Outline

I. Intro/Preface

Commented [RR(1]: Highlighted sections indicated bracketed language, or sections I need to revisit or do more work.

Commented [RR(2]: This section is perhaps unnecessary. The primary purpose is to link CBA to practical everyday decision-making. Can easily delete if it doesn't add value.

Cost-benefit analysis (CBA) is simply an accounting of the positive and negative impacts of the choices available when making a decision. As such, CBA is ubiquitous in everyday life. In fact, is difficult to imagine a careful decision without a consideration of both the positive and negative impacts the various choices would have on our lives. These decisions can be as consequential and complex as choosing where to live, or as simple as choosing a cereal at a grocery store. The former decision involves considering housing costs, size, and amenities; transportation options and costs; as well as geographical amenities of the community like schools, restaurants, and recreation. Housing choices will invariably differ along these qualities, and making a decision involves weighing tradeoffs associated with each choice. Likewise, choosing a cereal may involve considerations of nutrition, price, brand-recognition, and even box size may play a role for storage-space constrained consumers.

These two examples are instructive. For instance, the decision between cereals is minor and unlikely to have large consequences for a consumer's lifetime well-being. Of course, the vitamins and minerals offered by the cereal options will impact the consumer's health, but the incremental contribution of a single cereal decision to lifetime well being is very small. Because of this, some consumers may not spend much time deciding – and may choose based on the artwork on the box or some other trivial consideration. But for others, some care will go into the decision and those thoughts will invariably be some form of weighing the advantages and disadvantages of each option.

On the other hand, housing decisions are highly consequential choices that impact household wealth and happiness; the amount of time spent with their family; and even the opportunities available to children. Prospective homebuyers might consider making a list of the advantages and disadvantages of their housing options to help them make their choice. Some homebuyers may even research housing price growth in the various neighborhoods to approximate the impact of their choices on their net worth. Still others may make a spreadsheet to estimate the amount of equity they may have in their home after five or ten years. Surely, many people evaluate the monthly cost of the home and how

[1] Is there a public link?

much of their budget would remain for other pursuits. The particularly enterprising buyers may even factor in the impact of their decision on their children's future earnings.[2] Very few people are likely to think that these analyses are unwarranted, irresponsible, or overly time-consuming for such a consequential decision.

The examples highlight that CBA is a common tool people use to make decisions, and that the level of care and analysis we do to inform our decisions varies by how important the decision is. Not only does this explain why we may do more analysis on a housing decision than a cereal decision, it is why corporations have entire finance departments to evaluate the merits of proposed projects. CBA is deployed in the private sector to inform decisions on projects ranging from capital investment to new product offerings. Government regulator's use of cost-benefit analysis as a tool to assist in making and supporting decisions that impact *every* mortgage or *all* firms in an industry reflects the prudence and care we put into decisions we make in our personal and professional lives. The formal cost-benefit analysis done by government agencies in support of regulatory decisions mimics these decision-making processes that we all use every day. Furthermore, it lends credibility, accountability, and transparency to decisions that are often made by career or appointed civil servants that involve how we allocate our society's valuable and scarce resources.

II. History of Cost-Benefit Analysis in Agency Rulemaking

CBA of the informal variety referenced in the previous section has likely been a part of human decision-making for a very long time. For instance, Boardman et al. open their textbook on CBA with an extended quotation from a letter written by Benjamin Franklin to Joseph Priestly where Franklin describes his approach to making important decisions by making a list of pros and cons, and then striking through those pros and cons he believes cancel out.[3] Franklin says that the reason for this is that each of the "pro and con are not present of mind at the same time" and he says of the results, "I think I can judge better, and am less liable to make a rash step… ."[4]

The formal variety of CBA that has become ubiquitous at executive agencies and has been a cornerstone in regulatory decisions spanning four decades and six Presidential administrations began to take shape in the 1930s. The Flood Control Act of 1936 required the Army Corps of Engineers to conduct CBAs on planned flood and harbor projects. This requirement resulted in the further refinement of the practice and principles of cost-benefit analysis in water resource decisions in the following decades, ultimately culminating in the Bureau of the Budget's 1952 Circular A-47 outlining the principles of CBA in guidance for agencies making water resource decisions.[5]

While CBA in on-budget resource decisions began to flourish earlier in the 1930s and 1940s, nascent obligations resembling CBA began to appear in the regulatory space in the 1970s.[6] The first real

[2] [HYPERLINK "https://scholar.harvard.edu/hendren/publications/effects-exposure-better-neighborhoods-children-new-evidence-moving-opportunity"]
[3] Cite Boardman
[4] Cite Franklin letter
[5] [HYPERLINK "https://opensiuc.lib.siu.edu/cgi/viewcontent.cgi?article=1196&context=jcwre"]
[6] Shapiro, Stuart. "The Evolution of Cost–Benefit Analysis in US Regulatory Decisionmaking." (2011). [HYPERLINK "https://pdfs.semanticscholar.org/d06b/2183437547e4b32614e798025713c169e685.pdf?_ga=2.267257870.1026816008.1596222479-1635246547.1596222479"]

obligation to conduct CBA in support of regulatory as we know it today was established by President Reagan in 1981 with his EO 12291, which required that agencies conduct a regulatory impact analysis of all major regulations, including an assessment of benefits, costs, and net benefits. The order also established centralized review and coordination of agency rulemaking and associated regulatory impact analyses within the Office of Management and Budget (OMB).

In part due to procedural criticisms of OMB review, President Clinton replaced EO 12291 with EO 12866, which reaffirmed the practice and principles of regulatory CBA, but limited OMB review to "significant" regulations.[7] This reform substantially reduced the number of rules that OMB reviewed.[8] Nevertheless, EO 12866 has proven to have staying power, as every President since has reaffirmed its principles and the practice of CBA – and it remains in force to this date.

Between 1993 and today, many memos, circulars, and orders have been issued to enhance and further solidify the practice of conducting CBA in the rulemaking process for executive Agencies. OMB Circular A-4 was published in 2003 providing technical guidance for agencies on matters ranging from valuing reductions in mortality risks to the discount rates agencies should use for future benefits and costs to reflect social time preference.[9] President Obama issued EO 13563 in 2011, which required agencies to conduct retrospective analyses of prior rulemakings and remove outdated regulations. EO 13563 also built upon 12866's principles of considering impacts that are difficult to quantify by adding human dignity and fairness considerations, in addition to equity and potential distributive impacts of regulation. President Trump's EO 13771 reaffirmed both EOs 13563 and 12866 and introduced an additional constraint on regulatory decision-making in the form of a regulatory cost allowance for every executive regulator.[10]

While CBA has been a cornerstone of regulatory decision-making at executive agencies for decades, its development at independent agencies has been mixed. A report from the Administrative Conference of the United States summarized the statutory authorities of independent regulatory agencies and found that three were statutorily required to do cost-benefit analysis (CPSC, the Fed for electronic funds transfer rules, and FTC), six are obligated to adhere to a weaker standard of "considering" costs and benefits (CFPB, SEC, CFTC, the Fed, OCC, and FDIC), and three have no requirements at all (NRC, FERC, and FCC).[11]

Commented [RR(3]: If time, insert international experience with regulatory review and analysis, OECD recommendation, etc.

III. Dodd-Frank Cost-Benefit Requirement

The CFPB's requirements to consider the costs and benefits of their rules stem from Sec. 1022(b)(2) of the Dodd-Frank Act, which are worth repeating here:

> In prescribing a rule under the Federal consumer financial laws—(A) the Bureau shall consider—(i) the potential benefits and costs to consumers and covered persons, including the potential

[7] [HYPERLINK "https://www.archives.gov/files/federal-register/executive-orders/pdf/12866.pdf"]

[8] Data from www.reginfo.gov, comparing the period Feb. 19, 1981 through Sept. 30, 1993, with the period Oct. 1, 1993 through Sept. 30, 2017.

[9] [HYPERLINK "https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/circulars/A4/a-4.pdf"]

[10] [HYPERLINK "https://www.govinfo.gov/content/pkg/FR-2017-02-03/pdf/2017-02451.pdf"]

[11] Admin. Conf. of the U.S., Recommendation 2013-2, *Benefit-Cost Analysis at Independent Regulatory Agencies*, [HYPERLINK "https://www.govinfo.gov/content/pkg/FR-2013-07-10/pdf/2013-16541.pdf"] (July 10, 2013). Pg. 56.

> reduction of access by consumers to consumer financial products or services resulting from such rule; and (ii)the impact of proposed rules on covered persons, as described in section 1026, and the impact on consumers in rural areas… .

Therefore, the Bureau's requirement to consider costs and benefits have universe components (e.g. groups of people the analysis should cover), and content components (costs, benefits, and loss of access to financial products). [MAYBE ADD LANGUAGE HOW UNIVERSE COULD LIMIT CONSIDERATIONS OF CBA?]

Commented [RR(4]: I feel like more meat should be put on these bones by an attorney with background on statute and case law.

If legally defensible, it would be good to counter claim that this language forecloses a proper CBA consistent with principles below.

IV. Purpose of Cost-Benefit Analysis

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A formal cost-benefit analysis is a structured approach to organizing the assumptions, information, and knowledge about the advantages and disadvantages of competing approaches to solving a problem. A typical CBA begins with an analysis of the nature and extent of the problem the regulator is trying to solve. Then the analysis proceeds to identify and analyze alternative approaches to solving the problem while also disclosing the information and methods used. Finally, the analysis summarizes the benefits and costs of each alternative and recommends a preferred approach.

The purpose of using CBA in regulatory analysis are as follows:

1. **Improve regulatory decisions:** First and foremost, a rigorous and structured approach to analyzing a problem and evaluating the tradeoffs associated with alternative approaches to solving a problem can reveal new information or present information in valuable new ways that leads to better regulatory decisions.
2. **Transparency:** The process of conducting a CBA to support a regulatory decision enhances transparency by forcing agencies to identify the sources of information and the methodologies used to analyze a problem and the solutions.
3. **Accountability and credibility:** Federal regulators have numerous stakeholders in the actions they take, including Congress, the President, regulated parties, taxpayers, and voters. Agencies are often given broad authorities by Congress, which often prefers to defer certain regulatory decisions to professionals in agencies. A rigorous cost-benefit analysis makes transparent the trade-offs involved in a decision to the public and to Congress.

V. Principles and Best Practices of Cost-Benefit Analysis

Identification and implementation of a set of principles or best practices of CBA is a common feature in regulatory programs. In the United States, EO 12866 and OMB Circular A-4 provide guidance on best practices in regulatory CBA. Similar guidance exists in other countries, as well.[12] In some ways, the establishment of principles and best practices is itself a best practice. It standardizes important elements and establishes a set of policies to hold agencies accountable to. The accountability function can be enhanced by an oversight body that reviews regulatory analyses for consistency with the best practices.

[12] Provide survey: UK, etc.

To identify principles and best practices of CBA, the Taskforce reviewed several authorities on cost-benefit analysis – in addition to relying on expertise amongst the Taskforce members and staff. First, and perhaps most importantly, the Taskforce Reviewed OMB Circular A-4 providing technical guidance to the heads of executive agencies on regulatory analysis. Second, we reviewed another OMB resource - OMB Circular A-94, "Guidelines and Discount Rates for Benefit-Cost Analysis of Federal Programs."[13] Third, we reviewed the United Kingdom's Regulatory Policy Committee guidance on regulatory impact assessments.[14] Fourth, we reviewed the best practices for CBA identified in the Administrative Conference of the United States (ACUS) Recommendation 2013-2, *Benefit-Cost Analysis at Independent Regulatory Agencies.*[15] Fifth, we studied the Organisation of Economic Cooperation and Development's (OECD) 2012 *Recommendation of the Council of Regulatory Policy and Governance.*[16] Lastly, the Taskforce consulted *Cost Benefit Analysis; Concepts and Practice* by Boardman et al.[17] Perhaps unsurprisingly, there is broad agreement across these sources of expertise on the subject regarding the principles and best practices of CBA.

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The Taskforce believes that any CBA that fulfills the purposes mentioned above must at least adhere to the following principles and best practices:

1. **Analysis of the problem.** The agency should analyze the extent and nature of the problem it intends to correct. This analysis should include a discussion of any relevant market failures and present evidence in support of any claims of market failure. The discussion should also include any distributional concerns or problems related to fairness, equity, and human dignity.
2. **Definition of the baseline.** The agency should establish a baseline for comparing the cost and benefits of regulatory alternatives. This is usually more complicated than simply using data on compliance, production, or sales in the past. It usually involves forecasting sales or production into the future, as well as any potential voluntary compliance.
3. **Selection of a time horizon for the analysis.** Selecting a time horizon is an important part of regulatory analysis, and a potential source of bias if not done correctly. Because the timing of the costs and benefits of a regulation are often asymmetric, a time-horizon that is too short will bias the net benefits towards the earlier impacts. Unfortunately, there is no one size fits all approach to time-horizon selection, but generally agencies should strive to select a time-horizon to minimize bias. Product life-cycles or refresh/redesign cycles are often instructive. Generally, due to discounting

[13] [HYPERLINK "https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/circulars/A94/a094.pdf"]

[14] [HYPERLINK "https://www.gov.uk/government/publications/how-the-regulatory-policy-committee-scrutinises-impact-assessments/regulatory-policy-committee-recommendations-used-when-scrutinising-impact-assessments"]

[15] Admin. Conf. of the U.S., Recommendation 2013-2, *Benefit-Cost Analysis at Independent Regulatory Agencies*, [HYPERLINK "https://www.govinfo.gov/content/pkg/FR-2013-07-10/pdf/2013-16541.pdf"] (July 10, 2013).

[16] [HYPERLINK "https://read.oecd-ilibrary.org/governance/recommendation-of-the-council-on-regulatory-policy-and-governance_9789264209022-en" \l "page1"]

[17] Boardman cite

for social time preference (discussed in more detail on page XX), the longer the time-horizon of the analysis the smaller the potential bias.

4. **Identification of Alternatives.** Various approaches to solving the problem(s) identified should be identified. These alternatives should include non-regulatory options, such as enforcement actions or use of other non-regulatory incentives to encourage the desired behavior. These alternatives may also consider the role of state and local governments in solving the problem.
5. **Analysis of Benefits and Costs.** The agency should estimate the costs and benefits of each alternative using the best available science and evidence. Cost estimates should reflect the full opportunity cost to society of diverting resources towards compliance with the regulation. Likewise, benefit estimates should consider opportunity costs – or the value of what society is willing to forego to enjoy a benefit. While there are many approaches to valuing benefits and costs, willingness-to-pay approaches that assess a benefit or cost based on revealed valuations in market transactions are particularly compelling.[18] The benefits and costs of *each alternative* should be quantified, aggregated, and monetized to the maximum extent possible. Any assessment of benefits must include an analysis of how effective each alternative would be at addressing the problems identified.
6. **Assessment of Unintended Consequences.** The analysis should include assessment of potential unintended consequences and include them in the estimates of benefits and costs.
7. **Discounting future benefits and costs.** Agencies should create schedules of benefits and costs and discount them the to present value using an appropriate social discount rate. There are several methods for determining the appropriate discount rate depending on the nature of the rule being analyzed and the time horizon of the analysis. Executive agencies use a range of 3 percent reflecting a risk-free rate of return and 7 percent reflecting the opportunity cost of capital.[19]
8. **Treatment of economic transfers.** An economic transfer occurs when a benefit to one person group is exactly offset by a cost to another person or group. Common forms of transfers include government payments and welfare transfers between consumers and producers of a product associated with a change in price or change in market efficiency (e.g. reduction in market power results in some increased efficiency, but also a transfer from producers to consumers). These impacts are not comparable to benefits and costs and should not be allowed to influence the estimated net benefits. In some cases, transfers to certain groups may be part of the intent of rule or statutory requirement. These cases often involve considerations of distributive impacts, fairness, equity, or human dignity – and these are the benefits the analysis should focus on (as opposed to the dollar value of the transfer). If those considerations are unavailable, the agency may consider a cost-effectiveness analysis in lieu of a cost-benefit analysis.
9. **Identification and analysis of Uncertainty.** A CBA should identify key sources of uncertainty and discuss the potential impacts of that uncertainty on the results and conclusions of the analysis. For particularly important rulemakings, the agency should

[18] OMB Circular A-4 has an extended discussion of the various approaches to valuing benefits.
[19] [HYPERLINK "https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/circulars/A4/a-4.pdf"]

conduct sensitivity analyses to estimate the potential impact of that source of uncertainty on the analysis. If uncertainty is such that a determination as to whether the preferred regulatory approach has net benefits is impossible, the agency might consider whether to delay the rulemaking to explore the issue further.

10. **Incremental Analysis.** Many regulations contain multiple provisions that incur costs and generate benefits. For such rules, it is important that the net benefits of one provision aren't used to obscure the net costs of another – as doing so prevents the agency from identifying the alternative with the highest net benefits. The agency should independently assess the marginal contribution of each provision to the benefits and costs of the rule.
11. **Presentation of benefits, costs, transfers, and net benefits.** The aggregated and discounted benefits, costs, transfers, and net benefits should be summarized – usually in tabular form. Usually, this summary information is included in an introduction or executive summary, as well as a final chapter in the analysis.
12. **Policy Recommendation.** The analysis should recommend the alternative that maximizes benefits net of costs – including any non-quantified benefits. Non-quantified benefits may include distributional impacts or improvements in equity, fairness, or human dignity – though the agency should not foreclose the possibility that at least some portion of these benefits could be quantified and monetized. Note that if the agency were to reject the alternative that maximizes net benefits (including non-quantified benefits), the agency would have to explain their justification for doing so – which further advances the purpose of transparency in rulemaking.
13. **Analytical transparency.** A CBA must be as transparent and reproducible as possible. It must be clear about the data sources, methodologies, and assumptions used to conduct the analysis. It must identify any limitations of the analysis and discuss the impacts those limitations have on conclusions drawn from it. The analysis should be based on the best available science and evidence. Where the evidence supporting an analytical element is mixed, the agency should include a full or representative discussion of the varying sources of evidence and disclose how each source informed the analysis.
14. **Proportionality.** An agency should calibrate the amount of time and resources that go into regulatory analysis according to the importance of the decision they are analyzing. In other words, agencies should consider the costs and benefits of doing a cost-benefit analysis.

VI. Implementation of CBA

Commented [RR(7]: There are an endless number of combinations of attributes of an oversight body, so this discussion could become quite extended if we let it.

More work is needed here

Could benefit from TZ and HB thoughts on where to take this section.

Regulatory CBA best practices are often implemented alongside the creation or establishment of an oversight body that reviews regulatory analyses for quality and compliance. These oversight bodies can play a variety of roles in the development of regulations and regulatory analyses, including providing general guidance on implementing CBA, reviewing regulations and regulatory analyses for consistency with best practices prior to publication, and making public statements about the quality of regulatory analyses.

In 2012, OECD recommended that each of its member nations establish policies and principles of regulatory CBA, as well as "[e]stablish mechanisms and institutions to actively provide oversight of regulatory policy, procedures, and goals, support and implement regulatory policy, and thereby foster regulatory quality."[20] Since 2012, OECD has been monitoring implementation of its recommendations in member countries and has reported data on where this review function sits in the Government. The most prominent location for oversight and review is the "Center of Government." The second most popular location for these functions is a "non-departmental body" at arms-length from central government. Other popular locations are Finance, Treasury, or Justice departments.[21]

In the United States, the oversight and review functions are played by the Office of Information and Regulatory Affairs (OIRA) within the Office of Management and Budget (OMB), which functions within the Executive Office of the President (EOP). The location of OIRA within the White House almost certainly lends power and influence to the office, but it also means that OIRA is ultimately controlled by political forces.[22] Depending on your perspective, this could be a democratizing influence on technical decision-making, or it could be viewed as a political intrusion.

OIRA's role in the regulatory process is multifaceted, which is governed by Executive Order 12866.[23] During review, OIRA consults with regulators and provides advice on both the regulatory analysis and the decisions it supports. In addition to serving as a CBA resource and reviewer, they moderate interagency disputes and coordinate the White House review of agency regulations.[24] Typically, OIRA review concludes without any public statement as to the quality of the analysis or the rulemaking generally. On rare occasions when OIRA exercises its authority to return a regulation to an agency for reconsideration, a public return letter is released detailing analytical deficiencies.[25] Importantly, independent regulators, including CFPB, are not required to comply with OIRA guidance and are not subject to OIRA review.

So while the US may exemplify the "Center of Government" approach, the United Kingdom's Regulatory Policy Committee (RPC) is an example of an independent, or non-departmental, oversight and review office. [INSERT BRIEF DESCRIPTION OF AUTHORITIES].[26]

In contrast to OIRA, the RPC issues a public opinion of each of the regulatory analyses they review. The analysis is given an overall rating based on whether it was "fit for the purpose," as well as summarizing the analysis and offering critiques. [However, the RPC has no impact on regulatory decisions above and beyond the impact of their public and technical opinions. This is appropriate, given that the RPC is somewhat separated from democratic processes.]

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The differences between the two oversight and review offices are interesting. The OIRA model is powerful and integrated into the decision-making process. But perhaps because of its role in managing the decision-making process, its analytical findings are rarely made public. In contrast, the RPC is highly

[20] OECD Recommendation
[21] [HYPERLINK "https://www.oecd-ilibrary.org/sites/9789264303072-7-en/index.html?itemId=/content/component/9789264303072-7-en" \l "tablegrp-d1e6487"]
[22] Cite Cass Sunstein book
[23] 12866
[24] Cass again
[25] Link to return letters
[26] Need RPC research

transparent with its findings, but it isn't clear how influential they are. Importantly, it isn't clear the extent to which there is a real tradeoff between integrating CBA into decision-making and transparency of the oversight office, and not idiosyncratic attributes of these two institutions.

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VII. Evaluation of CFPB's Regulatory Guidance "Regulatory Analysis Policies and Procedures for Substantive Rulemaking"[27]

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The Taskforce reviewed the Bureau's guidance for rulemaking analysis "Regulatory Analysis Policies and Procedures for Substantive Rulemaking" (RAPP) for consistency with the regulatory best practices. The Taskforce found several areas of agreement, but also areas where there is some tension between the Bureau's analysis. This section summarizes our findings from the review.

- The guidance identifies market failures as a potential justification for regulation and provides that the Bureau should consider whether the underlying statute addresses any market failures. The agency also lists privacy and the dignity of consumers as other potential purpose of regulation. The guidance does not provide any guidance on the evidentiary support needed to justify a market failure claim.
- The RAPP directs Bureau analyses to define a baseline in a manner that is generally consistent with the best practices mentioned above – indicating that it is matter of professional judgment that requires consideration of a broad set of factors and circumstances.
- The guidance provides potentially contradictory direction on selection of the time horizon of the analysis. First it suggests "[a] possible ending point is the date at which staff expects to review a rule." It appears this refers to the five-year retrospective review schedule the agency has in place. This direction is highly unlikely to be an appropriate time horizon for an analysis, as it is likely the rule has asymmetric costs and benefits that continue out beyond five years. However, the RAPP also provides that the Bureau should seek to identify "the pattern in which the benefits, costs, and impacts will occur over time." This latter guidance is entirely consistent with the best practices mentioned above and would not generate any biases toward earlier impacts.
- The RAPP does provide that the Bureau should identify alternatives. However, while the guidance is permissive of a quantitative analysis of alternatives, it does not indicate that the Bureau must or should analyze alternatives quantitatively. Given the fundamental importance of the inclusion of alternatives in the quantitative assessment, this is a critical divergence from CBA best practices.
- The guidance in the RAPP on quantifying and monetizing benefits are generally consistent with the best practices above, with some exceptions. First, the guidance does not specify that costs and benefits should include opportunity costs. Secondly, the guidance does not emphasize that benefits and costs should be aggregated, quantified, and monetized to the maximum extent possible.
- A charitable read of the RAPP guidance would suggest that unintended consequences are contemplated in the assessment of costs and benefits. But there is no explicit

[27] Is there a public link?

guidance on how the Bureau should analyze and treat unintended consequences. Regulations change behavior by changing the price and choices of goods and services, as well as the quantities available. It is important for regulators to systematically analyze the potential ramifications of regulatory options – both positive and negative.

- The RAPP advises staff to consider discounting future costs and benefits, consistent with CBA best practices.
- A charitable read of the RAPP guidance may have intended to separate transfers from costs and benefits, but this is not explicitly addressed. Identification and qualification of transfers is a key element of CBA, and the absence of guidance on the subject is a significant weakness. The CFPB's authorities related to competition (RESPA and TILA) and fair lending have significant transfer implications that require careful consideration.
- The guidance is generally consistent with best practices regarding treatment of uncertainty. It indicates that uncertainty around assumptions should be described and advises staff to use sensitivity analyses to "examine how figures would change with plausible changes in assumptions and data."
- The RAPP doesn't explicitly direct staff analysts to conduct an incremental assessment, though it does advise "it may be appropriate to proceed through the relevant provisions of the regulation, discussing the benefits and costs on each affected group at the end." An incremental analysis is essential to identifying the alternative that maximizes net benefits, and as such must be a feature of any rulemaking with multiple provisions.
- The most significant divergence of the guidance from best practices is that it does not provide guidance on comparing costs and benefits, summarizing other impacts, and recommending a preferred alternative.

VIII. Results of Taskforce Review of CFPB Analyses of Major Rulemakings

Commented [RR(11]: Hope to create some summary tables showing qualitative information.

The Taskforce reviewed the analyses of [every? Most? Need to update here] rulemaking designated as Major under the Congressional Review Act to better understand how the agency implements cost-benefit analysis. The Taskforce reviewed for consistency with CBA principles and best practices, as well as Sec. 1022 of Dodd-Frank.

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The Taskforce believes that it is important to stress that its findings are not criticisms of Bureau staff. Indeed, the Taskforce is quite certain that the Bureau is staffed by many able economists and analysts that are up to the task of conducting a quality CBA. Instead, the Taskforce believes the problems identified owe to insufficient time, priority, and resources allotted to the task. If anything, we hope our findings serve to elevate the work and talents of the Bureau's technical staff by highlighting how critical they are to the policy process.

Furthermore, the Taskforce is aware that the CBA principles and best practices identified here go above and beyond what is required of the Bureau by Sec 1022 of Dodd-Frank. As such, a retroactive review for consistency with standards the Bureau was not required to satisfy cannot and should not be viewed as an assessment of performance. Instead, these reviews should be seen as a "gap analysis" seeking to understand the difference between current practices and those identified above.

Conclusions from Taskforce Review of Agency Analyses

Analysis of the Problem

Most of the Bureau's analyses feature some discussion of market failures and/or other problems they are trying to solve. In some circumstances, the Bureau even supports these market failure claims with evidence. For instance, in the 2013 final rule amending mortgage servicing rules under RESPA and TILA, the Bureau provided a summary of the literature on the external costs of foreclosure. In other instances, the Bureau provides no evidence to support market failure claims.[28] In one rule reviewed by the Taskforce, the Bureau relied on a single page non-scholarly and qualitative essay that no longer existed at the location cited.[29]

In those instances where the presence of a market failure or other problem is not supported by evidence, or supported only by weak and non-conclusive evidence, the agency can bolster support for its claims with more analysis of its own. Without regard to the conclusion of the analysis, the 2017 Payday Lending final rule attempted to justify its market failure claim with an extended discussion and analysis of the evidence concerning consumer expectations of payday lending products.[30]

However, the Bureau did not do such analysis in many instances – potentially leading to meaningful mistakes about the nature of the problem the agency was attempting to address. For instance, the 2013 HMDA final rule argued that HMDA data were a public good market failure – meaning that it is both nonrival and nonexcludable. Absent Government intervention, mortgage market data that lives in easily shareable files may be non-rival, in the sense that consumption of a unit of data by one person doesn't exclude the consumption of the same unit by another person. However, proprietary data can be made excludable by contractual obligation. As such, any critical analysis of this claim would reveal that mortgage data is not, in fact, a public good. Instead, it is better considered a "club good.[31] While it is certainly possible that government intervention is needed in a club good market, the nature of the optimal intervention will be different than in the case of a nonrival and nonexcludable public good (which necessitates government provision).

It is important to note that the analysis of the problem shouldn't involve simply listing every potential market failure that could be potentially relevant. Instead, it should be a careful assessment of the nature of the actual problem(s) for which mitigation is the true purpose of the rule. Furthermore, CBA best practices don't *require* that a market failure be present to justify regulation. For instance, a regulation may improve enforcement of standards in an efficient manner – and thus the net benefits of improved compliance with existing standards become the net benefits of the new rule – and this may be sufficient rationale. The 2013 HMDA rule did identify improved compliance and enforcement with fair lending and other standards as part of the purpose of the rule, and the benefits identified by the analysis are more connected to this problem than any market failure claim.[32] The analysis (and the

[28] 2013 Ability to Repay and Qualified Mortgage Standards and the 2013 HMDA final rule [NEED TO LIST THEM ALL] loan originator
[29] 2013 Loan Originators
[30] Insert formal citation to rule
[31] Footnote about club goods – established by Buchanan, could mention samuelson, provide source confirming nonrival excludable goods called club goods.
[32] A good rule of thumb is that if the benefits you identify aren't connected to a problem you identify, you have the wrong problem, the wrong benefits, or both.

decision-making it contributes to) may have been better off if it focused more on this issue, as well as the human dignity issues associated with improved compliance with fair lending rules.

Treatment of Alternatives

The Bureau's treatment of alternatives is one of its the most significant divergences from CBA best practices. In some instances, the Bureau does not identify any alternatives at all in their analysis, such as its analyses of the 2013 final rule amending mortgage servicing Rules under RESPA and TILA and the 2013 final rule on loan originator compensation requirements. The loan originator compensation rule is a particularly important example, which prohibits compensation to a loan originator based on the profitability of the loan products they sell. Generally speaking, incentive pay is a common form of compensation that is intended to reduce employer monitoring costs and align incentives between a firm and its employees – which in any reasonably competitive market should reduce costs to consumers.[33] Outright prohibition of this form of incentive pay is a particularly strident alternative to mitigate consumer harm when other alternatives are available, such as disclosure, standards of care akin to the suitability and fiduciary standards in investment adviser regulations, increased enforcement of fraud protections, etc. A CBA that evaluated the advantages and disadvantages of each approach would have been a valuable tool for decision-makers.

In all regulations reviewed, alternatives were generally excluded from the quantified and monetized analysis. The Taskforce identified one exception to this in the 2013 HMDA rule, where the Bureau quantitatively analyzed alternative reporting thresholds for closed-end mortgages – though this was not a fully monetized cost-benefit analysis. Other important level-setting decisions have gone without a quantitative assessment, such as the $500 maximum loan limit in the 2017 Payday rule (which doesn't identify or analyze any alternative loan limits).

Estimating Benefits, Costs, and Transfers

Aggregating costs and benefits are essential in CBA, as it makes comparing costs and benefits possible. In one analysis reviewed by the Taskforce, the Bureau presented aggregated cost and cost savings estimates.[34] In most cases, however, the Bureau does not endeavor to generate total cost and benefit estimates, even when doing so would have been a simple and straightforward task. Often, the Bureau did not aggregate unit cost estimates, and ongoing and upfront costs are not summed to form a total cost estimate.[35] As one example, the Bureau frequently references the benefits associated with reduced foreclosures,[36] but does not attempt to quantify these benefits even when estimates of the external costs of foreclosure have been developed and used by other agencies.[37] In the 2017 Payday Lending rule, the Bureau estimates the time cost of training employees, but does not use readily available wage information from BLS to monetize it.

[33] See discussion of agency costs here: [HYPERLINK "https://josephmahoney.web.illinois.edu/BA549_Fall%202012/Session%205/5_Jensen_Meckling%20(1976).pdf"]
[34] Respa-tila cite
[35] Payday and HMDA (and pretty much every rule)
[36] RESPA, RESPA-TILA? Loan Originators?
[37] The Department of Housing and Urban Development used a cost of foreclosure estimate of $10,339 in its Regulatory Impact Analysis for its Emergency Homeowners Loan Program. [HYPERLINK "https://www.huduser.gov/portal/periodicals/cityscpe/vol13num2/Cityscape_july2011_impact.pdf"]

Analyzing the effectiveness of each alternative is an important part of benefits estimation. In some instances, the Bureau has taken the effectiveness of the standard very seriously. For example, the 2014 rule integrating the RESPA and TILA mortgage disclosure forms presented evidence that the revised disclosure was easier to understand. In other instances, the assessment of effectiveness is quantitative in nature but incomplete.[38] Unfortunately, some analyses do not feature an assessment of the effectiveness of the standard. The 2013 rule prohibiting compensation based on the profitability of the loan products they originate did not include an assessment of how effective such a prohibition would be at reducing moral hazard. This would have been an important feature of the analysis, as one wonders why an employer couldn't just raise the base salary of the originators that earn the highest profits. In fact, it seems profitable originators would find themselves a hot commodity with other employers if their current employer didn't raise their base wages commensurate with their contribution.

In those cases where the Bureau estimates benefits or costs over the course of several years, the Bureau does tend to discount those future impacts back to present value appropriately. However, the justification for the selection of the time horizon of the analysis is often missing or non-transparent.[39] The Taskforce also noticed that the Bureau often amortizes upfront costs over a number of years, instead of putting them in the first year of the analysis without a clear justification.[40]

Finally, the Taskforce notes that it did not find a discussion of economic transfers in any of the regulations it reviewed. This may be due to the nature of the requirements under 1022 of the Dodd-Frank Act, which specifically require the Bureau to assess costs and benefits to specific groups, rather than society writ-large.

Policy Recommendation and Summary Information

None of the analyses reviewed by the Taskforce summarize, tabulate, or compare cost and benefits. Net benefits are never presented or calculated, and transfers do not appear in CFPB's analyses. Likewise, there are no qualitative discussions evaluating the tradeoffs. Omitting the presentation of cost and benefits, as well as any form of discussion evaluating the tradeoffs associated with alternative approaches, dramatically reduce the possibility that the Bureau's CBAs would achieve the purposes of improving decisions, advancing transparency, and enhancing credibility and accountability. The omission also forecloses the possibility that the CBA could recommend a policy alternative. This is the important and meaningful contrast between the best practices identified above (as well as the purposes of CBA) and CFPB's current practice.

Uncertainty and Transparency

At times, the Bureau has shown commitment to highlighting uncertainty and dealing with it appropriately. For instance, the 2013 Ability-to-Repay rule conducted an excellent sensitivity analysis for its liability cost estimates in response to comments that legal fees were likely to be higher than estimated at the proposed rule stage and the amount of billable hours were likely to be longer. In another example, the Bureau's 2013 rule on Loan Originator Compensation features a frank discussion of state of the literature on the subject:

[38] Payday assessment includes effectiveness at preventing loan, but not harm.
[39] All rules reviewed
[40] RESPA, at least

The Bureau, however, notes that the current state of academic research has not provided an unequivocal answer to the question of whether any given profit-based compensation arrangement will produce incentives sufficiently strong for individual loan originators to engage in consumer steering. The Bureau also notes that this research, whether based on theoretical or empirical methods, shows that the potential for any profit-sharing plan to create adverse incentives are acutely sensitive to the specific features of the working environment and the means by which such profits are distributed to the relevant individual loan originators. Finally, the Bureau notes that any potential reduction in the strength of these incentives is almost surely insufficient, under all realistic circumstances, to eliminate them entirely.[41]

Nevertheless, the Taskforce's review revealed that discussion of uncertainty was generally sparse. In its review of [X NUMBER] of Major rulemakings (that is, rules expected to have an annual impact of over $100m), the Taskforce identified only [ONE] sensitivity analysis. [IF TIME SUGGEST SOME AREAS FOR MORE SENSITIVITIES].

The Taskforce's review found that the Bureau's analyses were generally transparent and reproducible, with some exception. For instance, the 2017 rule on payday lending repeatedly references "simulations" done by the Bureau. While the analysis highlights some of the findings of the analysis, the inputs, outputs, assumptions and methodologies are generally withheld.[42]

Consistency with Sec. 1022 of Dodd-Frank

As discussed above in the [SECTION], the CBA requirements in Sec. 1022 of the Dodd Frank Act has universe components (e.g. groups of people the analysis should cover), and content components (costs, benefits, and loss of access to financial products). The Taskforce's review finds that the Bureau does very well in addressing the universe components of the Act. In fact, the Bureau organizes their CBA according to the identified groups of people and business identified in the Dodd-Frank Act and explicitly addresses costs and benefits to each group.

However, the Taskforce's review found that the Bureau rarely deliberates and scrutinizes issues related to access to financial products. Often, the Bureau merely provides a statement that it considered issues related to access, but summarily dismisses any concerns of reduced access without assessing them analytically or quantitatively – even in cases when the Bureau estimates increased costs that may be passed on to consumers.[43]

IX. Valuing Benefits

Commented [RR(13]: Hope to review symposium statements before drafting.

[Important topics to hit here:

- While CBA should accommodate difficult or impossible-to-value benefits qualitatively, its possible that most benefits are quantifiable.
- For instance, executive agencies have developed and refined methods to estimate the WTP to accept mortality risks, that allows agencies to value lives saved.

[41] Cite loan originators
[42] Reference payday
[43] HMDA, loan originators, respa

- DOJ prison rape rule monetized benefits, which helped make the case for the rule – monetizing doesn't mean less stringent regulation.
- The methods for valuing physical injuries and illnesses are relevant to the types of harms CFPB mitigates.
  - Its reasonable to suggest that victims of fraud, loss of privacy, discrimination/racism, etc. are injured some sense – they likely experience distress and pain they would be willing to pay to avoid.

X. Criticisms of Cost-Benefit Analysis

Commented [RR(14]: Should review comments

[Of course, there are some common objections to CBA. There are some who criticize cost-benefit analysis as undemocratic by placing democratically elected or appointed officials in a "strait-jacket" to select only the regulatory option that performs best in a CBA.[44] This criticism may be accompanied by a proclamation that the benefits of Federal regulation are often difficult to estimate and monetize – inevitably leading to a situation where costs are estimated but benefits are not. These critics contend that this imbalance may prejudice a decision against taking regulatory action. But these criticisms seem to fail with a more nuanced assessment of CBA. Federal regulators primary obligation is to promulgate regulations that are consistent with their statutory mandates and authorities and no cost-benefit analysis can override the constraints placed on the agency by Congress – and very few (if any) statutes require an agency to choose the best performing alternative in a CBA.

Commented [RR(15]: I'm not sure this language is necessary. It may be better to limit critiques to those that appear in comments to RFI.

Section needs more work – need to review comments to RFI

Furthermore, any guidance on CBA must address the treatment of benefits that are difficult or impossible to quantify and provide for the possibility that a qualitative assessment of unquantified benefits may lead to the selection of an alternative that is not the most the net-beneficial according to the quantified assessment. Nor is it clear that the presence of cost estimates together with the absence of benefit estimates biases decisions against more stringent regulatory alternatives. In fact, a standardized approach to cost benefit analysis that provides guidance on calculating and reporting the cost of regulations can mitigate the extent to which cost estimates are used out of context or inappropriately. For instance, standardized procedures for calculating the present and annualized value of costs prevents misleading characterizations to inflate costs (e.g. by using undiscounted costs over an extended horizon) or minimize them (e.g. by reporting only unit costs). Lastly, the evidence is clear that agencies often publish rules without quantified benefit estimates, so if there is a hurdle to climb associated with missing benefits estimates it must not be insurmountable.[45]

In contrast, CBA can elevate concerns and issues of people who are often left out of democratic decision-making. Two common cases reveal this point: the case of concentrated and diffuse impacts, and the case of the bootlegger and the Baptist. Federal regulations can often impose large and concentrated costs on a small constituency, while providing small and diffuse benefits to a large amount of people. In fact, it is likely that many people who receive these benefits don't even consciously recognize them. These rules include clean air rules that require large capital investments by industries but provide broadly diffuse benefits to many people who rarely observe the quality of the air they breathe; as well as driving time restrictions for truck drivers that result in small incremental reductions in risks to passenger vehicles. Indeed, the examples of concentrated costs and diffuse benefits are far

[44] Need cite here
[45] Cite report to congress on cost and benefits of fed regs

too numerous to list here and may even include most federal regulations. In these situations, the persons or entities that experience the concentrated costs of a regulation tend to be more vocal in a public decision-making process. They show up to public meetings and file public comments at a much greater rate than consumers of public roads or clean air. A complete CBA assigns a value to these diffuse benefits and ensures that the benefits to them are considered.

Occupational licensure can be an example of both concentrated benefits and diffuse costs (which is the inverse of what was examined above but is characterized by the same asymmetry in input and access) and the case of the bootlegger and the Baptist.[46] In the case of the bootlegger and the Baptist, two parties with separate and distinct interests combine their efforts in petitioning the government to bring about a shared interest. The bootlegger wishes to eliminate competition from legal competitors, and the Baptists seeks abolition for their moral and religious purposes. When they are successful, they both get what they wished for, but the consumer is made worse off via reduced competition, higher prices, lower quality, and/or misaligned preferences.[47] Occupational licensure often arises from petitions from the industry to be regulated that hopes to reduce competition and raise their prices. Often these petitions are joined by advocates for some public cause – frequently consumer protection or safety.[48] Meanwhile, the consumers that face higher prices due to licensing costs and reduced competition are rarely are even aware such a regulation is being considered. This is because the cost to the consumer is often small and diffuse, while the benefits to the regulated industry are large and concentrated. Again, a complete CBA would assign a value to these diffuse costs and ensure the concerns of the consumer are considered.]

Commented [RR(16]: Cite Krueger and other research here.

XI. Recommendations for Reform

The regulatory responsibilities of the CFPB are solemnly important and involve difficult tradeoffs. Its regulatory decisions influence some of the most important financial decisions consumers will make in their lives. Its fair lending rules address the painful legacy of redlining and segregation, as well as the ongoing menaces of racism and discrimination. Its regulations to protect consumers from fraud and loss of privacy can save consumer time, financial loss, and distress. On the other hand, regulations can impose costs that have the potential to raise the cost of credit, reduce access, and create unintended consequences with damaging results – and the consumers and families that live on the margins of these negative consequences may raise other distributional concerns that any prudent regulator must struggle with. Cost-benefit analysis is a tool for evaluating important decisions that involve difficult tradeoffs, and thus is an essential tool to be applied to the Bureau's regulatory decisions.

[Potential Recommendations

1. Adopt some principles of CBA that at minimum adhere to best practices in this chapter – develop them yourselves, or use OMB A-4.
2. Establish some form of regulatory review – OIRA, internal office at CFPB, some hybrid independent. Another option: OIRA review, but OIRA only issues public statements about analytical quality

[46] [HYPERLINK "http://pirate.shu.edu/~rotthoku/Liberty/On%20Bootleggers%20&%20Baptists.pdf"]
[47] Krueger discusses labor effects here [HYPERLINK "https://www.jstor.org/stable/pdf/10.1086/669060.pdf"] - want more on consumer costs
[48] Bootlegger and the baptist

3. Develop willingness to pay estimates for avoided consumer harms – including loss of privacy, fraud, discrimination?, financial crises?

Commented [RR(17]: If we recommend financial crises valuation, we should also discuss high-consequence, low-probability events and how CFPB will never have an effectiveness estimate for this.

ACUS Recommendations:

Recommendation: To the extent that independent regulatory agencies are required to do more economic analyses of their proposed and final rules, additional funding for those analyses should be provided

Recommendation: Independent regulatory agencies and OIRA should use whatever flexibilities exist within the Paperwork Reduction Act to expedite the collection of information needed in agencies' economic analyses.

Commented [RR(18]: Don't like this one! OMB significantly improves statistical collections.

Recommendation: When additional analytical expertise or experience is needed, independent regulatory agencies should consult with other agencies (e.g., through the Council of Independent Regulatory Agencies) and/or with OIRA (perhaps using memoranda of understanding to document the nature of the relationship).

Recommendation: To help ensure that regulatory analysis is used in decision making, independent regulatory agencies should make the analysis an early part of rule development.

Recommendation: Each independent regulatory agency should consider developing written economic analysis guidance tailored to its particular statutory and regulatory environment. That guidance should represent the agency's "best practices," and can help ensure that the agency's analyses are consistently conducted.

Recommendation: Independent regulatory agencies should include in the notice of proposed rulemaking and in the final rule a summary statement or table concisely showing the agencies' overall estimates of costs, benefits, and transfer payments.

Recommendation: Independent regulatory agencies' regulatory analyses should be as transparent and reproducible as possible. In particular, agencies should disclose how the analyses were conducted, post the analyses on the internet, and summarize the methods and results in the notice of proposed rulemaking

Recommendation: Independent regulatory agencies should quantify and monetize regulatory costs and benefits whenever possible. If costs or benefits cannot be quantified or monetized, agencies should explain why and take other actions to promote understanding of regulatory decision making (e.g., cost-effectiveness analysis or breakeven analysis).

Recommendation: Consistent with applicable laws, independent regulatory agencies' analyses should generally include both statutorily mandated requirements and those resulting from the agency's discretion. Showing both types of effects separately can improve transparency and allow the public to understand whether Congress or the agency is responsible for regulatory burden.

Recommendation: Independent regulatory agencies should voluntarily adopt the general principles for economic analysis contained in OMB Circular A-4 to structure their analyses: (1) identify the need for the regulation, (2) examine plausible alternative regulatory approaches, and (3) estimate the benefits and costs of those alternatives.]