

July 9, 2018



Battles Raging Below

While most would rather be somewhere on a back porch in July, this month promises to be extremely busy and potentially brutal in Washington. The Senate will start to fill the vacancy created on the Supreme Court due to Justice Kennedy's June surprise (not to mention the prospect of being here most of next month) and the long August recess looms large for the House. The appropriations process also will continue to move forward, with a conference expected on the first "minibus" as well as efforts to move other similar packages in both chambers. Outside of the Supreme Court nominee and spending bills, Congress likely only has the bandwidth to do perennial items (flood insurance reauthorization, defense authorization and the Farm Bill are discussed below, but FAA and water resources also must be completed this year) before November 6th. And as we continue to endure a long campaign season, with the repercussions of some results just beginning to be felt, July offers a bit of a respite before we face the last of the primaries next month and in early September ahead of the two-month slog to the mid-terms. We highlight these and other issues below as we preview what we believe will be the focus in Washington this month, subject as always to external or unexpected events that could disrupt the schedule.

Supreme Court Nomination

Any eyes that aren't normally focused on President Trump will be focused on him later today when he is scheduled to announce his nominee to fill the Supreme Court seat vacated by Justice Kennedy. Expect an intense battle over the next few months with heightened rhetoric, accusations, political implications that change by the hour, etc., with an intense focus on where the moderate Republicans (specifically Sens. Collins (R-ME) and Murkowski (R-AK)) and moderate Democrats (specifically those up for re-election in Trump states – Sens. Tester (D-MT), Heitkamp (D-ND), Donnelly (D-IN), Manchin (D-WV) and McCaskill (D-MO)) will be on Trump's pick. With Trump moving quickly to put forth his nominee and Senate Republicans saying they will hold a confirmation vote this fall before the mid-term elections, the vacancy, nominee and process will likely preclude any progress on major legislation this fall.

Heading into today, three names appear to comprise the shortlist: Brett Kavanaugh of the U.S. Court of Appeals for the D.C. Circuit, Amy Coney Barrett of the U.S. Court of Appeals for the Seventh Circuit and Raymond Kethledge of the U.S. Court of Appeals for the Sixth Circuit. Of note, Kavanaugh has heard several cases involving challenges to financial regulations. In 2016, Kavanaugh wrote the opinion for the three-judge panel that found the CFPB's structure to be unconstitutional.

Appropriations

Both the House and Senate will continue to spend a significant amount of time on appropriations bills throughout the remainder of the summer. Members in both chambers have expressed to us that they don't believe President Trump will sign another year-end omnibus and could make a stand on border wall funding, making the process significantly more important this year. We expect both the House and Senate will continue to move "minibus-type" bills. In the Senate, Defense and Labor HHS could be paired together next, while in the House the Financial Services and Interior bills will be on the Floor the week of July 16th. Both chambers have already passed one "minibus" made up of the Energy and Water, Legislative Branch and Military Construction/VA bills, and an official conference will get underway once Congress returns.

SBC/HFSC Activity and Nominations

The Senate Banking Committee (SBC) is expected to consider several Trump nominees this month, with hearings scheduled for President Trump's picks to head the CFPB, the Ex-Im Bank, Ginnie Mae and a commissioner slot on the SEC (additional details on each of these positions can be found at the end of this preview document). Federal Reserve Chair Jerome Powell is also scheduled to testify on July 17th for his semiannual Humphrey-Hawkins hearing. On the other side of the Hill, efforts by House Financial Services Committee (HFSC) Chairman Hensarling (R-TX) to craft a JOBS Act package are expected to continue this month. We expect much of his committee's work will focus on this proposal, including an expected mark-up, which will include bills that were to be considered at the postponed June 27th mark-up, among others. Other issues expected in front of HFSC are discussed below, including Bank Secrecy Act/anti-money laundering and data security. HFSC also will hear Humphrey-Hawkins testimony from Powell the week of July 16th.

Bank Secrecy Act/Anti Money Laundering

HFSC has struggled to find a path forward on BSA/AML legislation. Republican committee members have been unable to reach consensus on what beneficial ownership (BO) language, if any, should be included in the bill. HFSC Chairman Hensarling still considers overall BSA/AML legislation a priority but has told Members that it will not move forward until the BO issue is resolved. We understand that the bill likely would have significant support from Democrats should the collection of BO information be included in the final product, but would not get much bipartisan support without it. The bill could be included in the July markup should the BO issue be resolved. This also continues to largely still be a House exercise, as the Senate Banking Committee has not made any significant progress in this area.

Data Security

The House continues to make slow progress on data security. Our understanding is the process decelerated due to the New York primaries late last month, but staff is hopeful that it will pick up steam again this month. HFSC and the House Energy and Commerce Committee have not resolved differences between their two preferred approaches despite recent attempts by House Republican Leadership. Because of this, HFSC may begin to explore a "plan b" that would not rely on Energy and Commerce jurisdiction. Data security has been a politically tough issue for members – one that pits the financial and retail industries against each other – and committee

leaders generally shy away from such topics leading up to an election. However, Republican Leadership has made clear they intend to move a data security bill if another large data breach occurs this year. Having a “plan b” measure drafted would keep Congress from having to craft reactionary legislation on the fly.

Data security efforts may get a boost from the Trump Administration with the final Treasury Executive Order report (discussed later) expected to touch on security of consumer financial data. Treasury Secretary Mnuchin previously testified before the House Financial Services Committee that he supports a national data security and breach notification standard.

National Defense Authorization Act (NDAA) – CFIUS and ZTE

As if there weren’t enough acronyms in Congress, this year’s national security focused “America first” agenda brought us the convergence of the NDAA, the Committee on Foreign Investment in the United States (CFIUS) and Chinese telecommunications giant ZTE Corporation. Both CFIUS and ZTE are looking to take a ride on this year’s NDAA reauthorization, as the Senate included language on both in its version of the NDAA. Both Chambers have already passed their respective versions of the NDAA, and we expect that they will go to conference shortly after Congress returns this month. Since the Senate CFIUS language was unanimously approved by the Senate Banking Committee, included in the base text of the Senate passed NDAA, and has the support of the Administration, we expect the Senate version to remain in the NDAA conference report, and thus be signed into law later this year.

Earlier this year, the United States banned US companies from selling their products to ZTE because, according to the Commerce Department, ZTE failed to live up to an agreement it entered into for violating U.S. sanctions prohibiting sales to Iran, North Korea, and others. Breaking the supply chain for one of China’s largest companies caused the ZTE issue to be escalated to the Oval Office in the lead up to President Trump’s North Korea summit, prompting the Administration to reach a new deal with China over ZTE – effectively saving its supply chain. Bipartisan outrage erupted in Congress over this new deal and language addressing ZTE was included in both the Senate and House versions of the NDAA (although not identical) as well as many appropriations bills. It remains unclear which provisions impacting ZTE the Administration will support, but given the bipartisan backlash it seems likely there will be language that addresses ZTE in a final bill.

Trade and Tariffs

Whether or not the US will withdraw or join trade agreements and the imposition of tariffs have been fluid topics of President Trump’s term. Trump has either imposed or threatened to impose tariffs on most major trading partners indiscriminately of whether a country is either an ally or adversary, all under the auspices that America has been taken advantage of in trade agreements and our workers have not received a fair shake. Outstanding trade issues include:

- Renegotiation of the North American Free Trade Agreement (NAFTA) – which has likely been made more complicated by the election of Andrés Manuel López Obrador as Mexico’s President, solidifying a shift there to a leftist-nationalist government.
- Section 232 aluminum and steel tariffs against Canada, Mexico, and the EU – further complicating NAFTA.

- China – which may or may not be subject to tariffs as a result of a Section 301 investigation into unfair trade practices, tariffs as a result of the current trade deficit, investment restrictions through a Congress-passed enhanced CFIUS process, or others.
- Brexit – with implications for trade with the EU and a potential bilateral trade deal with the UK.
- WTO – Numerous WTO challenges to tariffs by various countries. Additionally, the Administration is developing draft legislation to provide the President more discretion to apply tariffs differently for different countries.

Housing Finance

June was a surprisingly busy month for housing finance developments, as we saw the Trump Administration and the Federal Housing Finance Agency (FHFA) take some initial public steps. Congressional action on the other hand remains muted, as resources and attention have been devoted to other legislative priorities.

OMB Proposal

The Office of Management and Budget (OMB) released a plan entitled “Reshaping American Government in the 21st Century.” The plan includes a number of proposals to reorganize or restructure government programs. Of note, OMB included a proposal to reform the federal role in mortgage finance. Key components of the proposal include ending the conservatorship of Fannie Mae and Freddie Mac, reducing their role in the housing market, and providing an explicit, limited Federal backstop that is on budget and apart from the Federal support for low- and moderate-income homebuyers. However, the proposal is light on details and we still believe more definitive Trump Administration views on housing finance reform could come later this year. To that end, we also have learned that this document is not necessarily representative of the Administration’s full views on housing finance reform, but some characteristics could be used as guide posts for future action.

FHFA Capital Framework

The FHFA issued a proposed rule for a new regulatory capital framework for Fannie Mae and Freddie Mac. The proposed rule is structured around both new risk-based capital requirements and updated minimum leverage requirements. The risk-based component will focus on credit, market and operational risks. When the GSEs were placed into conservatorship, FHFA suspended their capital requirements. The suspension will remain in effect, but FHFA noted that releasing the new capital requirements will “provide transparency to all stakeholders about FHFA’s supervisory view on this topic.” This proposed rule represents a major signal about the capital that will be required in a post-conservatorship world.

Farm Bill/CFTC Nominees

The House and Senate have both completed work on separate versions of farm bill reauthorization, but there are significant differences between the two bills, including the nutrition title and work requirements for recipients of assistance. While an official conference could begin in July, it will be difficult to reconcile the differences, so a short-term extension for the program, which expires at the end of the September, is definitely a distinct, and some would say likely, outcome. With work still to be done on the Farm Bill, that continues to leave CFTC Commissioner nominee Dan Berkovitz in limbo, but we still expect a nomination hearing for him

sometime this work period and a potential pairing of him with CFTC commissioner nominee Dawn Stump on the Senate Floor before or by the fall.

Flood Insurance

The National Flood Insurance Program (NFIP) expires at the end of the month on July 31st, so congressional action is necessary during this work period. Sens. Kennedy (R-LA) and Cassidy (R-LA) were able to attach a clean six-month extension to the Farm Bill. As mentioned above, it's unlikely that a Farm Bill conference will be completed before the end of July, so a NFIP extension will still need to be attached to another piece of "must-pass" legislation. House Republican Leadership, including Majority Whip Scalise (R-LA), have made clear that they will not allow the program to lapse and are considering several vehicles to extend the program until after hurricane season and the midterm elections. We also understand some Members would like to see an extension into March to allow a new HFSC Chairman to have time to work on a comprehensive package with reforms, but it remains unclear if that will occur.

Treasury Report on Nonbank Financial and Innovation

This month, Treasury is expected to release its fourth and final Executive Order report – this one focused on nonbank financial companies and FinTech/innovation. The report is expected to address traditional nonbank policy issues like credit reporting, mortgage servicing and auto lending. Additionally, it is expected to focus heavily on innovation by both banks and nonbank financial companies. Speaking at a SIFMA event in June, Treasury's Craig Philips noted the report will touch on the interplay between federal and state regulation, regulatory charters and sandboxes. As with past Treasury reports, we expect there to be recommendations for both regulators and Congress.

Political

While Democrats continue to recover from the primary defeat of their Caucus Chair, Rep. Joe Crowley (D-NY), they and Republicans can take a short breath, because July will be very quiet on the election front with only two runoffs and no primaries this month. One race to pay attention to, however, is a week from tomorrow when we'll see Rep. Martha Roby's (R-AL) runoff and whether her opposition to President Trump leads to her defeat (even though Trump has now endorsed her). While election activity is limited in July, next month will be very busy with primaries in 14 states and a special election to fill a House seat in Ohio. This will be followed by primaries in four northeastern states in early September as the primary season winds down heading into the November mid-term elections.

As for immediate and long-term impact of Crowley's loss, we do not see many remaining primaries where there could be a similar outcome, aside from a comparable situation facing Rep. Mike Capuano (D-MA) in his primary in early September. While the results of an election where less than 28,000 votes were cast have been overblown, Crowley's defeat does mean that there will be an open seat in House Democratic leadership. With progressives feeling their oats and New Democrat ranks still likely to swell after November, there will be a lot of moving parts and competition for his position as well as potential other spots among Dem leadership. But stay tuned...as none of this is likely to sort itself out until after November 6th (unless Crowley decides to leave early, à la former Majority Leader Cantor (R)).

On the House Republican leadership front, things remain relatively quiet. Assuming Republicans retain control of the House, we expect current Majority Leader Kevin McCarthy (R-CA) to be the front-runner and eventually the Speaker. In this scenario, it is likely the rest of the core leadership team moves up one slot with current Whip Scalise becoming Majority Leader and Chief Deputy Whip Patrick McHenry (R-NC) becoming the new Whip. However, a dynamic to keep an eye on is whether the Freedom Caucus can muster enough support to pick off a key leadership spot. If this materializes, the two front-runners appear to be current Freedom Caucus Chairman Mark Meadows (R-NC), who is personally close with President Trump, or former Freedom Caucus Chairman Jim Jordan (R-OH), who is currently facing allegations of turning a blind eye to sexual abuse when he was a college wrestling coach during the late 1980s and early 1990s. As of now, it looks like Speaker Paul Ryan (R-WI) will run through the finish line in November before stepping down. If things were to change, expect the leadership battle to intensify quickly and publicly.

Additional Details on Nominees Scheduled to be Considered by Senate Banking in July

The Senate Banking Committee is scheduled to consider at least four nominees in two hearings this month. Note that all four nominees have congressional experience.

July 19th Nomination Hearing

Export-Import Bank Chair

In June, President Trump nominated Kimberly Reed to be chair of the Ex-Im Bank. Reed previously was nominated by the President to be First Vice President of the Bank, and SBC favorably discharged her in December. Her nomination as chairman comes after Trump's previous nominee, former congressman Scott Garrett, withdrew when it became apparent a pathway to his confirmation wasn't achievable. To date, none of the President's Ex-Im nominees have been confirmed by the Senate. Reed has broad support from the business community, including endorsements from the National Association of Manufacturers and the Chamber.

CFPB (BCFB) Director

In June, Kathleen Kraninger was nominated by President Trump to lead the CFPB or BCFB. Kraninger currently serves as a Program Associate Director (PAD) for General Government at OMB under Director Mulvaney. Earlier in her career, she served as a senior policy and management staffer at the Departments of Homeland Security and Transportation. Her Senate experience includes serving as the lead staffer on the Senate Appropriations Committee where she oversaw the Subcommittee on Homeland Security. Until she or someone else is confirmed, Mulvaney will be able to continue leading the Bureau.

July 24th Nomination Hearing

SEC Commissioner

Elad Roisman was nominated by President Trump early last month to be a commissioner at the SEC. If confirmed, Roisman will take the seat of departing Republican Commissioner Michael Piwowar, who is leaving the agency this month. Roisman currently serves as Chief Counsel of SBC for Chairman Mike Crapo (R-ID) and previously served as Senior Counsel under former Chairman Richard Shelby (R-AL). Roisman is no stranger to the SEC as he served as one of former Commissioner Dan Gallagher's counsels focusing on trading and markets. Often SEC commissioners are paired together (one R and one D) when being considered by the Senate. Democratic Commissioner Kara Stein is serving on an expired term, but she has the ability to serve until the end of this year. As a result, it appears Roisman may need to move individually.

Ginnie Mae President

Michael Bright was nominated by President Trump in May to be President of Ginnie Mae. Bright currently serves as COO of Ginnie Mae, a non-confirmed position. Bright has both private sector and government experience related to housing finance policy. Most notably, he served as the lead staffer during housing finance reform discussions by the Senate in 2013 and developed a major housing finance reform policy paper while working at the Milken Institute. We expect Bright to play a key role on the Administration's housing finance reform team if reform discussions intensify.