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WASHINGTON POLICY STRATEGY

Potomac Perspective

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This note updates investors on three key developments regarding economic policy

While the House hearings on January 6th and gun control dominate the headlines, some in the Senate continue to seek compromise on a slimmed down Build Back Better bill.

A draft of a major cryptocurrency bill was released this week. Passing legislation in 2022 is unlikely, but an update on the policy and political issues related to the bill provides insight into the issues that need to be sorted out.

Finally, a key banking regulator is closer to Senate confirmation which, in turn, could set off the process to change bank merger guidelines. Some of the potential changes are discussed herein.

BBB 2.0

House hearings regarding January 6th and negotiations on gun legislation continue to dominate the headlines but behind the scenes, talks have continued in the Senate regarding a slimmed down Build Back Better bill (aka BBB 2.0). Although the bill has appeared to be on life support for several months, there are some signs of recovery. A possible revival raises two main questions – why and what would BBB 2.0 look like?

First, Democrats believe they need to pass something (anything) in order to energize their base ahead of the midterm elections. Related to that, premiums on American Cares Act (Obamacare) plans are set to rise in 2023 because subsidies passed in COVID-relief legislation are scheduled to expire. Notices on the premium increases would be sent out in October which could be devastating to Democrats just before the election. Also, since it seems almost certain that Democrats will lose the House in the upcoming election, they face the question of “If not now, when?”. BBB 2.0 might not include Progressives’ wish list, but it could include some important policy items at a critical time.

While there is no agreement yet on what a bill might look like, it seems likely that a bill would probably include a climate component (including subsidies for clean energy technologies and electric vehicles), extended subsidies for Obamacare policies, a prescription drug component, and a tax section. Some of the increased revenues would be designated for deficit reduction.

The tax plan, which has yet to be worked out, could look similar to the 2021 version of BBB and include.

- an alternative minimum tax for corporations;
- a global minimum tax regime;
- a one percent tax on stock buyback; and
- a surcharge for very high-income individuals

It is unclear whether there would be changes to trust and estate taxes or changes in rules for taxpayers with large retirement accounts, but that seems unlikely. It is also unclear whether there would be changes to limits on the deductibility of state and local taxes.

There seems to be some political will among Democrats to pass a bill and it is in their political interest to do so. However, the calendar is increasingly becoming the party's enemy. Much of June will be consumed with January 6th hearings and talks on gun legislation (also, the Supreme Court decision in the *Dobbs* case will suck up a lot of oxygen). Congress will be out of session for the week of July 4th and then on its summer break in August. Thus, Democrats do not have much time left to reach a deal, write the bill, and pass it through both the Senate and House. There is also the question of whether Progressives would let the perfect be the enemy of the good and sink a bill that fails to meet their purity test.

Odds are still against BBB 2.0 passing, but the bill is not dead. Investors should have the bill on their radar

CRYPTOCURRENCY BILL

Earlier this week, Senators Cynthia Lummis (R-WY) and Kirsten Gillibrand (D-NY) introduced legislation to clarify the regulation of cryptocurrencies. Here are some initial thoughts.

Many crypto advocates welcome the legislation as another step on the path towards acceptance. However, the bill is still some ways away from passing. Chances of significant legislative action (i.e. passing a congressional committee) are low and passing either the full House or Senate are even lower (close to zero). This is more likely a 2023-24 event and passing a bill in the next Congress is far from a sure thing. While crypto policy is important to stakeholders in the financial services and tech universes, it does not rank high on the overall congressional agenda.

Compared to earlier drafts of the bill, the new bill seems to give more power to the Commodities and Futures Trading Commission (CFTC) to regulate the spot market and seems to favor the CFTC over the Securities and Exchange Commission (SEC). This might have more to do with a congressional power play than policy preferences. Sen. Gillibrand is a member of the Senate Agriculture Committee but not the Banking Committee, so she sits on a committee that oversees the CFTC but not the SEC. This could have a big impact on how the bill is structured.

Not surprisingly, the bill would keep the Howey test which is used to determine if an asset qualifies as a security and is thus subject to securities law regulation and SEC oversight. Both senators have previously supported keeping the Howey test.

Earlier drafts would have created a new self-regulatory organization, but that aspect of the bill has been dropped. That's not entirely surprising since many Democrats would have been suspicious that a new SRO would be too beholden to the industry, while Republicans might be reluctant to support more bureaucracy (they want less).

There has been a lot of attention on the Lummis/Gillibrand bill and for good reason, since it is the most prominent bill regarding cryptocurrency. It is unlikely, however, to remain the only show in town. Senate Agriculture Committee Chair Debbie Stabenow (D-MI) and the committee's top Republican, Sen. John Boozman (R-AK) could write their own bill and, given their oversight of the CFTC, it would probably be like the Lummis/Gillibrand bill in giving preference to the CFTC over the SEC. Meanwhile, there's a bit of a vacuum at the Senate Banking Committee, which oversees the SEC as well as among the banking regulators, who will also have a say in whatever moves forward. Committee Chairman Sherrod Brown (D-OH) has not made crypto a priority and the committee's lead Republican, Sen. Pat Toomey (R-PA) is retiring at the end of the year. If the Senate flips, Sen. Tim Scott (R-SC) could be the committee's next chairman. He could write his own bill or defer to Lummis who is a Banking Committee member, but other committee members will want input too. If Brown remains chairman, he might push for a different approach than what the Lummis or Stabenow

bills would propose. Chairman Brown has been critical of crypto and could team up with Senator Elizabeth Warren (D-MA) to block legislation they think is too industry friendly.

Again, this is a topic that is likely to play out in Congress next year. In the meantime, President Biden's executive order on cryptocurrencies mandated federal agencies to draft at least a half-dozen reports on crypto-related topics including central bank digital currencies and stablecoins. These reports could impact the congressional debate as could any enforcement actions brought by the CFTC and SEC related to crypto.

BANK M&A

Earlier this week, the Senate Banking Committee approved the nomination of Michael Barr to become the Vice Chairman of Supervision of the Federal Reserve Board. Several committee Republicans voted for Professor Barr so he should be confirmed easily by the full Senate sometime in the coming weeks. Once confirmed, Barr could set in motion the process for the banking regulators to revise their bank merger review guidelines. The Federal Deposit Insurance Corporation has requested public feedback on its merger rules but has yet to propose revisions to its guidelines. The Fed could also request public feedback or simply issue a proposal for new rules which would be subject to public comments. The Fed, the FDIC, and the Comptroller of the Currency would probably act in concert in proposing rules changes, as is the historic norm.

In reviewing the merger guidelines, the regulators are likely to focus on "financial stability" which the Dodd Frank Act added to the list of factors regulators consider under the Bank Merger Act. Financial stability has yet to be clearly articulated in the bank merger review guidelines, so this seems like a prime opportunity for regulators to address the issue. Changes to rules related to safety and soundness, convenience and needs, and competition are also likely. In a related action, in December 2021, the Department of Justice requested public feedback regarding its bank merger review guidelines. DOJ reviews mergers for possible antitrust law violations. DOJ could issue a formal proposal simultaneously with the banking regulators.

Proposals could be issued in the fall and finalized in mid-2023. In the meantime, outstanding bank mergers are likely to be considered under the existing guidelines.

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