Welcome to the November issue of the Investments & Wealth Institute’s Washington Insights. This month’s column reviews the potential impact of the midterm elections on wealth managers, and by extension, a key part of the $100 trillion capital markets overseen by the Securities and Exchange Commission (SEC). Washington Insights also provides a brief wrap-up of other public policy topics of interest to wealth and institutional managers.

Advisors Keep Eye on How Midterms Will Impact Compliance

On November 8, millions of voters will go to the polls to select 435 members of the House of Representatives and 35 in the Senate. The latest trendlines are starting to heavily favor Republicans taking the House, with Senate control still a toss-up.

Like the daily stock market news, the media often is fixated on short-term events—especially the horse race aspect of who is winning and which party may capture (or retain) control of Congress.

Still, it wouldn’t be an election if the pundits weren’t spinning forecasts. Except that—spoiler alert—financial advisors are less likely to be impacted by what happens on Capitol Hill than they are by the SEC and the Department of Labor (DOL). Not to be overlooked are the federal courts, which likely will have more say-so over regulatory actions than Congress during the next two years.

Below are some scenarios of what financial advisors can expect after November 8.

A divided Congress. Whether Republicans take the House or Senate, expect gridlock. Keep in mind that although Democrats technically control both chambers, the Senate’s filibuster rule effectively blocks passage of non-fiscal legislation without 60 votes. The Senate is currently divided 50–50, leaving Democrats in marginal control via Vice President Kamala Harris’ ability to break tie votes as Senate President. Democrats currently need at least nine Republican votes (59 total) to end a filibuster, also known as cloture.
At best, Democrats can hope for only a slightly enlarged majority of 52–48 in the Senate. If this occurs, they could employ the so-called “nuclear option” by eliminating the filibuster rule and allowing a simple majority vote on legislation. Currently two Democratic senators, Kyrsten Sinema (D-AZ) and Joe Manchin (D-WV), oppose eliminating the filibuster.

In either event, if Republicans take control of the House or Senate, it is unlikely Democrats will be able to pass non-fiscal legislation, including any legislation that affects financial advisors. However, there is currently strong bipartisan support for a retirement bill dubbed “SECURE Act 2.0.” If it doesn’t pass this year, it’s likely to be reintroduced in the next Congress.

Expect legislative “noise” to continue in a divided Congress, with so-called “messaging” bills introduced, but with little or no chance of passing, and agency oversight hearings.

Meanwhile, financial regulators like the SEC and DOL will continue, uninterrupted, to promulgate new regulations and defend against potential industry lawsuits by “bullet-proofing” new regulations as much as possible. For example, bullet-proofing could include agencies adding more time for public comments or reopening them for comment to avoid claims in court alleging that a rulemaking was rushed.

**GOP controls Congress.** In the event Republicans control both chambers after November 8, a GOP-controlled Senate would need to employ the nuclear option to pass non-fiscal bills with a simple majority vote. This exercise would largely be for messaging purposes because partisan legislation would likely be vetoed by President Joe Biden.

Republicans also could take advantage of the Congressional Review Act (CRA) in order to overturn agency rules they dislike. The CRA allows each chamber to take a streamlined approach to pass a resolution that overturns a specific agency rule by skirting lengthy committee reviews and moving the bill quickly to the floor. A simple majority vote would be required for passage in either chamber—nuclear option or not.

In 2016 the Republican-controlled Congress used the CRA in an effort to overturn the DOL’s fiduciary rule. After both chambers passed the resolution then-President Barack Obama vetoed it. The House failed to muster the necessary two-thirds vote to override the veto. Had it passed the House, the Senate also would have been required to override the veto with a two-thirds majority vote.

Efforts to override presidential vetoes typically fail. Since George Washington issued the first presidential veto in 1792, less than 5 percent of the 2,500-plus presidential vetoes (including pocket vetoes) have been overridden by Congress.

**Democrats retain control of Congress.** As of late October, most polls indicate it is highly unlikely Democrats will retain control of the House. However, if they keep control of the House and add two more Democrats to the Senate, they may be tempted to employ the nuclear option because of the opposition from Senators Sinema and Manchin. Conceivably this procedural change could allow Democrats to advance a broad legislative agenda, including potential legislation with tougher market conduct standards for financial advisors.
**Litigation risk.** Although prolonged legislative gridlock means Congress poses little threat to new rulemakings by the SEC or DOL—outside of tough rhetoric in oversight hearings, bill introductions for messaging purposes, and efforts to add riders to appropriation bills defunding specific regulatory activity—the courts are more likely to block agency rulemakings.

As many advisors are aware, this occurred in 2018 when a panel of the Fifth Circuit Court of Appeals vacated the Obama-era fiduciary rule after Republicans’ efforts to use the CRA failed. Industry opponents already have filed lawsuits challenging current DOL rulemakings or guidance and more litigation can be expected. In particular, the SEC’s environmental, social, and governance (ESG) disclosure rule for public companies will be a likely target, as well as any effort by the DOL to revive parts of the old Obama-era fiduciary rule that would expand the definition of an investment fiduciary to industry brokers.

**Summary.** The trade press will closely cover the results of the midterms; however, wealth managers and others would be well-advised to avoid the political noise and focus on what the regulatory agencies are doing. It also would be helpful to keep tabs on legal challenges to SEC and DOL rules, which have increased in recent years, although some could take years to resolve.

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**THE WRAP-UP**

**SEC Regulation**

**SEC proposes formal advisor oversight of outsourcing to third-party service providers.** A [new rule proposal](#) released October 26 for public comment would require registered investment advisers (RIAs) to conduct due diligence, document, and periodically monitor outside services providers’ performance, including investment guidelines, portfolio managers, digital advice, model indexes, trading services, and software.

“Though investment advisors have used third-party service providers for decades, their increasing use has led [SEC] staff to make several recommendations to ensure advisors that use them continue to meet their obligations to the investing public,” SEC Chair Gary Gensler said in a statement accompanying the proposal.

The SEC also [adopted a rule requiring mutual funds](#) to provide investors with more “visually engaging annual and semi-annual reports,” including electronic versions that are “more user-friendly and interactive.”

**Fast pace of SEC rulemakings draws GOP ire.** As the SEC continues an aggressive rulemaking program, a half-dozen Republican senators are protesting, writing a letter to SEC Chair Gary Gensler raising concerns about the “operational integrity” of the agency following a recent Inspector General’s report expressing concerns with SEC staff plowing through too many regulations.

One of the signatories of the letter, Senator Thom Tillis (R-NC), asked Gensler how he is addressing these challenges, and warning that “any efforts to ram through hurried rulemaking without proper analysis, deliberation or consideration of downstream negative impacts is nothing short of regulatory malpractice.”
Congress

**Major retirement legislative action likely in lame-duck session of Congress.** Bipartisan retirement legislation (dubbed SECURE Act 2.0) is on hold as members of Congress campaign for reelection. However, Capitol Hill observers expect Congress to act on the legislation during the lame-duck session that begins November 14 and ends in mid-December. The Senate still has to take floor action on two companion bills before a reconciliation bill can pass both chambers and go to the White House for a signature.

Combined, some 97 provisions in the Senate and House legislation would amend federal retirement law to boost workers’ and retirees’ ability to save for retirement by:

- Expanding plan coverage for part-time workers
- Increasing tax credits as an incentive for small businesses to establish retirement plans
- Allowing employers to set up automated employee payroll deductions for emergency savings accounts

The legislation also would allow companies to make matching contributions to 401(k)-type plans while employees’ match would go to student loan repayments.

ESG

**DOL’s ESG rule nears final release.** The DOL rule supporting the use of ESG investment products in retirement plan lineups has been submitted to the White House’s regulatory office for review, signaling the final regulation may be released within a few weeks.

The [proposed version](#), released by the DOL employee benefits agency in October 2021 for public comment, would in effect encourage private sector plan sponsors to consider ESG factors when making decisions about plan investments.

**DOL Enforcement**

Wells Fargo and a plan trustee agreed to a settlement with the DOL on September 12 for allegedly requiring plan participants to overpay for company stock.

According to [a DOL news release](#), Wells Fargo and GreatBanc Trust Company caused the company’s 401(k) plan to pay between $1,033 and $1,090 per share for Wells Fargo preferred stock when the stock converted from common stock under a set value of $1,000 per share, resulting in alleged overpayments of $131.8 million.

The DOL said the settlement funds would be allocated to current and former participants and that GreatBanc would not act as a fiduciary to public companies in that same capacity.

In other enforcement action, the [DOL settled with plan fiduciaries](#) of InterArch Inc., on September 23 for allegedly investing plan assets in two companies in which the company owners had significant investments.
InterArch company owner Shirley S. Hill and her spouse Vernon W. Hill II, agreed to pay $1.8 million to settle with the DOL in addition to $1.1 million in a private class action filed by a former employee in 2020. According to a news report, Ms. Hill invested most of the plan’s assets in a bank owned by her husband, costing the bank more than $17 million after the bank’s shares declined to less than 96 percent of their peak value. Additionally, 13 percent of plan assets were invested in the stock of another bank in which Mr. Hill was a senior executive.

ABOUT WASHINGTON INSIGHTS

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If you have questions after reading this update, please contact the Institute’s general counsel, Robert (Rob) Frankel at rfrankel@i-w.org.

ENDNOTE