reserve Chair Paul Volker, it bars banks from investing in, or owning, hedge and private equity funds for their own profit.
- **"Stress Tests":** On an annual basis, the Federal Reserve conducts a "stress test" for all banks with over 50 billion dollars in assets. In 2016, this included 33 institutions. These tests are meant to assess a bank's ability to deal with various economic scenarios such as high unemployment or a drop in the stock market. Banks are required to submit a report to the Federal Reserve who then in turn makes an assessment and gives the bank a pass or fail grade.
- **Derivative Regulation**: Dodd-Frank set up mechanisms for the regulation of certain derivatives, most notably "credit default swaps." These types of derivatives are often blamed as a major cause of the financial crisis.
- **Expanded Whistleblower Protections:** The legislation expanded already existing whistleblower protections in the financial community by broadening who is considered a whistleblower, prolonged the statue of limitations to make a claim from 90-180 days, and provided a mechanism of a possible monetary reward of 10-30 percent if some sort of settlement is reached.
- **Regulation of Credit Rating Agencies (CRAs):** Dodd-Frank included increased supervision of CRAs. Both corporations and governments issue debt to raise funds. They do so through a host of debt instruments, such as corporate, government and municipal bonds, CDs and mortgage-backed securities. CRAs evaluate these debt issuers' ability to pay back these "loans" and give them a rating, which then can affect the interest rate of the debt instrument being utilized.

Criticisms

A major criticism of Dodd-Frank is that it is too far-reaching and is hurting America's ability to compete globally with other countries that have less stringent policies. Some critics say it creates undue strains on the financial sector at a time when the focus should be on creating jobs. On the other side, some note that Dodd-Frank has helped bring the nation out of the recession, with unemployment rates decreasing.

Resources

The Dodd-Frank Wall Street Reform and Consumer Protection Act. Final Legislative Text.

Board of Governors of the Federal Reserve. Dodd-Frank Regulatory Reform Website.

American Bankers Association Dodd-Frank Resource Center.

About Center Forward

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