Our Perspectives:
Commentary on the economy & regulatory policies affecting financial companies

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It's Not Just the Cabinet Positions That Count*

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Every once in a while there is a new president elected and the scramble begins among prognosticators and transition teams to predict or select the individuals what will lead the new administration. Well that there should be such a scramble because there are a lot of positions to fill. Most of the focus, however, is on a very few positions — the heads of Treasury, State, the Office of the Attorney General, Chief of Staff of the White House, and similar high profile positions. From the perspective of the financial services industry, other offices not quite so visible are at least as important and the industry will be looking carefully at who will be selected for those positons.

Consumer Financial Protection Bureau. One of the most important governmental positions for carrying out presidential policy vis-a-vis consumers is the Director of the Consumer Financial Protection Bureau. The scope of the agency is extremely broad, covering financial products and services that effect consumers in nearly every sector. The director has ramped up its staffing quickly in the few years of its existence. Its regulatory arm has churned out a massive number of regulations in a relatively short period of time, and its enforcement arm is innovative and aggressive.

There are assertions that the actions of the Bureau, both in the regulatory and enforcement spheres, have led to tightened credit and consequently a reduction in the amounts that are allocated to particular groups of citizens. It is also asserted that the actions have led to very sound prudential books of business for the industry; for example, delinquencies in mortgages are nearly back to what could be argued is "normal" for the industry. Part of the reason the changes have occurred has been the regulations themselves, but in addition it would be necessary to conclude that a significant part has been the threat of prosecution by the Bureau or its ally, the Department of Justice. Fines and penalties have been very large.

The tone and direction for the Bureau is set in the first instance by the president, of course, but on a regular day by day basis, it is set by the Director of the Bureau. Changing the Director would most likely lead to a reconsideration of the balance in the Bureau between protection of

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consumers and providing to those same consumers an environment in which they could get the financial products and services they need. With only a few tweaks to regulations and a less hawkish approach to enforcement (currently, the industry sees the Bureau as always believing it is composed only of "bad guys") more credit would be made available to deserving borrowers.

There is some question whether the president could remove the Director at will or whether the current incumbent had the right to continue in office until the end of his appointed term in 2018. That issue is currently before the federal courts, and in the most recent decision, a federal court of appeals has said that the president has the right to remove the Director without cause. It is likely that the new administration would take this position also, and while the Democrats in the Senate could stall any confirmation of a new appointee, an Acting Director, one who doesn't need Senate approval, could serve to perform the tasks deemed necessary by the new administration.

Heads of other financial services agencies. In most changes of administration, the heads of financial regulatory agencies are replaced, generally with the concurrence of both the administration and the incumbent. That is not always the case however, and to the extent that one or more of the offices is not seen as actively engaged in policies contrary to those of the administration, it has been the practice to let those heads continue until the end of their fixed terms. Whether the president could utilize the decision of the court of appeals that addressed the term of the Director of CFPB to remove one or more with fixed term appointments is not clear.

Most of the noise about heads of financial services agencies has been concerned with CFPB, not the other agencies. While there have been some complaints by one senator recently about the head of the SEC, any discussion about the continuation of the Chair in that position was canceled when the Chair announced that she had submitted a letter of resignation to the President. There had been pressure from some sources to persuade that agency to punish individuals in large corporations directly rather than simply fining the corporations themselves. How that policy positon might be addressed remains unclear.

One possible target of the new administration could be the Director of the Federal Housing Finance Agency. If the new administration wants to move rapidly with new ideas on the conservatorship or receivership of the GSEs, it would be best to start with a new Director. By and large the current incumbent has not received serious criticism from either industry or the activists groups, however, and it could be that the incumbent and the new administration could reach agreement on the kinds of changes needed. From the perspective of financing one of the largest segments of our economy, however, this position is directly in the bullseye.[1]

Smaller banks care a lot about the positons of the FDIC, of course, but the current Board and Chairman have not provoked any widespread anguish in that sector; small banks' concerns are with the rules under which they have to operate and the perceived disadvantage they have compared with larger banks. The FDIC does not receive criticism on those fronts.

The Federal Reserve System, National Economic Council, Treasury subordinate secretaries, Office of Foreign Assets Control, et al. The financial services industry deals with many other parts of the government, of course, such as the Internal Revenue Service, Export-Import Bank, Office of Foreign Trade, National Economic Council, the assistant secretaries at Treasury, Office of Foreign

[1]See the discussion of the PHH case and the position of the Director of FHFA in this issue: Implications of the PHH Ruling on the Federal Housing Finance Agency, by Ray Natter.

Assets Control, and a variety of others. One of the most significant of all of these other offices is the Federal Reserve System in its many ramifications, and in particular, the Board of Governors.

It is possible that the independence of the Federal Reserve System could come under attack from both the left and the right during the coming year. Not only do populists generally resist the domination of the Federal Reserve on monetary policy, if any agency epitomizes the isolated secretive working of Washington, the Federal Reserve would have to be considered one of the most likely candidates for that honor. Of course, for the financial sector, the Federal Reserve, and not just the Board of Governors, is crucial to the structure of its members and many of their activities. Many see the Federal Reserve as not sufficiently hostile to that sector.

Currently, the Board of Governors is short two members, with its membership at five instead of seven. The Board can act with five or fewer members, but it presents serious problems if the number is fewer than four. With four members, a quorum of the Board would be three members, and since a great deal of the work of the Board is done through its three member committees, the Government in the Sunshine Act would require that much of the confidential work of the Board would be open to the public and subject to seven days' notice when a quorum of the Board is present at the meeting. With the present five members, a quorum is four so meetings of the committees would not be subject to that Act and sensitive issues can be discussed confidentially among Board members. Should a member resign, however, the Board would be in the difficult position of having only four Board members. Of course, for some commentators, requiring the committees of the Board to operate in open meetings might be just what they would like to see.

The Treasury Department operates through a number of Assistant Secretaries. They cover all aspects of the department and to list them is to understand how important they are to the financial services industry: Domestic Finance, Economic Policy, International Affairs, Office of Financial Research, Office of Financial Stability, Tax Policy, and Terrorism and Financial Intelligence. Of course they each report to the Secretary directly or indirectly, but by and large they are expected to run their divisions without additional assistance. Yet, while great attention is spent on worrying about who will run the department, less concern is shown early in the process for who might run those divisions. One could argue that those assignments make a greater difference to the financial services industry than the appointment of the Secretary.

<u>Summary</u>. There are other departments that, on specific issues, are crucial to the operation of the businesses and consumers in our economy. HUD, HEW, Department of Education, Commerce — these and many others fill that bill. Within each of these there are bureaus of subordinate offices that interact with the financial services industry on a regular basis. Take FHA or Ginnie Mae in housing for example, or student lending within the Department of Education.

Together these and others not listed are managed by individuals who often receive their assignments without any display of substantial public interest. Yet, they are the most crucial managers in the relationship between the Federal Government and the public.

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