Our Perspectives:
Commentary on the economy & regulatory policies affecting financial companies

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The CHOICE Act Would Fundamentally Alter Rulemaking Process for Federal Financial Regulators*

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Chairman Hensarling's omnibus financial reform bill, the CHOICE Act, would significantly alter the procedures governing the issuance of regulations by the federal financial regulators.

The agencies covered by the proposed changes are: the Federal Reserve Board, the Community Financial Opportunity Commission (which is the new name the CHOICE Act gives to the Consumer Financial Protection Bureau), the Commodities Futures Trading Commission, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the Comptroller of the Currency, the National Credit Union Administration, and the Securities and Exchange Commission.

The bill would require that each of these agencies —

- be governed by five-member boards, appointed by the President and approved by the Senate;
- be subject to the Congressional appropriations process;
- be prohibited from issuing rules that cannot pass a cost/benefit test;
- have major rules approved by Congress; and
- not be accorded deference by a court when the court is reviewing a rule issued by the regulators.

Presumably, these proposed changes are a reaction to the stream of regulations issued by federal financial regulators following passage of the Dodd-Frank Act. However, the changes raise a fundamental question about the role of Congress and its relationship with independent regulatory agencies. That is — What is the proper relationship between Congress and these independent agencies?

Each of these agencies was created by Congress and is accountable to Congress. They all must issue annual reports to Congress on their actions, and some are required by law to testify before Congress on

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a regular basis. Moreover, the regulations issued by these agencies must be based upon laws passed by Congress; otherwise such regulations are subject to reversal by the courts. Yet, there is a tension inherent in the relationship between Congress and these agencies. With the creation of these agencies Congress has, in effect, delegated some of its own authority to the agencies.

My own view is that the current relationship between the Congress and the agencies is out of balance, but the fault rests more with Congress than the agencies.

Congress could be more systematic in the exercise of its oversight function. Greater transparency into agency policies and practices can affect the manner in which an agency operates. Active Congressional oversight, however, requires Congress to dedicate sufficient resources to this task. Congress also could eliminate much of the overlap and conflict between agencies by rationalizing the agencies through consolidation.

As for the specific provisions in the CHOICE Act, I have a mixed reaction. I could argue the merits of a commission structure versus a single agency head either way. A commission may provide greater policy continuity over time, yet may lack a quorum to act on some occasions. Conversely, an agency led by a single individual may be more decisive, yet may be subject to specific biases held by that individual. A better approach would be to tailor the governance structure for each agency based upon its specific mission.

I have reservations with the call for placing all of these agencies under the appropriations process. The appropriations process is a key power of the Congress, but Congress must exercise this power carefully. For example, the Office of Federal Housing Enterprise Oversight (OFHEO), which was responsible for supervising Fannie Mae and Freddie Mac, was underfunded by Congress. We are still living with the consequences of the failure of those two enterprises. Regulatory agencies should have sufficient funding to perform the tasks assigned to them by Congress.

I also have reservations about the elimination of deference for these agencies when regulations are challenged in the courts. As a technical matter, deference applies only when a statute is ambiguous and an agency must interpret its meaning. Thus, more carefully drafted statutes would reduce the application of this doctrine. More fundamentally, these agencies have a level of expertise in the subject matter that cannot be duplicated by individual judges, and that expertise should be accorded some consideration.

On the other hand, I favor subjecting new regulations to a cost/benefit analysis. The benefits of a regulation should outweigh its costs. This requirement should be a factor considered in the issuance of a regulation, but not necessarily an absolute bar to the issuance of a regulation.

I also favor requiring Congressional approval for major regulations. This process would ensure that there is an alignment between the statute upon which the rule is based and the rule. Moreover, the current Congressional Review Act, which gives Congress a veto power over regulations, has proven to be fairly ineffective.

In sum, the CHOICE Act would rebalance the current relationship between Congress and the federal financial regulatory agencies. However, there are some alternative actions Congress could take that would be more effective, especially the allocation of sufficient resources to perform effective oversight of agency operations and activities.

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