CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

February 11, 2016

H.R. 1941
Financial Institutions Examination Fairness and Reform Act

As ordered reported by the House Committee on Financial Services on July 29, 2015

SUMMARY

H.R. 1941 would establish the Office of Independent Examination Review within the Federal Financial Institutions Examination Council (FFIEC). The council would investigate complaints from financial institutions about examinations, conduct regular reviews of the quality of examinations, and adjudicate appeals of determinations made as part of an examination. The bill also would prohibit financial regulators from classifying certain commercial loans as non-performing and from requiring certain banks to raise more capital to cover the potential losses from those loans.

CBO estimates that enacting H.R. 1941 would increase net direct spending by $192 million and reduce revenues by $40 million over the 2016-2026 period; therefore, pay-as-you-go procedures apply. In total, CBO estimates that enacting H.R. 1941 would increase budget deficits by $232 million over the 2016-2026 period. Implementing H.R. 1941 would not affect spending subject to appropriation.

CBO estimates that enacting the legislation would not increase net direct spending or on-budget deficits by more than $5 billion in any of the four consecutive 10-year periods beginning in 2027.

H.R. 1941 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA).

H.R. 1941 could increase the cost of an existing mandate on private entities required to pay fees. Based on information from the affected agencies, CBO estimates that the incremental cost of the mandate would fall well below the annual threshold for private-sector mandates established in UMRA ($154 million in 2016, adjusted annually for inflation).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary effects of H.R. 1941 are shown in the following table. The costs of this legislation fall within budget function 370 (commerce and housing credit).

	By Fiscal Year, in Millions of Dollars												
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2016-2021	2016-2026
CHANGES IN DIRECT SPENDING													
Office Of Independent Examination Review													
Estimated Budget Authority	0	4	10	11	9	9	9	10	10	10	10	43	92
Estimated Outlays	0	4	10	11	9	9	9	10	10	10	10	43	92
Other Administrative Costs													
Estimated Budget Authority	0	1	1	1	1	1	1	1	1	1	1	5	10
Estimated Outlays	0	1	1	1	1	1	1	1	1	1	1	5	10
Prohibitions on Regulatory Actions													
Estimated Budget Authority	0	2	5	8	9	10	10	11	11	12	12	34	90
Estimated Outlays	0	2	5	8	9	10	10	11	11	12	12	34	90
Total Changes													
Estimated Budget Authority	0	7	16	20	19	20	20	22	22	23	23	82	192
Estimated Outlays	0	7	16	20	19	20	20	22	22	23	23	82	192
CHANGES IN REVENUES[a]													
Estimated Revenues	0	-1	-3	-4	-4	-4	-4	-5	-5	-5	-5	-16	-40
NET INCREASE IN DEFICITS													
Increase in Deficits	0	8	19	24	23	24	24	27	27	28	28	98	232

a. Negative numbers denote decreases in revenues.

BASIS OF ESTIMATE

For this estimate, CBO assumes that the bill will be enacted near the end of fiscal year 2016 and that spending will follow historical patterns for similar regulatory activities.

H.R. 1941 would establish a new office, the Office of Independent Examination Review, at FFIEC to investigate complaints from financial institutions related to examinations, to review examination standards to ensure consistency across the agencies, to adjudicate appeals of determinations made as part of an examination, and to conduct a continuing program of quality control and assurance.

FFIEC was established to promote uniformity in supervision of financial institutions; generally, its operating costs are borne by four financial regulatory agencies—the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), and the Federal Reserve System. Under H.R. 1941, a portion of the costs of the office also would be covered by the Consumer Financial Protection Bureau (CFPB).

Three of those regulators—the OCC, the FDIC, and the NCUA—collect fees to offset operating costs. Because of lags between the time costs are incurred by some of the financial regulators and when additional fees would be imposed, not all additional costs resulting from the bill could be recovered within the next 10 years. Costs borne by the CFPB are recorded in the budget as direct spending because the agency has permanent authority to spend amounts transferred from the Federal Reserve System. Finally, costs incurred by the Federal Reserve System to implement the bill would reduce remittances to the Treasury (which are recorded as revenues) and would therefore affect the federal budget by reducing revenues.

Currently, the FFIEC is supported by 15 staff who are employed by the regulatory agencies but assigned to the council.

Direct Spending

Office of Independent Examination Review. CBO expects that establishing the Office of Independent Examination Review would require a significant increase in the council's staff. Based on information from FFIEC, CBO estimates that an additional 50 staff positions would be needed to meet the bill's requirements to investigate and resolve appeals and to review examination procedures. CBO expects that it would take several years to reach that new staffing level and that the costs would be spread evenly among the five regulatory agencies.

Based on information from the affected agencies, CBO estimates that establishing the office would cost $202 million over the 2016-2026 period to supply the FFIEC with additional staff and to cover other operating expenses. That amount reflects some savings to the regulators because a portion of the complaints they receive under current law would be handled by FFIEC under the bill. We expect that 80 percent of the net cost, or $162 million, would be spread equally among four financial regulators—the FDIC, OCC, NCUA and CFPB—increasing gross direct spending by that amount.

As noted above, three of those regulators collect fees to offset operating costs, but because there is a lag in the timing of collections, not all costs would be offset over the 2016-2026 period. CBO estimates that over the ten-year period additional fees collected from financial institutions would total about $70 million. On net, CBO estimates that enacting H.R. 1941 would increase direct spending by $92 million over the 2016-2026 period.

The remaining 20 percent would be charged to the Federal Reserve System; those effects are discussed below under the heading "Revenues."

Other Administrative Costs. The bill also would establish deadlines for the federal banking regulators to complete examination reports. Based on information from those agencies, CBO estimates that they would need to hire additional staff to meet the deadlines established in the bill, at an estimated net cost of about $10 million over the 2016-2026 period.

Prohibitions on Regulatory Action. The bill would prohibit financial regulators from classifying certain commercial loans as nonperforming and from requiring certain banks to raise more capital to cover the potential losses that could stem from those loans. CBO expects that those prohibitions would primarily affect loans for commercial real estate. For institutions with limited or moderate exposure to such loans that otherwise have diversified loan portfolios, such limitations would be unlikely to result in a bank failure where the federal government incurs any costs. However, some banks with holdings that are primarily concentrated in the commercial real estate sector could experience a reduction in their capital reserves, which would lead to a higher probability of a bank failure and would increase the probability of additional federal costs to resolve the liabilities of failed institutions.

Based on a review of information contained in bank reports and on criteria established by federal financial regulations, CBO estimates about 450 federally insured financial institutions have portfolios that are concentrated in commercial real estate. The assets of those banks account for about 40 percent of all bank assets. Any significant downturn in the commercial real estate market could cause instability and losses for the portfolios of those institutions. CBO's baseline for deposit insurance programs includes the probability that some banks will fail in any given year. Although the likelihood of deterioration in the market for commercial real estate is uncertain, the prohibitions in H.R. 1941 on regulation of commercial real estate loans would probably lead to a small increase in the number of banks that fail and require resolution through the FDIC's Deposit Insurance Fund (DIF).

Based on the historical components of bank failures, CBO estimates that there would be about a 10 percent increase in failures for banks with portfolios that hold significant amounts of commercial real estate. Using CBO's baseline projections of losses from the DIF, we estimate that a 10 percent increase in the rate of failure for those banks would cost about $90 million over the 2016-2026 period.

Revenues

The Federal Reserve System remits its profits to the Treasury, and those payments are recorded as revenues in the federal budget. Increasing the costs of operating the Federal Reserve System reduces federal revenues. CBO estimates that the portion of the costs to establish the Office of Independent Examination Review that would be allocated to the Federal Reserve would average about $4 million per year; over the 2016-2026 period, revenues would decline by $40 million.

PAY-AS-YOU-GO CONSIDERATIONS

The Statutory Pay-As-You-Go Act of 2010 establishes budget-reporting and enforcement procedures for legislation affecting direct spending or revenues. The net changes in outlays and revenues that are subject to those pay-as-you-go procedures are shown in the following table.

CBO Estimate of Pay-As-You-Go Effects for H.R. 1941, as ordered reported by the House Committee on Financial Services on July 29, 2015

	By Fiscal Year, in Millions of Dollars												
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2016-2021	2016-2026
NET INCREASE IN THE DEFICIT													
Statutory Pay-As-You-Go Impact	0	8	19	24	23	24	24	27	27	28	28	98	232
Memorandum													
Changes in Outlays	0	7	16	20	19	20	20	22	22	23	23	82	192
Changes in Revenues[a]	0	-1	-3	-4	-4	-4	-4	-5	-5	-5	-5	-16	-40

a. Negative numbers denote decreases in revenues.

INCREASE IN LONG-TERM DIRECT SPENDING

CBO estimates that enacting the legislation would not increase net direct spending or on-budget deficits by more than $5 billion in any of the four consecutive 10-year periods beginning in 2027.

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

H.R. 1941 contains no intergovernmental mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

If financial regulators increase fees to offset some of the costs of implementing the new activities of the FFIEC, the bill would increase the cost of an existing mandate on private entities required to pay those fees. Based on information from the affected agencies, CBO estimates that the incremental cost of the mandate would amount to no more than about $25 million over the 2016-2021 period and would fall well below the annual threshold for private-sector mandates established in UMRA ($154 million in 2016, adjusted annually for inflation).

PREVIOUS CBO COST ESTIMATE

On July 29, 2015, CBO transmitted a cost estimate for S. 1484, the Financial Regulatory Improvement Act of 2015, as ordered reported by the Senate Committee on Banking, Housing, and Urban Affairs on June 2, 2015. Section 104 of S. 1484 would establish the Office of Independent Examination Review. H.R. 1941 contains a provision that would direct the office to adjudicate appeals of determinations made as part of an examination; that provision is not included in Section 104 of S. 1484. CBO's estimate of the cost to establish the office in each bill reflects that difference.

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