From:	[redacted]
To:	Public Information; Comments
Subject:	[EXTERNAL MESSAGE] Request for Information on a Framework for Analyzing the Effects of FDIC Regulatory Actions(FDIC RIN 3064-ZA13)
Date:	Thursday, February 20, 2020 5:22:26 PM

Robert E. Feldman, Executive Secretary
ATTN: Comments
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RE: Request for Information on a Framework for Analyzing the Effects of FDIC Regulatory Actions(FDIC RIN 3064-ZA13)

Dear Executive Secretary:

In this RFI the Corporation seeks input on improving its internal economic analysis of rulemaking actions. There is no dispute concerning the importance of thoughtful analysis in the process of designing rules. Both legally and as a matter of common sense, the Corporation and other regulatory agencies should consider the effects of potential rules and seek to accomplish statutory goals in an effective and efficient manner. Like all rulemaking agencies, the Corporation is subject to the Administrative Procedures Act, which requires it to state the basis and purpose of any legislative rule. Such justifications are subject to judicial review based on an “arbitrary and capricious” standard. These restrictions, as well as the Corporation’s own commitment to reasoned rulemaking, support a measured approach to rulemaking.

Recommendations in relation to this RFI:

1) Any instructions given to internal analysts at the FDIC regarding the analysis of costs and benefits should avoid locking the agency into a false and oversimplified framework of “cost-benefit analysis” that rests regulatory decisions simply on comparing estimates of quantitative costs and benefits.

2) There are a number of positive elements in this RFI would help to avoid such an outcome. These include the requirement to measure regulatory actions against a variet

of key policy goals, weighing of non-quantifiable benefits, and attention to distributional effects of policy. These elements should be maintained in any final guidance to analysts.

3) Analysis of costs and benefits should not incorporate a pre-statute baseline, but instead isolate the effect of the regulation itself.

4) A balancing of costs and benefits should be conducted for deregulatory steps, not simply for new or stronger regulations.

The FDIC Should Avoid the False Framework of “Cost-Benefit Analysis”
This RFI states that the Corporation is now seeking to incorporate more

explicit consideration of costs and benefits into its rulemaking. Properly performed, this can be beneficial, but it also carries significant dangers. The full costs and benefits of a new rulemaking are generally highly uncertain and usually cannot be definitively determined or quantified in advance. When an agency locks itself into a framework that demands an explicit net weighting of costs and benefits before taking any regulatory action, its freedom to take action to protect the public is restricted. Furthermore, regulated entities are highly motivated to take issue with agency estimates of the costs of regulatory action, even when such estimates are well grounded. They can take legal action to exploit the inherent uncertainties of cost-benefit assessment and sue to stop rulemaking. Such a lawsuit can effectively move the decision making point regarding the rule away from agency experts and into a trial court where the judge is far less experienced concerning bank regulatory policy than the agency.

The difficulty and uncertainty of quantifying costs and benefits of financial regulatory rules is well documented and is effectively summarized in a recent Yale Law Journal article by Harvard Law professor John Coates. After an extensive review of the track record of quantified costbenefit analysis in financial regulation, Coates concludes that such quantified analysis amounts to what is effectively "guesstimation", or "judgement in disguise." Coates also concludes that "Empowering courts to review even conceptual CBA/FR policy analysis is likely to be a bad idea." Note that Coates' conclusions are in part based on an extensive analysis of the analytic uncertainties involved in estimating the estimated costs and benefits of increased capital requirements, an issue highly relevant to FDIC rulemaking.

For these reasons, the Corporation should not tie itself to any analytic procedure which requires that all costs or all benefits of a regulatory action be summed up as a single quantitative figure. Nor should it require all costs and benefits to be netted out in a single quantitative "net benefits" estimate which is taken to be determinative of whether a regulation should proceed.

There are a Number of Positive Elements of the RFI

The discussion of cost and benefits of regulatory action in the RFI is thoughtful and contains a number of positive elements that should help to avoid locking the agency into the false and destructive model of "cost-benefit analysis". In general, the RFI does not propose that the costs or benefits of a regulatory action can be reduced to a single quantitative figure and that a costbenefit analysis can be conducted simply by comparing such quantitative estimates. Instead, it is appropriately sensitive to issues of non-quantitative benefits, statutory goals, and distributional impacts. This sensitivity should be maintained in any final guidance based on the RFI.

Some of the specific strengths of the RFI that should be maintained include:

Attention to a variety of critical policy goals – Table 1 of the RFI lays out a number of important policy goals which the RFI states must be given significant weight in any cost-benefit analysis. These include protecting the Deposit Insurance Fund, improving the treatment of financially underserved communities, distributional effects, and effects on economic performance and the availability of credit. This is critical as the Corporation must avoid any cost-benefit procedure that would

support actions which harm critical FDIC priorities, such as protecting the Deposit Insurance Fund or providing fair treatment to financially underserved communities, based on general arguments about economic performance. Explicitly requiring these specific priorities to be weighed and considered in all analyses is a way of avoiding such an outcome.

Analysis of true social costs – The RFI correctly distinguishes between broad economic welfare and gains to particular stakeholders. For example, a reduction in bank compliance costs is not in itself a gain to economic welfare more broadly. It is simply a gain to banks that is counterbalanced by a loss to others who provide compliance services, and if it results in further costs due to lack of compliance with regulations it may represent a net loss to society. Costbenefit analyses should not focus on partial tabulations of costs to regulated industry that are counterbalanced by benefits to other parties. In many cases a transfer from one entity to another may be very desirable for distributional and equity reasons (e.g. a transfer from banks to consumers through the prevention of fraudulent or misleading financial practices), but analysts should be clear as to when a cost is a true social cost as opposed to a transfer.

Cost-Benefit Analysis Should Not Incorporate a Pre-Statute Baseline
The RFI requests comment on whether the Corporation should use a pre-statute baseline in evaluating costs and benefits of regulatory action. It is not felt this is appropriate, as the FDIC does not and should not control whether a statute is passed or determine the merits of any particular statute. It is not the role of the agency to give its views on the costs and benefits of Congressional action, but simply to determine the best and most effective way to implement statutory directives.

Instead, the FDIC should use a baseline corresponding to the world before the regulation is passed, and compare alternative means of implementing the statute.

The FDIC Should Properly Apply Cost-Benefit Considerations to Deregulatory Actions

It has been noticed that in recent rulemakings aimed at reducing the scope of post-crisis bank regulations, the Corporation has not appropriately considered the social costs of reducing regulatory oversight. This has occurred even in cases where the benefits of strong regulation were explicitly discussed in the prior rule which is now being rolled back. To take just one recent example, the proposal eliminating swap margin for inter-affiliate swaps at large banks did not appear to consider the costs of losing the prudential protections that had served as the justification for the rule in the first place.
Another example of a deregulatory rule where the costs of losing regulatory protections were not fully considered is the recently finalized modifications to the Volcker Rule, which sharply restricted the applicability of the rule to bank assets without providing any analysis of the costs to financial stability this could create. Many other examples could be given.

Therefore the Corporation should fully incorporate consideration of the benefits of strong regulatory oversight of publicly insured banking organizations into future rules, including those that are deregulatory.

Thank you for the opportunity to comment on this Proposal.

Yours sincerely,
Robert E. Rutkowski

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