BANKTHINK
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Try Thinking Outside Dodd-Frank

By Greg Wilson

Andrew Haldane, executive director of financial stability and a member of the Financial Policy Committee of the U.K.'s Bank of England, has done the U.S. a public service with his recent paper presented at the Federal Reserve Bank of Kansas City's 36th annual summit of central bankers in Jackson Hole, Wyo.

In "The Dog and the Frisbee," Haldane explores one of the great conundrums facing financial regulators and industry leaders today: is more, and increasingly complex, regulation better? Is this complexity adding any value or simply creating new risks? Or would a simpler, more "heuristic" approach produce better regulatory outcomes for end users and the economy?

You don't have to agree with all five of Haldane's major policy initiatives to appreciate his willingness to challenge the conventional wisdom of the current regulatory path of more and more rules of increasing complexity. My major takeaway from his provocative paper is that we ought to be having this same debate at the same high intellectual level here today. We are not, but this is understandable given where we are in our current election cycle: both the generalized Democratic mantra that the Dodd-Frank Act is inviolable and the Republican mantra to repeal Dodd-Frank are untenable.

It is never too late, however, to rethink basic problems and policy prescriptions, and then achieve better regulatory and economic outcomes, even if it means further legislation. 2013 offers us some hope to reflect and reassess where we are and where we are going.

My hypothesis, first developed in my 2011 book, is that ultimately the Dodd-Frank Act will be viewed as a net drag on our economy, and therefore a combination of both financial market and real-world economic forces, like slow growth and stubbornly high unemployment rates, will force us into a fundamental reassessment of the major financial regulatory issues and their economic implications for all end users.

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Haldane demonstrates that financial regulatory complexity can be not only cumbersome and costly to banks, and therefore end users, but counterproductive and suboptimal. In 1988, Basel I consisted of 30 pages, while Basel III grew to 616 pages by 2010, and this is before national implementing rules, which here could be 1,000 pages. Or take BHC reporting forms, which comprised 547 Excel columns in 1986 but had morphed to 2,271 by 2011, with more on the way for capital planning, stress testing, resolution planning and systemic risk analysis.

In arguing for better regulatory outcomes, this central banker stresses "less" can be "more." "More" is not always "better." Simple can be better. There is a real risk that complex rules – especially 400 new Dodd-Frank rules of varying complexity spanning potentially up to 30,000 pages – can create their own unique sets of risks and unintended outcomes, which can undermine or defeat their original purpose.

Three actions steps can begin to resolve this policy conundrum.

First, U.S. policymakers, regulators and industry leaders owe it to themselves to read Haldane's paper and understand his major theses. Even if you don't agree with his prescriptions, both his methodology and intellectual challenge to conventional regulatory wisdom are as refreshing as they are useful.

Second, all stakeholders – especially financial institutions and their end-user customers – need to rethink regulation through the lens that Haldane offers us. Are there greater risks in complex rules, which in turn become unmanageable? Have we fully explored the complete spectrum of optimal solutions to real problems, ranging from simple to complex, to achieve better regulatory outcomes for our economy? Can we agree on simpler, transparent rules and greater market discipline to foster greater economic growth, not thwart it?

Finally, we can take a lesson from the global gathering of central bankers at which this topic was first raised by a distinguished central banker. If there can be an annual event like Jackson Hole for monetary policy, why isn't there a comparable event to debate the equally critical importance of financial regulation for the real economy. Instead of just mostly central bankers, bank executives, board members, policymakers and end users in the real economy all should be there.

Andrew Haldane gave us both a lens and an excuse to act. Now, we need an urgent call to action for a debate worth having on a sustained basis. And 2013, after the U.S. elections, would seem the appropriate time to galvanize the best thinking on this critical issue. We need an annual conference of stakeholders, comparable to Jackson Hole, to focus exclusively on better financial regulatory outcomes for our economy as a national policy priority, a goal to which even Democrats and Republicans should be able to agree.

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