The Daily Dish

Tailoring and the Regional Banks

DOUGLAS HOLTZ-EAKIN | MAY 15, 2023

Remember the Dodd–Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank)? Enacted in 2010, Dodd-Frank was a costly regulatory overhaul of the U.S. banking system. So costly to comply with, in fact, that the same U.S. banking system that averaged 137 new banks from 1990 to 2007 averaged only five new banks from 2011 to 2022. (Indeed, there was only one new bank in 2012, 2013, and 2015, and zero in 2014 and 2016.) The costs of complying simply ended entry into the banking business.

The banks certainly noticed the burden. But there was impact on the industry as a whole. New entry is the best way to ensure competition for large, existing banks. It is the best way to generate competitive pressures for lower-cost services and new products. Consumer advocates noted the impact of Dodd-Frank and noted that perhaps Dodd-Frank had overdone some things. Congress came to the conclusion that it might be wise to fine tune Dodd-Frank.

In May 2018, it passed the Economic Growth, Regulatory Relief, and Consumer Protection Act (S.2155), a financial services bill aimed at "tailoring" the regulatory regime to the size of banks, in particular capital requirements for community and mid-tier banks. (For more on the "tiering" of banks and the capital standards that apply, see a primer here.) In particular, S.2155 raised the threshold for systemically important financial institutions from $50 billion to $250 billion while also empowering the Federal Reserve to articulate a new regulatory approach to supervising banks with assets exceeding $100 billion.

All was good.

Good, that is, until the cratering of Silvergate, Signature, and Silicon Valley Bank, and followed shortly thereafter by the demise of First Republic Bank. Immediately, the White House and Fed began pointing fingers at S.2155 and proposed to undo the "tailoring," even though there is exactly no evidence that those particular reforms contributed to these banks' problems. There is evidence, however, that the problem might be Fed supervision (and the fact that Silicon Valley Bank was the worst-run bank ever). The Government Accountability Office noted that the Fed can be slow to rectify problems in reports as far back as 2015 (before "tailoring").

The rush to judgment on tailoring is entirely unjustified and Congress should resist calls to unwind it as well. A better route would be a thorough oversight review of the Fed supervision.