CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

July 29, 2015

S. 1484
Financial Regulatory Improvement Act of 2015

As reported by the Senate Committee on Banking, Housing, and Urban Affairs on June 2, 2015

SUMMARY

S. 1484 would amend federal laws that regulate certain financial institutions and securities markets. Specifically, the legislation would change the process and procedures that federal regulators follow for determining which firms should be designated as systemically important financial institutions (SIFIs), and it would alter a number of provisions of current law that provide protection to consumers of financial products.

CBO estimates that enacting the legislation would increase net direct spending by $284 million and reduce revenues by $93 million over the next 10 years, leading to a net increase in the deficit of $377 million over the 2016-2025 period. Some of that cost would be recovered from financial institutions in years after 2025. Pay-as-you-go procedures apply because enacting the legislation would affect direct spending and revenues.

CBO estimates that enacting the legislation would not increase net direct spending or on-budget deficits by at least $5 billion in at least one of the four consecutive 10-year periods beginning in 2026.

S. 1484 would amend several provisions of law enforced by the Securities and Exchange Commission (SEC). CBO estimates the implementing those changes would cost about $2 million over the 2016-2020 period. Under current law, the SEC is authorized to collect fees sufficient to offset its annual appropriation; therefore, we estimate the net cost to the SEC would be negligible.

S. 1484 contains intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA) because it would limit the application of some state laws. The bill would preempt state laws that govern civil liability, nullification of specific types of contracts, and licensure of mortgage originators. Although the bill would limit the application of state laws, it would impose no duty on states that would result in additional spending or a loss of revenues.

S. 1484 contains private-sector mandates as defined in UMRA on individuals and businesses in the financial services industry. The bill would eliminate exiting rights of action, require additional reporting for some insurers, apply standards for processing funds in two American territories, and increase certain regulatory fees. Because the incremental changes required to comply with the mandates would be small relative to existing practices, CBO estimates that the aggregate cost of the mandates in the bill would probably fall below the annual threshold established in UMRA for private-sector mandates ($154 million in 2015, adjusted annually for inflation).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary effect of S. 1484 is shown in the following table. The costs of this legislation fall within budget function 370 (advancement of commerce).

BASIS OF ESTIMATE

The major costs of the legislation would stem from increased administrative costs and changes in the regulatory process that would be required of financial regulators, including the following:

- Consumer Financial Protection Bureau (CFPB),
- Federal Deposit Insurance Corporation (FDIC),
- Federal Financial Institutions Examination Council (FFIEC),
- Federal Reserve System,
- Federal Housing Finance Agency (FHFA),
- Financial Stability Oversight Council (FSOC),
- National Credit Union Administration (NCUA), and
- Office of the Comptroller of the Currency (OCC).

	By Fiscal Year, in Millions of Dollars											
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2016-2020	2016-2025
NET INCREASE IN THE DEFICIT FROM CHANGES IN DIRECT SPENDING AND REVENUES												
General Administrative Costs	14	20	21	21	21	22	22	22	24	24	98	213
Administrative Costs to Financial Regulators to Review and Designate Financial Institutions [a]	2	5	9	9	9	9	10	10	11	11	35	84
Additional Costs to the FDIC to Resolve Failed Financial Institutions [b]	0	3	9	9	10	11	10	10	9	9	31	80
Total Increase in the Deficit[c]	16	29	40	39	40	42	42	43	43	43	164	377
Memorandum: Components of the Net Increase in the Deficit												
CHANGES IN DIRECT SPENDING												
Total Changes in Direct Spending												
Estimated Budget Authority	9	21	31	29	30	32	33	33	34	35	121	288
Estimated Outlays	8	20	31	29	30	32	32	34	34	34	118	284
CHANGES IN REVENUES [d]												
Total Changes in Revenues	-8	-10	-9	-9	-9	-10	-9	-9	-9	-9	-46	-93

Source: Congressional Budget Office.

Notes: Amounts may not sum to totals because of rounding; FDIC = Federal Deposit Insurance Corporation.

a. Administrative costs to financial regulators include costs incurred by the Federal Deposit Insurance Corporation, the Financial Stability Oversight Council, the Federal Financial Institution Examination Council, the Office of Comptroller of the Currency, the National Credit Union Administration, and the Federal Reserve System. Costs to the Federal Reserve System reduce remittances to the Treasury (which are recorded in the budget as revenues). Administrative costs to some of the other financial regulators are offset, over time, by assessments levied on financial industries.

b. Additional costs to resolve financial institutions under S. 1484 would be offset, over time, by increased assessments on financial industries.

c. CBO estimates that about one-third of the net increase in the deficit over the 2016-2025 period would be offset by fees and assessments collected after 2025.

d. Negative changes in revenues indicate a loss of revenue.

Some financial regulators can eventually recover additional costs through assessments on the industry; the Federal Reserve System and the CFPB cannot. Because of lags between the time costs are incurred by some of the financial regulators and when additional assessments would be imposed, not all additional costs can be recovered within the next 10 years.

CBO also estimates that provisions in the bill that would change the standards and procedures for designating systemically important financial institutions would slightly increase the probability of losses to the FDIC from resolving possible future defaults by certain bank and nonbank financial institutions. The FDIC can eventually recover its costs for resolving those defaults from assessments on the financial industry; however, CBO estimates that such recoveries would occur over many years, resulting in a small additional net increase in the deficit over the 2016-2025 period. Finally, S. 1484 would modify the operations of Fannie Mae and Freddie Mac and change the definition of a qualified mortgage. CBO estimates that enacting those provisions would have no significant net cost.

General Administrative Costs

S. 1484 would increase administrative costs of financial regulators by:

- Making changes in several statutes that protect consumers of financial products and services;

- Establishing a new office, the Office of Independent Examination Review, to investigate complaints from financial institutions related to examinations, review examination standards to ensure consistency across all regulators, and conduct a continuing program of quality control; and

- Making a number of changes affecting the Federal Reserve System, including setting new requirements for the Federal Reserve Board’s monetary policy report, allowing the hiring of support staff for members of the Board, and establishing a commission to study the structure of the Federal Reserve System.

Based on information from the financial regulators and incorporating a partial recovery of administrative costs, CBO estimates that those provisions of S. 1484 would increase budget deficits by $213 million over the 2016-2025 period. About half of that amount would be spent to establish the Office of Independent Examination Review.

Administrative Costs to Financial Regulators to Review and Designate Systemically Important Financial Institutions

Enacting S. 1484 would increase the workload of FSOC and other financial regulators that are charged with designating depository institutions and other financial firms as SIFIs. Under current law, all banks with consolidated assets over $50 billion are automatically designated as SIFIs, while nonbank financial firms that meet certain criteria are designated by FSOC on a case-by-case basis. S. 1484 would repeal the automatic designation for banks that have less than $500 billion in assets and establish a new process for FSOC to designate those firms on a case-by-case basis. The bill also would revise the designation process for nonbank financial firms to require FSOC to provide additional information and opportunities for hearings, appeals, and approvals by certain other regulatory entities.

Based on information from the financial regulators and incorporating a partial recovery of administrative costs, CBO estimates that enacting this provision of the legislation would increase budget deficits by $84 million over the 2016-2025 period.

Additional Costs to the FDIC to Resolve Failed Financial Institutions

Under current law, firms that are designated as SIFIs are subject to enhanced prudential regulation by financial regulators. Among other things, those measures require SIFIs to undergo special stress tests, develop resolution plans, and maintain certain levels of liquidity and loss absorbing capacity. Based on information from national credit rating agencies and academic, industry, and regulatory experts, CBO concludes that the added capital and transparency that results from those enhanced prudential regulations improve the safety and soundness of the affected firms.[1] On balance, CBO estimates that such regulation lowers the FDIC's cost of resolving insolvent firms (whether through the Orderly Liquidation Fund or the Deposit Insurance Fund) by 2 percent to 3 percent, primarily because those measures should result in shareholders and other creditors absorbing a larger share of any losses in the event of insolvency.

CBO expects that the revised standards and procedures in S. 1484 could delay the designation of some bank and nonbank firms as SIFIs and may reduce the number of firms so designated. Under current law, CBO estimates that enhanced prudential regulation of SIFIs will reduce the net losses incurred by the FDIC by about $500 million over the next 10 years. Based on recent trends in the designation process, CBO estimates that the amount of assets subject to enhanced regulation would be about 10 percent to 20 percent smaller under this bill, resulting in an estimated increase in the deficit from losses of $80 million over the 2016-2025 period. Changes in the designation of nonbank firms and banks with assets between $50 billion and $250 billion account for most of that estimated cost. Most of those costs would be offset after 2025 by income to the FDIC from fees paid by insured depository institutions and large financial firms.

Market Access for Mortgage Finance

Title VII would direct Fannie Mae and Freddie Mac to equip their joint securitization platform—which they are developing to merge their securitization functions—to accommodate private issuers of mortgage-backed securities, develop standards for private issuers to access those functions, and transfer ownership of the corporate structure

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1. See, for example, Standard and Poors, "Dodd-Frank Five Years Later: The Good, the Questionable, and the Unintended," July 1, 2015.

associated with those securitization functions to a private nonprofit entity. Based on information from Federal Housing Finance Agency and organizations representing the views of the private financial markets, CBO estimates that enacting title VII would not significantly change Fannie Mae and Freddie Mac's administrative costs. Those entities spend about $4 billion annually on administrative costs, and CBO expects that activities required under S. 1484 could be accomplished within current plans to develop a joint securitization platform.

Qualified Mortgages

Section 106 would alter the definition of a type of mortgage called a qualified mortgage for purposes of legal exemptions. A qualified mortgage has certain characteristics that make the loan more affordable; borrowers who are eligible for such loans are presumed to be able to repay amounts owed. Among other things, the legislation would provide additional protections to creditors that hold mortgages that are not federally guaranteed or are not part of a private securitization and that do not meet certain qualified mortgage characteristics, such as limits on the allowable debt-to-income (DTI) ratio. The legislation also would provide additional protections to creditors that hold mortgages that do not meet certain qualified mortgage characteristics, such as limits on the allowable DTI ratio. Mortgages with a higher DTI would be slightly more likely to default than mortgages with a lower DTI, potentially exposing financial institutions that offer such mortgages to additional risk. CBO estimates that the magnitude of the marginal change in mortgage losses as a percent of total bank portfolios would be small, less than one-tenth of one percent. Losses to financial institutions, however, would not necessarily translate into a bank failure with related losses to the Deposit Insurance Fund. As a result, CBO estimates that enacting the provision would not have a significant effect on budget deficits over the 2016-2025 period.

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 S. 1484 as reported by the Senate Committee on Banking, Housing, and Urban Affairs on June 2, 2015

	By Fiscal Year, in Millions of Dollars												
	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2015-2020	2015-2025
NET INCREASE OR DECREASE (-) IN THE DEFICIT													
Statutory Pay-As-You-Go Impact	0	16	29	40	38	39	42	42	43	43	43	164	377
Memorandum:													
Changes in Outlays	0	8	20	31	29	30	32	32	34	34	34	118	284
Changes in Revenues	0	-8	-10	-9	-9	-9	-10	-9	-9	-9	-9	-46	-93

INCREASE IN LONG-TERM SPENDING

CBO estimates that enacting the legislation would not increase net direct spending or on-budget deficits by at least $5 billion in at least one of the four consecutive 10-year periods beginning in 2026.

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

S. 1484 contains intergovernmental mandates, as defined in UMRA, because it would limit the application of some state laws. Because the preemptions would impose no duty on state governments that would result in additional spending or a loss of revenues, CBO estimates that the aggregate costs of the intergovernmental mandates would fall well below the UMRA threshold ($77 million in 2015, adjusted annually for inflation).

Mandates in the bill would:

- Preempt state laws that allow the voiding of contracts between Federal Home Loan Banks and insolvent credit unions whose deposits are insured by private insurers;

- Preempt state and local laws by granting people protection from civil liability when they disclose, in good faith, unethical appraisal practices. Any penalties associated with such disclosure also would be waived; and

- Preempt state licensing laws by granting a temporary, 120-day license for some registered loan originators who become employed by a state-licensed mortgage lender, banker, or servicer.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

S. 1484 would impose private-sector mandates as defined in UMRA on individuals and businesses in the financial services industry. The bill would eliminate exiting rights of action, require additional reporting for some insurers, apply standards for processing funds in two American territories, and increase certain regulatory fees. Because the incremental changes required to comply with the mandates would be small relative to existing practices, CBO estimates that the aggregate cost of the mandates in the bill would probably fall below the annual threshold established in UMRA for private-sector mandates ($154 million in 2015, adjusted annually for inflation).

Limitations on Existing Private Rights of Action

Safe Harbor for Portfolio Lending. Section 106 would impose a private-sector mandate by eliminating an existing right of action against lenders that hold mortgages on their balance sheets. Under current law, lenders of mortgages that meet the standards for qualified mortgages are granted legal protection from civil actions based on a claim that the lender failed to comply with the ability-to-repay requirements. By broadening the definition of qualified mortgages to include mortgages held on a lender’s balance sheet, the bill would limit the right of borrowers to file claims against holders of such loans. The cost of the mandate would be the forgone value of the awards and settlements in such claims. Based on information from the Consumer Financial Protection Bureau, CBO estimates that the number of such claims and the awards in such cases would be relatively small.

Safe Harbor for Complaints Against Appraisers. Section 112 would impose a private-sector mandate by limiting an existing right for appraisers to pursue defamation or other civil claims against individuals who, in good faith, report unethical appraisal practices against them. According to industry sources, a number of limitations in local common law and statutory law currently deter appraisers from bringing defamation lawsuits against complainants. As a result, the number of appraisers that would be limited in their ability to pursue such claims as a result of the bill would be small, and CBO estimates that the forgone value of any potential awards from such claims also would probably be relatively small.

Requirements on Private Insurers of Credit Unions

Section 102 would impose a mandate on private insurers of deposits at credit unions that are members of the Federal Home Loan Bank system. It would require such insurers to submit a copy of their annual independent audit to the Federal Housing Finance Agency. Because such insurers already submit their annual audits to other entities, CBO estimates that the cost of complying with the mandate would be minimal.

Extended Application of the Expedited Funds Availability Act

Section 120 would impose a private-sector mandate by requiring accounts at and checks drawn on commercial banks in American Samoa and the Northern Mariana Islands to meet standards required under the Expedited Funds Availability Act. The standards would require those banks to process such accounts and checks sooner than is their current business practice. The cost of the mandate would be the administrative expenditures and the net income forgone from lost interest as a result of expediting their banking processes. Based on the small number of banks that would be affected, CBO estimates that the direct cost of the mandate would be relatively small.

Increased Fees and Assessments

CBO expects that some regulatory agencies would increase fees or assessments to offset some of the costs of implementing the additional regulatory activities required by the bill. Thus, the bill would increase the cost of existing mandates on private-sector entities required to pay those fees or assessments. Based on information from various financial regulatory agencies, CBO estimates that the incremental costs of such fees and assessments would average about $10 million per year over the 2016-2020 period.

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