CENTER ON FINANCE, INSURANCE, AND REAL ESTATE
RESEARCH & COMMENTARY
THE HEARTLAND INSTITUTE

Research & Commentary: Early Effects of Dodd-Frank

The Wall Street Reform and Consumer Protection Act, also known as the Dodd-Frank Act, created many new restrictions on financial instruments and activities. The new regulatory powers include a consumer protection agency and the creation of a single federal bank regulator.

The act replaces market-based financial monitoring with government bureaucracies, many of which lack oversight and are completely unaccountable for their actions or budgets. Dodd-Frank also fails to address the problems of Fannie Mae and Freddie Mac, the two government-sponsored entities that guarantee much of the nation's mortgage debt and which many observers say contributed greatly to the real estate bubble that led to the current economic downturn.

Supporters of the new regulations argued the prior regulatory system did not do enough to prevent or mitigate the financial crisis. But the new regulations and bureaucracies under Dodd-Frank will do little to prevent future crises. Dodd-Frank places great faith in regulators' ability to predict and detect problems that could affect financial markets, but these regulators include many of the people who missed the systemic problems that led to the crisis.

Opponents of Dodd-Frank say the new policies repeat many of the government's mistakes while failing to address the most pressing problems of the previous regulatory system. Although parts of the new regulatory system under Dodd-Frank remain unimplemented, we are now beginning to see some of the economic effects of the implemented regulations.

These new regulations have put smaller financial companies at a disadvantage, leading to further industry consolidation. The creation of additional regulatory barriers to lending and higher capital requirements for banks have made new credit less available to investors and entrepreneurs. The new rules also threaten to increase the prices consumers pay for their products while curbing the products and services offered. A good example of this is the debit card and interchange fees regulated under Dodd-Frank; because the government limits the fees banks can charge their customers for certain services, banks make up for the lost revenue by increasing other fees or cutting services.

Dodd-Frank repeats many of the government's recent mistakes in housing finance, imposes needless new regulatory burdens, and fails to address the most pressing problems. Good financial policy allows the market to grow and thrive while protecting consumers and investors from unscrupulous business practices. Risk will always exist, and the government cannot regulate it away. Efforts to do so only cause further harm.

Legislators should oppose new regulations and the creation of new bureaucratic agencies that distort the market both before and after implementation.

The following articles examine Dodd-Frank and its effects on financial markets and the economy.

Dodd-Frank: What It Does and Why It's Flawed
http://mercatus.org/publication/dodd-frank-what-it-does-and-why-its-flawed
In this book, Hester Peirce and James Broughel of the Mercatus Center closely consider some Dodd-Frank provisions in an effort to assess the act's efficacy. Looking behind the act's celebrated objectives shows it fails to achieve many of its stated goals, reinforces dangerous regulatory pathologies that became evident during the last crisis, and creates new pathologies that could lay the groundwork for the next crisis.

10 Ways Dodd-Frank Will Hurt the Economy in 2013
http://www.usnews.com/opinion/blogs/economic-intelligence/2013/01/07/10-ways-dodd-frank-will-hurt-the-economy-in-2013
Writing in *US News and World Report*, Hester Peirce of the Mercatus Center outlines Dodd-Frank's shortcomings, arguing the hastily written law could do widespread economic harm. "As Dodd-Frank comes to life, its harmful effects will come into plain view," she writes. "Solutions crafted without a clear focus on the problems that need fixing can create new, even more severe consequences."

Dodd-Frank: The Economic Case for Repeal
http://american.com/archive/2012/june/op-ed-on-dodd-frank/
Peter Wallison of the American Enterprise Institute examines the effect of Dodd-Frank on GDP and makes an economic case for its repeal: "As the second anniversary of the act approaches, its role in slowing our economic recovery is coming into focus. GDP growth shrunk immediately after the law passed and has never recovered, while key terms in the law remain undefined."

Dodd-Frank: Two Years Later, Countless Questions Remain
http://mercatus.org/expert_commentary/dodd-frank-two-years-later-countless-questions-remain
On the second anniversary of the passage of Dodd-Frank, Hester Peirce and James Broughel of the Mercatus Center examine several of the problems with the measure.

Did the Dodd-Frank Act Fail?
http://www.aei.org/article/economics/financial-services/banking/did-the-dodd-frank-act-fail/
Alex J. Pollock of the American Enterprise Institute argues the greatly increased bureaucracy and regulation mandated by Dodd-Frank will not prevent another crisis. The act failed to address in any way the concentrated, duopoly system of Fannie Mae and Freddie Mac. When considering the costs and benefits of proposed regulations, lawmakers should specifically take into account their effects on competition, Pollock writes.

The Dodd-Frank Act: Creative Destruction, Destroyed
http://heartland.org/policy-documents/dodd-frank-act-creative-destruction-destroyed
This *Financial Services Outlook* paper from the American Enterprise Institute discusses several of the most serious policy problems created by the Dodd-Frank Act.

The Dodd-Frank Wall Street Reform & Consumer Protection Act of 2010: Is It Constitutional?
http://heartland.org/policy-documents/dodd-frank-wall-street-reform-consumer-protection-act-2010-it-constitutional
C. Boyden Gray and John Shu of the Federalist Society consider the constitutional issues raised by three of the Dodd-Frank Act's central grants of regulatory power: the Financial Stability Oversight Council and its powers in Title I, the Federal Deposit Insurance Corporation's related liquidation authority in Title II, and the Bureau of Consumer Financial Protection in Title X.

The Consumer Protection Financial Bureau: Savior or Menace?
http://heartland.org/policy-documents/consumer-protection-financial-bureau-savior-or-menace
Todd Zywicki provides a short history of the Consumer Financial Protection Bureau (CFPB) and of consumer credit regulation in America, including many of the lessons researchers have learned from decades of bureaucratic design. The CFPB's structure ignores many of these lessons, Zywicki writes. He outlines several problems that plague bureaucratic organizations and explains why the CFPB will be particularly vulnerable to these failings, absent significant reform.

Towards an Alternative Regulatory Culture
http://reason.org/news/show/alternative-regulatory-culture-dodd
Anthony Randazzo of the Reason Foundation discusses several problems with the Dodd-Frank regulations and suggests how to solve them.

Dodd-Frank Not Likely to End Bailouts as Promised
http://news.heartland.org/newspaper-article/2012/07/16/dodd-frank-not-likely-end-bailouts-promised
Thomas Jacobs of DePaul University argues in this *Heartlander* digital magazine article that the Dodd-Frank regulations are unlikely to end bailouts. "Bailouts are an attempt to prevent something worse such as the collapse of the financial system," he writes. "As there is no test to confirm the systemic risk of a financial firm in advance, a regulator will choose taxpayer-funded support of the firm over risking the demise of the financial system. Although the Boxer amendment to Dodd-Frank prevents the use of taxpayer funds to avoid liquidation of troubled financial firms, Dodd-Frank and its regulatory implementation to date leave plenty of bailout loopholes. Consider three mechanisms: markets with inherent systemic risk, the regulation of firms prior to financial distress, and the resolution of distressed firms."

The New Financial Deal: Understanding the Dodd-Frank Act and Its (Unintended) Consequences
http://heartland.org/policy-documents/new-financial-deal-understanding-dodd-frank-act-and-its-unintended-consequences
David A. Skeel Jr. of the University of Pennsylvania Law School examines the various components of Dodd-Frank and how they are intended to work. He suggests several simple bankruptcy reforms that would curb the excesses of the new government-bank partnership, plus ways to address international dimensions of the new financial order he maintains Dodd-Frank largely neglected.

The Dodd-Frank Act: A Flawed and Inadequate Response to the Too-Big-To-Fail Problem
http://heartland.org/policy-documents/dodd-frank-act-flawed-and-inadequate-response-too-big-fail-problem
Arthur E. Wilmarth Jr. of the George Washington University Law School evaluates whether the new statute is likely to solve the too-big-to-fail problem and discusses several possible alternatives or changes to Dodd-Frank that could solve the problem.

Dodd-Frank: Quack Federal Corporate Governance Round II
http://heartland.org/policy-documents/dodd-frank-quack-federal-corporate-governance-round-ii
Professor Stephen Bainbridge argues the corporate governance provisions in Dodd-Frank qualify as "quack corporate governance." Bainbridge identifies eight attributes of quack corporate governance regulation and finds Dodd-Frank meets several of the criteria.

Research & Commentary: Proprietary Trading and the Volcker Rule
http://heartland.org/policy-documents/research-commentary-proprietary-trading-and-volcker-rule
Matthew Glans of The Heartland Institute examines the proprietary trading and Volcker Rule provisions of Dodd-Frank. The Volcker Rule forces separation of the investment banking, private equity, and proprietary trading sections of commercial financial institutions from their traditional consumer lending divisions. "Critics of the Volcker Rule argue it will be incredibly difficult to enforce, have little effect on systemic risk, and could cut banks' competitiveness," he writes. "The vagueness of the rule could lead banks to undertake even riskier investments, they say. These concerns and others have convinced the Federal Reserve to at least slow implementation of the Volcker Rule."

Research & Commentary: Commodities Position Limits
http://heartland.org/policy-documents/research-commentary-commodities-position-limits
In the 2010 Dodd–Frank Wall Street Reform and Consumer Protection Act, "position limits" on the number of options or futures contracts an investor may hold on any one underlying security were placed on all commodity futures, options, and swaps, to curb speculation some people blamed for the high price volatility of certain commodities, primarily crude oil contracts that affected gasoline prices. In this *Research & Commentary*, Matthew Glans examines commodities position limits, arguing they may do more harm than good.

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