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REGULATING IN THE DARK AND A POSTSCRIPT ASSESSMENT OF THE IRON LAW OF FINANCIAL REGULATION

Roberta Romano*

I. INTRODUCTION

How should one regulate in the midst of a financial crisis? This is a fundamental question for financial regulation, and it is not readily answerable, as the issues implicated are truly complex, if not intractable. Yet, foundational financial legislation tends to be enacted in a crisis setting, and over the past decade, when confronted with this question, the U.S. Congress has answered it reflexively by enacting legislation massively increasing the scope and scale of the regulation of business firms, and, especially, financial institutions and instruments, in a manner seemingly oblivious to the cost and consequences of its actions. 1 A simple, but telling, comparison of a commonly used measure of...
legislative complexity, a statute’s published length, conveys what Congress has wrought. The Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley” or “Sarbanes-Oxley Act”) is 66 pages long and the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank” or “Dodd-Frank Act”) is an astounding 848 pages, whereas the twentieth century foundational federal banking legislation, the Federal Reserve Act of 1913 and the Banking Act of 1933 (“Glass-Steagall Act”), are 31 and 37 pages, respectively.

In addressing how to regulate in a financial crisis, there is a related question: whether there is something different about financial institutions and markets, compared to other regulatory domains that makes regulation more challenging and crisis responses more prone to legislative failure? This Article addresses both questions by contrasting three recent examples of financial regulation which, I contend, are, in the main, misguided: (1) Sarbanes-Oxley, the response to the accounting scandals and bankruptcies of several large public corporations accompanied by a sharp stock market decline in the early 2000s; (2) Dodd-Frank, the response to the global financial crisis originating in the subprime mortgage crisis of the late 2000s; and (3) the Basel capital accord (“Basel accord”), through which central banks and banking regulators of the leading industrial nations have sought to harmonize international financial regulation since the late 1980s.

The answer to the two questions regarding crisis-generated financial regulation is, I believe, not really an issue of institutional competence, that is, of Congress’s lack of the requisite expertise to understand technically complicated financial products and markets. Financial regulators, in promulgating permutations of internationally harmonized capital requirements, have not fared much better in protecting the global financial system from catastrophic systemic risk, and, I would contend,

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6. Mark J. Perry, 2,319 Page Dodd-Frank Bill aka the “Lawyers’ and Consultants’ Full Employment Act of 2010,” CARPE DIEM (July 16, 2010, 7:50 AM), http://mjperry.blogspot.com/2010/07/dodd-frank-aka-lawyers-and-consultants.html. The Dodd-Frank figure is a single-spaced page count; a longer page count of 2319 pages, often publicized in the media and provided by Perry, references an official bill format that is double-spaced. Id. Perry’s counts for the two earlier statutes are undercounts in relation to the two newer statutes, because the page margins are narrower, but even if we were to adjust for a formatting difference, the point is still broadly accurate: Dodd-Frank dwarfs those pieces of legislation.
have, albeit unintentionally, contributed to it—though one would have a hard time figuring that out from media accounts.\(^7\)

Rather, the nub of the regulatory problem derives from the fact that financial firms operate in a dynamic environment in which there are many unknowns and unknowables, and state-of-the-art knowledge quickly obsolesces. In such a context, even the most informed regulatory response—which Congress’s reaction in the recent crises was not—will be prone to error, and is likely to produce backward-looking regulation that takes aim at yesterday’s perceived problem, rather than tomorrow’s, for regulators necessarily operate under considerable uncertainty and at a lag behind private actors. But, using market actors’ superior knowledge to inform regulation is not necessarily an effective solution, as indicated by the utter failure in the recent crisis of Basel II, which relied on banks’ internal risk ratings to measure capital requirements.\(^8\) This only further highlights the fluid, fast-moving, and uncertain environment in which financial institutions operate—even firms’ state-of-the-art risk-management techniques proved inadequate in the confluence of events that produced the global financial crisis.

In order to understand financial regulation undertaken in a crisis, we need to take account of, as Frank H. Knight put it, “human nature as we know it.”\(^9\) Human nature, in this context, is that legislators will find it impossible to not respond to a financial crisis by “doing something,” that is, by ratcheting up regulation, instead of waiting until a consensus understanding of what has occurred can be secured and a targeted solution then crafted, despite the considerable informational advantage from such an approach, which would, no doubt, improve the quality of decision-making. Compounding the problem, Congress tends not to move nimbly to rework financial legislation when it becomes widely acknowledged as flawed or seriously deficient. For instance, despite substantial consensus regarding the statutes’ problems, it took decades to repeal the Glass-Steagall Act’s separation of commercial and investment banking;\(^10\) eleven years to make relatively small revisions to accounting

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7. See Roberta Romano, *For Diversity in the International Regulation of Financial Institutions: Critiquing and Recalibrating the Basel Architecture*, 31 YALE J. ON REG. 1, 16-17 (2014) [hereinafter Romano, *For Diversity*].
8. See id. at 26 n.68.
9. FRANK H. KNIGHT, RISK, UNCERTAINTY AND PROFIT 270 (Univ. of Chi. 1971) (1921).
and bribery provisions of the Foreign Corrupt Practices Act of 1977;\(^\text{11}\) and eight years to amend the Sarbanes-Oxley Act to exempt only the smallest firms from the auditor attestation of internal controls’ effectiveness requirement.\(^\text{12}\)

This Article contends that the best means of responding to the typical pattern of financial regulation—legislating in a crisis atmosphere under conditions of substantial uncertainty followed by status quo stickiness—is to include as a matter of course in such legislation and regulation, sunset provisions requiring subsequent review and reconsideration, along with regulatory exemptive or waiver powers that create flexibility in implementation and encourage, where possible, small-scale, discrete experimentation to better inform and calibrate the regulatory apparatus.\(^\text{13}\) Such an approach, in my judgment, could mitigate, at least at the margin, errors, which invariably accompany financial legislation and rulemaking originating in a crisis atmosphere. Given the fragility of financial institutions and markets, and their centrality to economic growth and societal well-being, this is an area in which it is exceedingly important for legislators acting in a crisis with the best of intentions, to not make matters worse.

II. LEGISLATING FINANCIAL REGULATION IN TIMES OF CRISIS

Most significant financial regulation is adopted in response to financial crises.\(^\text{14}\) This pattern is consistent with the political science literature on policy agendas.\(^\text{15}\) According to that literature, issues move to the top of the legislative policy agenda in conjunction with “focusing events” and shifts in national mood, which render the public receptive to government action to redress a specific problem.\(^\text{16}\) This constellation of events opens a window in which individuals (referred to as “policy entrepreneurs”) present their preexisting preferred policies as “solutions”


\(^{12}\) 15 U.S.C. § 7262(c) (2010); see Romano, Does the Sarbanes-Oxley Act, supra note 11, at 239-42.

\(^{13}\) See infra Part III.A–B.

\(^{14}\) See STUART BANNER, ANGLO-AMERICAN SECURITIES REGULATION: CULTURAL AND POLITICAL ROOTS, 1690-1860, at 257 (1998); Romano, The Sarbanes-Oxley Act, supra note 1, at 1591-94.

\(^{15}\) See generally JOHN W. KINGDON, AGENDAS, ALTERNATIVES, AND PUBLIC POLICIES (2d ed. 2011).

\(^{16}\) Id. at 19-20.
to the problem at hand.\textsuperscript{17} A typical pattern in a financial crisis is a media clamor for action, reflecting, if not spurring, a similar popular demand, and as a crisis intensifies, an accompanying suggestion that government inaction is prolonging the pain and suffering.\textsuperscript{18} A risk averse legislator, whose objective is reelection, will, no doubt, conclude that there is a need to respond without seeking to ascertain, if it were even possible, whether such demands are media-driven or popularly shared, or, in fact, necessary to resolve the problem.

There is theoretical and empirical political science literature, based on agency models of political representation, supporting that hypothesized course of legislators' action: it indicates a close connection between an issue's salience in the media, election outcomes, and implementation of policy.\textsuperscript{19} For a legislator, "doing something" in response to a crisis is both easier to explain to anxious constituents and more likely to be positively reported in the media, as opposed to inaction, and therefore, it would appear to be a clear-cut superior route to reelection, which is the posited focus of legislators.

The heightened issue saliency, or in the vernacular "media frenzy," that accompanies the exigency of a financial crisis compels legislators not only to respond, but to respond quickly, even though they will be aware that they cannot possibly determine what would be the best policy to adopt in the circumstances; there would be considerable uncertainty in the first place about what has just occurred and why. Yet, without an understanding of the causes of a crisis, regulatory fixes, except by fortuity, are bound to be off the mark. Indeed, paralleling the political science literature's explanation of how policy proposals reach the congressional decision-making agenda, legislation adopted in financial crises typically contains recycled proposals fashioned to resolve quite

\textsuperscript{17} Id. at 20.

\textsuperscript{18} For example, a media frenzy over corporate accounting scandals, calling for a government response, was a key factor in the enactment of the Sarbanes-Oxley Act. See Romano, The Sarbanes-Oxley Act, supra note 1, at 1567-68. In the ongoing global financial crisis, media coverage, on a daily basis, includes repeated calls for a wide variety of government action to resolve the crisis. See id. at 1567.

\textsuperscript{19} The models suggest that by raising the salience of an issue, the media facilitates citizens' ability to monitor their elected representatives, and thereby bring about government adoption of policies the citizenry prefers. KINGDON, supra note 15, at 60-61, 65-66; Romano, Does the Sarbanes-Oxley Act, supra note 11, at 255-56. There are numerous empirical studies that support the theory, finding a link between policy, election outcomes, and media coverage. For a summary of the literature, see Romano, Does the Sarbanes-Oxley Act, supra note 11, at 255-58. Kingdon contends that rather than affecting a policy issue's movement onto a legislative agenda directly, the media exerts an indirect effect on policy, either by affecting public opinion on an issue and thereby influencing legislators, who pay attention to public opinion, or by magnifying movements that had already started elsewhere in the policy process. KINGDON, supra note 15, at 58-61.
unrelated problems, imagined or real, which policy entrepreneurs advance as ready-made solutions to immediate concerns, to a Congress in need of off-the-shelf proposals that can be enacted quickly.20 Given this reality, the repeated legislative failures that we have witnessed with regard to financial regulation should not be a surprising outcome.

Sarbanes-Oxley, for instance, is a case study of legislative failure. The statute’s highly-touted governance mandates of independent audit committees, restrictions on auditor services, and certifications of internal controls, essentially “off-the-rack” initiatives that had been advocated by policy entrepreneurs for some time, had minimal support in the academic literature publicly available both before and even more so after the legislation’s enactment, regarding their efficacy at improving performance or reducing audit failures.21 Not surprisingly, those ostensible reforms apparently had no bearing on financial institutions’ ability to withstand the 2007-2009 financial crisis.22 Yet, Sarbanes-Oxley’s governance mandates are still law, imposing considerable costs on firms,23 and it will take a herculean effort to repeal them given the organization of government.

In addition, a considerable portion of Dodd-Frank and, to a far lesser extent, Sarbanes-Oxley, consists of substantive rulemaking instructions to federal regulators.24 Dodd-Frank requires 400 final rulemakings and 87 studies,25 the vast majority of whose legislative deadlines will, no doubt, be missed.26 Indeed, at the statute’s one-year


26. The mind-boggling number of regulatory actions mandated by Dodd-Frank is so daunting
anniversary, 104 rulemaking deadlines had already been missed. This legislative strategy of delegation would appear, at first glance, to be attentive to the informational concern regarding decision-making in a crisis that I have mentioned, as the contemplated rulemaking process could generate, in theory, needed information to improve the quality of policy-making. Such an explanation works hand in glove with the conventional rationale for delegation and deference, that among government institutions, "agencies are the repositories of expert knowledge and experience."

However, it is difficult to posit seriously that in delegating so extensively, Congress was concerned with improving the information available for decision-making, given the statute's absurd demands on agencies, in both the plenitude of rulemakings and implementation timetable. An illustration, underscoring how agencies cannot be expected to accumulate, let alone assimilate, relevant, available information in the rulemaking process contemplated by the statute, involves the Securities and Exchange Commission's ("SEC") proxy access rule, which Dodd-Frank expressly authorized. The rule was struck down by the U.S. Court of Appeals for the D.C. Circuit in Business Roundtable v. SEC, as "arbitrary and capricious" for having been adopted with an inadequate cost-benefit analysis of its effect. Yet, the proxy access rule had been in the making for well over a decade, in contrast to the vast majority of the statute's required rulemakings.

A strand of the political science literature provides an alternative rationale for regulatory delegation, that it is a means by which legislators can avoid responsibility for adverse policy consequences. That

for a business to follow that law firms have introduced paying client services that track agencies' progress on the statute's required rulemakings and reports.

29. Congress frequently imposes unrealistic deadlines. There is no compelling explanation for the widespread use of this practice. One theory is that Congress, fully aware that its deadlines will not be met or will produce "incomplete or flawed" rules, uses deadlines as a mechanism of accountability, by providing a tactical advantage for constituents to challenge rulemaking in court, and to exert influence over the content of the rule. CORNELIUS M. KERWIN & SCOTT R. FURLONG, RULEMAKING: HOW GOVERNMENT AGENCIES WRITE LAW AND MAKE POLICY 226-27 (4th ed. 2011).
31. 647 F.3d 1144 (D.C. Cir. 2011).
32. Id. at 1148-51.
explanation offers a more compelling account of Dodd-Frank’s large-scale delegation strategy than the interpretation of a Congress earnestly seeking to cope with having to legislate under uncertainty by creating a window for additional information gathering and regulatory fine-tuning. Rather, in this scenario, delegation enables legislators to “do something” in a crisis, by passing “something” and thereby mollifying media and popular concerns, while at the same time shifting responsibility to an agency for potential policy failures, outcomes that legislators may well suspect to be possible, given the paucity or poor quality of information available concerning a crisis’s causes when the legislation is being crafted. If that possibility were to be realized, legislators, without missing a beat, would be positioned to criticize the agency, with the policy failure attributable to faulty implementation rather than an ill-conceived congressional mandate, and would have the further possibility to provide valuable constituent services, assisting firms and individuals to navigate difficulties created by administrative action. But if the policy implementation were to be successful, legislators could, of course, still take credit. In short, by means of delegation, legislators can have their cake and eat it too, so to speak.

From a legislator’s perspective, the delegation strategy would appear to have minimal cost, under both the benign and more manipulative explanations. But, many members of the business and academic communities view Dodd-Frank as having exacerbated the severe economic downturn that has followed the global financial crisis. As banks are spending in the billions of dollars on Dodd-Frank compliance, the statute quite plausibly adversely affects the price or availability of credit. But equally, if not more important, is the increase in business uncertainty generated by the immense number of required rulemakings. Until proposed, let alone promulgated, regulatory compliance costs cannot be estimated with any confidence, which deters investment. Moreover, because Dodd-Frank was enacted on a party line vote, in contrast to the bipartisan, unanimous, or near unanimous support crisis-driven financial legislation has typically received, an additional source of uncertainty affecting business investment is the possibility that, in the near future, control of Congress and the presidency could shift

34. Id. at 47, 53.
before all of the required rulemakings are completed and dramatically alter the implementation of the law.

The full cost of Dodd-Frank is rendered further opaque by regulators finding, as they attempt to implement the statute, that Dodd-Frank’s mandates pose unanticipated operational issues that create new risks, complicating implementation. For example, in order to decrease the risk of trading customized off-exchange derivative securities, Congress required derivative trades, wherever possible, to be cleared on exchanges. 37 Yet, this requirement, it turns out, increases risk for pension funds and asset managers, due to the way exchanges handle margin collateral, and changing exchange brokerage arrangements to reduce the risk significantly increases costs. 38

In short, by requiring agencies to enact a multitude of rules often devoid of guidance and consideration of how the rules would interact with institutional practice, Dodd-Frank’s delegation strategy has created a minefield for business planning. Moreover, adding insult to injury, Dodd-Frank does not even attempt to address the financial crisis’s ground zero, Fannie Mae and Freddie Mac, the government-sponsored enterprises (“GSE”) that back mortgages, which are estimated to require billions of dollars in taxpayer support by the end of the decade. 39 Perhaps that omission should not be surprising: throughout their pre-bailout existence, the GSEs have been considered “too influential and too politically connected to be regulated,” with “each successive presidential administration turn[ing] a blind eye” to their unconstrained, highly-leveraged and increasingly risky lending activities. 40

But, there are also Dodd-Frank delegations to agencies (along with statutory provisions that require agency action without discretion in implementation) that have at least some connection to the financial crisis, those explicitly directed at reducing systemic risk, such as the creation of a Financial Stability Oversight Council, and regulatory directives on minimum leverage and risk-based capital requirements. 41

40. ACHARYA ET AL., supra note 39, at 22, 28.
This suggests that a helpful comparative benchmark would be the efforts of the international financial regulatory community to reduce systemic risk by harmonizing capital requirements in the Basel accords. Given the greater technical expertise of regulatory agencies compared to Congress, if institutional competence were to explain flaws in legislated financial regulation, then financial regulators would be expected to do a better job than Congress.

Moreover, the negotiations of financial regulators over the Basel accords do not receive as intensive media coverage, and accompanying popular attention, pressing for immediate action, as does congressional deliberation in times of financial crisis. Basel II, for example, whose initiation was in 1998, Daniel Tarullo contends, "was not impelled by a crisis specific to banks in member countries," and was not approved until 2004. But, even Basel initiatives motivated by crises took years to bring negotiations to conclusion, in contrast to Congress's relatively quick crisis-response legislative output. And the notable exception, the relatively quick approval of Basel III in 2010, within two years of the onset of the global financial crisis, contains an extended timetable for implementation and observational reassessment, which, for some key provisions, ranges from five to ten years. Therefore, in further contrast with Congress, international regulators have more time to obtain additional information concerning a crisis's causes and consequences, and to refine their regulatory responses.

Despite the seemingly decisive differences between financial regulation initiated by Congress and central bankers, which would suggest that the latter might be better positioned to get things right, the ongoing financial crisis suggests, to the contrary, that such an expectation would be misplaced. In fact, the harmonized international financial regulation produced by the Basel accords contributed to the ongoing global financial crisis, perversely increasing systemic risk, by encouraging banks to hold, in levered concentrations, the assets at the epicenter of the ongoing crisis, residential mortgages and residential

43. Id. at 121-22. Although some might contend that Basel II was initiated in response to the Asian financial crisis of 1997, Tarullo maintains that was not the causal initiating factor because Basel members' banks were not seriously impacted by that crisis. Id. at 90, 91 & n.9.
44. See id. at 91 n.9. For example, Tarullo notes that Basel I, which was adopted in 1988, was set in motion as a response to the Latin American debt crisis of the early 1980s. Id.
mortgage-backed securities, and sovereign debt. Because the accords were global, banks worldwide were incentivized to follow broadly similar business strategies, so when the value of the mortgage-related assets preferred by Basel collapsed, it led to a global financial crisis, rather than one more localized where the subprime mortgage crisis originated. Basel's flawed regulatory architecture is also implicated in the ongoing Eurozone sovereign debt crisis, as sovereign bonds have an even greater preference in the Basel risk-weighted capital schema than residential mortgages and mortgage-backed securities.

Why would financial regulation produced by central bankers and banking regulators of the most developed economies, with sophisticated technical knowledge and resources at their disposal, and without media demands for quick action, end up so profoundly mistaken? One possible answer is bad luck. Although there may well have been some bad luck, the answer seems to me to be more a function of dynamic uncertainty in financial markets, and explicit political considerations affecting the Basel accords. Dynamic uncertainty, a term used in the literature on terrorism, refers to the fact that the action of the regulated in response to regulation alters risk in unanticipated ways that evolve nonlinearly, rendering it extremely difficult to predict the impact of regulation over time.

The truth is that the current state of knowledge does not permit us to predict, with any satisfactory degree of confidence, what the optimal capital requirements or other regulatory policies are to reduce systemic risk, or, indeed, what future categories of activities or institutions might generate systemic risk. Regulations that are appropriate when initiated can rapidly become inappropriate as a financial system's business, legal, and technological conditions change. Moreover, institutions and individuals adapt their behavior in response to regulation, and their reactions change over time, interacting with the regulatory environment in nonlinear ways, greatly complicating analysis.

Notwithstanding considerable advances in knowledge, the fast-moving and constantly changing dynamic of financial markets also

46. Jeffrey Friedman & Wladimir Kraus, Engineering the Financial Crisis: Systemic Risk and the Failure of Regulation 62-67 (2011); Romano, For Diversity, supra note 7, at 24-25, 27.

renders it improbable that any future state of knowledge would enable us to make predictions with confidence. Risk management in today’s context of large and interconnected financial institutions and complex financial instruments must grapple with unknown and unknowable risks, and not simply known risks. 48 Yet, the Basel approach has focused the attention of the private sector, regulators, and academic researchers on knowns, that is, on measuring capital adequacy through statistical probabilities of risks, disregarding the equal, if not more important, need to create internal control and regulatory systems that emphasize adaptability to the challenge of unknown and unknowable risks. 49

Moreover, knowledge of past relations across asset returns, used in risk management, can be misleading, for in times of financial stress, asset correlations not only change, 50 but also increase significantly. 51 In such an environment, regulators are bound to make mistakes, and Basel’s global harmonization template is poorly suited to catch them, as it neither adapts readily to change, nor fosters diversity, both of which are strategies that increase system survivability; 52 rather, it may well increase the likelihood of systemic failure. 53

But, the failure of the Basel accords is not solely due to inappropriateness of a top-down harmonized regulatory approach for the dynamic uncertainty of financial markets; the accords are also informed by political judgments, which have had adverse consequences for financial system stability. 54 The most critical terms in the accord, the definition of core (tier one) capital and the choice of risk weights, have been a subject of repeated political log-rolling. A case in point is the tripartite agreement devised under Basel I, in which Japanese negotiators obtained their desired (core) capital treatment for deferred tax assets; U.S. negotiators for mortgage servicing rights; and European (French and German) negotiators for minority interests in other financial institutions; a logroll carried forward in Basel III with all three assets

49. See id. at 5.
50. Id. at 25.
53. See RICHARD F. HERRING & ROBERT E. LITAN, FINANCIAL REGULATION IN THE GLOBAL ECONOMY 134-35 (1995) (arguing that the Basel protocol is failing partially because “[r]egulators are always trying to catch up with the rapidly changing market practices”).
54. See TARULLO, supra note 42, at 87.
continuing to qualify as tier one capital, albeit limited to the precise same ten percent. There is no economic or prudential justification for the three asset categories to be treated equivalently, let alone characterized as equity capital. And, as mentioned earlier, favorable Basel risk weights for residential mortgages are illustrations of political considerations influencing risk weight assignments so as to be in conformance with, and furtherance of, national policies.

By tending to enact comprehensive financial legislation only in reaction to an immediate financial crisis, Congress acts most swiftly precisely when greater deliberateness is called for, given the paucity of information available to produce a high quality decision. The Basel regulatory architecture premised on global harmonization is just as poorly suited for the task, as it is not designed for generating information concerning what new risks might require regulation, let alone what regulation would be best suited for specific risks. Nor is it nimble enough to adapt and change course rapidly to scotch looming problems, when information becomes available that a regulatory approach is likely to be mistaken or no longer appropriate. Although Congress is not about to restrain itself from acting in a crisis, nor are Basel committee members about to abandon their commitment to harmonization any time soon, the unintended consequences likely to accompany their decisions can, in my judgment, be mitigated by deploying systematically procedural mechanisms that require the revisiting of enactments and by fostering experimentation in regulatory approach.

III. IMPROVING THE QUALITY OF CRISIS-BASED FINANCIAL REGULATION

There are two key components that should be included in financial regulation to mitigate the effect of legislative and regulatory failure: (1) a sunset requirement that regulation be reviewed and reconsidered within a fixed period after enactment (e.g., five to six years) to stay on the books; and (2) a structure that is hospitable to regulatory experimentation wherever possible. By permitting legislators and regulators to incorporate new information into the decision-making process, and simultaneously increasing the likelihood that new information will be generated from the regulatory variety resulting from

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55. See Basel Comm. on Banking Supervision, supra note 45, at 26.
56. E.g., Mathias Dewatripont et al., Balancing the Banks: Global Lessons from the Financial Crisis 30 (Keith Tribe trans., 2010).
experimentation, the quality of decision-making has a better chance of being improved.

A. Sunsetting Financial Regulation

Sunsetting—providing that a statute expires on a specified date unless reenacted—is a time-honored legislative tool.\textsuperscript{57} It has been used by Congress and state legislatures since the nation’s founding, although its use as a lawmaking strategy has ebbed and flowed over time. For instance, in the late 1970s, sunset legislation rapidly coursed through the states, with thirty-five legislatures enacting sunset laws to review administrative agencies, widely perceived to be ineffective and wasteful.\textsuperscript{58} At the same time, Congress considered, but did not enact, a broad sunset statute, yet it still followed the trend in sunsetting the newly created Commodity Futures Trading Commission (“CFTC”) in the Commodity Futures Trading Commission Act of 1974.\textsuperscript{59}

By 1990, enthusiasm for administrative agency sunsetting waned, given the time and cost of reviews, but over twenty states still have some form of active sunset review;\textsuperscript{60} in recent years, as states’ fiscal situations have deteriorated, states have once again adopted or reinvigorated the process.\textsuperscript{61} Articles discussing the effectiveness of state sunset reviews in their heyday in the 1970s indicate that they were on balance successful, resulting in the termination of agencies (although no major entities were terminated), and improvements in agency operations, even in states that discontinued sunset reviews.\textsuperscript{62}

\textsuperscript{57} For an overview of the use of temporary legislation, of which sunset statutes are one variety, see Jacob E. Gersen, Temporary Legislation, 74 U. CHI. L. REV. 247, 251 (2007). The U.S. income tax code is, in fact, rife with time-delimited provisions, often referred to as “extenders” (because they typically are automatically rolled over), rather than “sunsets.” For a critical appraisal of the political dynamics of tax sunsets, which, being related to evasion of restrictive budgetary rules, is orthogonal to the issues concerning the use of sunsets in this Article’s context of crisis-driven legislation, see Rebecca M. Kysar, The Sun also Rises: The Political Economy of Sunset Provisions in the Tax Code, 40 GA. L. REV. 335, 338, 342 (2006).


\textsuperscript{61} See Waller, supra note 60, at 47. See generally SARAH WEAVER, INTRODUCTION TO SUNSET REVIEW, JOINT SUNSET REVIEW COMMITTEE (2011), available at http://assembly.ca.gov/search?qs=weaver (outlining the experience of California).

Sunsetting is particularly well-suited for crisis-driven financial legislation. Of the rationales for adopting a sunsetting strategy, the key justification in the financial regulatory domain is that sunsetting mitigates the predicament of legislating with minimal information, and therefore, running the risk of getting things seriously and, for all practical purposes, permanently wrong. Congress can, of course, in principle, modify crisis legislation that turns out to be misplaced. But the U.S. political system’s organizing principles of separation of powers and checks and balances create numerous veto points throughout the legislative process (e.g., approval of both chambers, then Presidential approval, or approval by a supermajority of both chambers) that make repealing a statute extremely arduous. Sunsetting loosens the institutional stickiness of the status quo by putting a statute in play, with a need for affirmative legislative action at a specific date to remain in effect.

But, more important in the financial regulation context, sunsetting sets in motion a process by which post-enactment information can be incorporated into the regulatory regime. For instance, by the time of a statute’s sunset review, several years after enactment, there should be a better understanding of the causes of the crisis that the legislation sought to address, along with knowledge of the enacted legislation’s consequences, information indispensable for getting regulation right, but unavailable when a crisis necessitates a response. In addition to permitting a more clear-eyed assessment, with the benefit of hindsight, of the crisis-enacted regulation, economic and technological conditions may have dramatically changed in the interim, with financial innovation occurring apace, and that information can also be taken advantage of in

63. Romano, The Sarbanes-Oxley Act, supra note 1, at 1595. John Coffee questions the intellectual consistency of my critique of Sarbanes-Oxley and my advocacy of sunset as a means of mitigating the adverse consequences of emergency legislation, quoting another article criticizing my advocacy of sunset review for offering "no empirical evidence that sunshine provisions provide any benefits on balance," and commenting that “[i]t seems ironically inconsistent for Professor Romano to criticize Congress for enacting many of SOX’s provisions without (in her view) adequate empirical support and then in turn propose a legislative remedy of her own (a mandatory sunset rule) that also has no empirical support.” John C. Coffee, Jr., The Political Economy of Dodd-Frank: Why Financial Reform Tends to Be Frustrated and Systemic Risk Perpetuated, 97 CORNELL L. REV. 1019, 1033 n.53 (2012) [hereinafter Coffee, The Political Economy]. Coffee and the authors to whom he refers, Robert A. Prentice and David B. Spence, ignore the long and well-established U.S. experience with sunset legislation, as an instrument in legislators’ conventional toolkit, as well as the literature evaluating the results. Although empirical research on sunset reviews is limited, those studies that do exist, noted in the text, provide positive, albeit mostly qualitative, assessments. Id. My response to the Prentice and Spence article that Coffee cites can be found at Romano, Does the Sarbanes-Oxley Act, supra note 11, at 260 n.127.
the legislative “second look,” for the most appropriate regulatory responses will undoubtedly have shifted, as well.

John Coffee critiques sunsetting crisis-driven financial regulation on two principal grounds. First, he maintains that the review process will be captured by financial institutions and produce outcomes at odds with the public interest that he contends characterizes emergency legislation. Second, he asserts that flaws in crisis legislation go away

64. Coffee, The Political Economy, supra note 63, at 1026. Coffee sweepingly seeks to dismiss the scholarship with which he disagrees by engaging in name calling, referring to Steve Bainbridge, Larry Ribstein, and me as “the ‘Tea Party Caucus’ of corporate and securities law professors” (a claim that would have been humorous had it not been said earnestly), and “conservative critics of securities regulation,” (a claim, at least in my case, that would be accurate if he had dropped the adjective), and by further referring to Bainbridge and Ribstein, as “[m]y loyal allies.” Id. at 1024 (internal citations omitted). One should at least get labels right when attempting to disparage intellectual foes. In point of fact, in the American political tradition and academic literature, advocacy of sunsetting and, in particular, as a means to implement cost-effective regulation, has historically cut across political party lines. Kearney, supra note 60, at 49. It has had a distinguished liberal pedigree, having been advocated by, among others, President Jimmy Carter, Senator Edward Kennedy, political scientist Theodore Lowi, and the “good government” advocacy organization Common Cause. STEPHEN BREYER, REGULATION AND ITS REFORM 366 (1982); Kysar, supra note 57, at 353. A more recent instance is the bipartisan support of sunset provisions in the USA PATRIOT Act. Robert O’Harrow, Jr., Six Weeks in Autumn, WASH. POST MAG., Oct. 27, 2002, at 17, 20. Moreover, the aim of sunsetting is to eliminate regulations that are either ineffective, lack intelligence, or have had perverse consequences—not all regulation, as Coffee suggests with his comment: “Such an outcome [a sunset review of the federal securities laws undertaken in the 1930s that would result in their elimination in entirety] seems sensible only if one believes, as Professor Romano may, that markets need little regulation, and regulatory interventions, if any, should be short-lived, disappearing like snowflakes in the sun.” Coffee, The Political Economy, supra note 63, at 1024. The historical experience with sunsetting demonstrates that Coffee misunderstands the legislative technique: states did not terminate all or even most administrative agencies subject to their sunset reviews in the 1970s, as opposed to specific programs, practices, and entities thought not to be cost-effective. See, e.g., Kearney, supra note 60, at 52-53. Nor has Congress eliminated the CFTC, which, created as a sunset agency, comes up for periodic reconsideration and renewal. Coffee further claims that I (and others who have similarly critiqued Sarbanes-Oxley) see democratic politics as “dismaying, dangerous, and need[ing] to be discouraged.” Coffee, The Political Economy, supra note 63, at 1022. He has it precisely backwards. Advocacy of sunset review in this context—emergency financial legislation—perfects democratic politics by seeking to have elected representatives—legislators—make decisions. It is Coffee who would leave the revision of flawed crisis-driven legislation or its inept implementation to unelected functionaries with their own private and institutional agendas, whose decisions are often beyond public scrutiny or, when visible, so technical as to be beyond public comprehension. Id. at 1035-36. Coffee’s critique, in the very same paper, of regulators’ implementation of Dodd-Frank’s executive compensation rules, among others, for eviscerating Congress’s objectives makes my point. Id. at 1067-68, 1071-72.

65. Coffee, The Political Economy, supra note 63, at 1030. Coffee asserts that his argument about the administrative process’s undoing or “water[ing] down” of crisis-driven financial legislation does not assume that regulators are captured. See, e.g., id. at 1028, 1081. But, much like Hamlet’s mother and the player queen, despite his protestations, Coffee’s analysis bespeaks otherwise. For example, he states that “financial regulators are often so closely intertwined with those that they regulate that they respond in an equivocal and even timid fashion.” Id. at 1080. By
over time because the administrative process through which the legislation is implemented will eventually revise the more problematic parts.\textsuperscript{66} Although the significance Coffee draws from this second claim with regard to sunset review is not made explicit, he would appear to be arguing that over time, bad laws can be undone by administrative agency action.\textsuperscript{67} Whatever the intended interpretation, his bottom line is that the "greater danger" is that too little or no regulatory "reform" will be enacted in a crisis, because "overbroad regulation is usually repealed or curtailed relatively quickly, without the need for mandatory sunsets," and that the "forces of inertia will veto or block all change."\textsuperscript{68}

Coffee's first claim regarding the legislative process is, however, mistaken in depicting crisis-driven financial legislation as a triumph of a dispersed public interest, unrepresented in times of normal politics, against the concentrated interest of business.\textsuperscript{69} There are, in fact, highly organized and powerful interest groups on both sides of financial regulation issues, and solutions appearing in crisis-driven legislation are often policies that a range of those groups have advocated, sometimes for an extended period of time,\textsuperscript{70} and not simply the work of "champions" of investors whose voices would never be heard by Congress or regulators in the absence of a crisis, as Coffee contends.\textsuperscript{71}

In particular, the counterpart in the political arena of Coffee's "concentrated" business interest is certainly not a dispersed investor public in need of a crisis-induced "political entrepreneur" to be represented against business, but rather, well-funded and politically
influential labor unions, public pension funds, and the plaintiff's bar, along with the corporate governance cottage industry and a variety of trade groups, whose leadership regularly is called to testify in congressional hearings. Moreover, these groups are full-time political players, and do not just spontaneously emerge as a counterweight to business interests solely in a crisis, as Coffee would have it. Such groups are equally active in the normal politics of the administrative process, which Coffee contrarily characterizes as the domain of one concentrated interest—"business." Although the objectives of those groups in relation to the public good or the interests of individual investors can be deeply problematic, their prominent presence in the policy process, in crisis and non-crisis times, is an incontrovertible fact and it tends to counterbalance business influence.

In addition, business is not a monolithic interest group, as Coffee's invocation of Mancur Olson suggests. Rather, business firms are quite often divided on legislative issues, including those related to financial regulation. For example, large and small companies split over supporting Sarbanes-Oxley, and the securities, futures, and banking sectors of the financial industry were in continual conflict over the regulation of derivatives in the 1990s. Of course, even if businesses were in unison on a specific proposal, it would be incorrect to assume, as does Coffee, that simply because businesses support a particular policy, it cannot be good public policy. To the contrary, a comprehensive study of business lobbying found that when a united business front "wins" in a

72. Coffee dismisses the political significance of public pension funds because they do not make campaign contributions. Id. at 1031. But, that misses the mark: public pension funds are often led by prominent state political figures whose positions and contacts provide considerable clout and a bully pulpit that can further political ambitions. See Roberta Romano, Public Pension Fund Activism in Corporate Governance Reconsidered, 93 COLUM. L. REV. 795, 800, 801 & n.20 (1993) [hereinafter Romano, Public Pension Fund].

73. See Romano, The Sarbanes-Oxley Act, supra note 1, at 1569-71.
77. See Romano, Does the Sarbanes-Oxley Act, supra note 1, at 238-39.
deliberative process over controversial regulation it is because the public supports business’s policy position, rather than business’s having “captured” legislators.  

Coffee’s second contention, that problematic components of crisis-driven financial legislation are revised over time through the administrative process, is inconsistent with his first claim, that the administrative process is captured by business. An administrative process that is properly revising problematic legislation would not simultaneously be eviscerating legislation in the “public” interest. Coffee cannot have it both ways. Moreover, the example Coffee provides, of “quick” regulatory adjustment to the problematic internal controls provision of Sarbanes-Oxley, proves the precise opposite of what he claims. It took eight years and an act of Congress to undo costly

79. MARK A. SMITH, AMERICAN BUSINESS AND POLITICAL POWER: PUBLIC OPINION, ELECTIONS, AND DEMOCRACY 167 (2000). Coffee cites a law review article in support of his view that business dominates politics and for the proposition that businesses outspends unions on lobbying, and is apparently unaware of the comprehensive research on lobbying by Baumgartner et al., which details the offsetting lobbying resources that coalesce against large organized lobbying expenditures by business, and the data indicating that resources spent do not explain lobbying success. FRANK R. BAUMGARTNER ET AL., LOBBYING AND POLICY CHANGE: WHO WINS, WHO LOSES, AND WHY 194, 202-03 (2009); Coffee, The Political Economy, supra note 63, at 1031 nn.46-48 (citing Dorie Apollonio et al., Access and Lobbying: Looking Beyond the Corruption Paradigm, 36 HASTINGS CONST. L.Q. 13, 47, 50 tbl.2 (2008)). The error in relying on the article Coffee cites is that Apollonio et al. use aggregate lobbying expenditures, without examining how the funds were allocated across issues, to ascertain how they line up; not only are businesses affected by many more issues than unions because there are many different business sectors affected by different laws, but also, on many issues businesses and unions are not at odds. Apollonio et al., supra, at 36, 38 & n.142, 50. More important, contrary to the article’s correlative claim that businesses outspend unions in campaign contributions, and Coffee’s contention that unions are outspent by banks, the Center for Responsive Politics, which tabulates campaign contributions, has constructed a list of the “all-time” top campaign contributors over 1989 to 2014. Cf. for Responsive Politics, Heavy Hitters: Top All-Time Donors, 1989-2014, OPENSECRETS (Dec. 16, 2013), http://www.opensecrets.org/orgs/list.php. Of the top fifteen donors, nine are unions, one is the trial bar, one is the national realtors’ trade association, and the number one is ActBlue, a collector of funds for Democratic Party candidates, while only three are corporations (AT&T, Goldman Sachs, and Citigroup). Id. Another three unions, but no corporations or corporate trade groups, are in the top twenty on the list. Id. And of course, these contributions do not include the kind campaign contributions that unions, not businesses, make in the form of “get out the vote” and other candidate support efforts. Most important, Coffee’s position regarding the import of business lobbying is incoherent. He is contending—in favor of the “democratic” nature of emergency legislation over a more deliberative legislative process as would be occasioned by sunset review—that business’ lobbying of agencies post-crisis enables them to dominate the rulemaking process, but a few pages later, in arguing against sunsetting and advocating that any reconsideration of crisis-driven legislation should be left to agencies, he buttresses his position against sunsetting by asserting that the only reason to support sunsetting would be a belief that an agency is “captured.” Coffee, The Political Economy, supra note 63, at 1035.

81. See id. at 1031 & nn.46-48.
regulation by a bit, and much of the agency action that was directed at the problem in the intervening years was not self-correcting administrative action, as Coffee contends, but rather, undertaken in response to action, or the threat of action, by Congress. 82

Finally, and most important, both of Coffee's concerns that motivate his objection to sunsetting, contrary to his contention, would, in fact, be addressed, not exacerbated, by a sunset requirement. If his first objection to sunsetting were correct, and the post-crisis administrative implementation process is captured by business interests that undo public-regarding legislation, then sunsetting should, all the more, be endorsed. Sunset review entails a far more transparent public process than administrative action, with congressional hearings that would attract media attention, rendering it more difficult for any one organized interest group or groups to control the process. And, if Coffee's second objection were accurate, and the post-crisis administrative process is one in which all or nearly all statutory flaws are eventually ironed out, as he claims, 83 then sunset review would reduce the cost of such errors by further facilitating and accelerating the revision process.

But to be effective, it is important that the sunsetting process be crafted in light of the states' experiences with what works. To guide the collection and analysis of information in a sunset review, and hence the reassessment of whether legislation should be retained or revised, evaluative criteria for the sunset review, and not simply an expiration

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82. See Romano, Does the Sarbanes-Oxley Act, supra note 11, at 276-77, 288-89. Coffee contends that the problem with the internal controls provision was not the fault of Congress and the crisis-based haste in which the statute was crafted, but rather, due to the Public Company Accounting Oversight Board's ("PCAOB") implementation. See Coffee, The Political Economy, supra note 63, at 1038. As earlier discussed in the text, emergency legislation often adopts a delegation strategy in order to deflect blame for the consequences of a poorly-thought out legislative strategy by placing it on the implementing agency, as Coffee has done. See supra Part II. In making such a distinction, Coffee misunderstands the scope and intention of sunset review of crisis-driven legislation: it encompasses problems in regulatory implementation as well as in statutory drafting. See supra notes 57-81. Moreover, what Coffee regards as a problem of implementation cannot be readily separated from the legislative process as he attempts to do, for the difficulties in implementation are, in fact, a product of hastily drafted crisis-driven legislation that encourages the use of readily available solutions, which, upon more sober reflection, would be recognized as inapt. The internal controls provision is an illustration of this phenomenon. It was simply lifted from a provision in the Federal Deposit Insurance Corporation Improvement Act of 1991 requiring banks to submit reports on their internal controls, with auditor attestation, to banking regulators as part of the bank examination process. See COMM. ON BANKING, HOUSING & URBAN AFFAIRS, PUBLIC COMPANY ACCOUNTING REFORM AND INVESTOR PROTECTION ACT OF 2002, S. REP. No. 107-205, at 31 (2002). Unfortunately, no one attempted to consider, let alone analyze, whether such a template could costlessly be imposed on all sizes and types of public companies as part of the public audit process.

83. See Coffee, The Political Economy, supra note 63, at 1026.
date, need to be specified in the statute responding to the crisis. Otherwise, a review will lack focus and may become a pro forma process, as legislators will often have more immediate concerns that they wish to pursue rather than undertake a serious reassessment, especially if, as is probable, constituent concerns in a crisis that motivated the statute in the first place have drifted to new matters. The evaluative criteria will, of course, vary depending on the specific legislation.

Taking Dodd-Frank as an illustration, a crisis-specific evaluative criterion would be whether implemented regulations have had a positive (or at least non-negative) effect on financial system stability (banks’ safety and soundness), along with a more general criterion of whether the benefits (e.g., the increase in bank soundness) outweigh the costs. An example of the latter might be whether there has been an increase in the cost of credit to small businesses, which, because they are more reliant on bank financing than large corporations that can access public capital markets, are considered the parties most at risk from a reduction in bank lending that the statute may cause. Estimation of the economic effect of financial regulation is a quite feasible, albeit most certainly imperfect, endeavor, as academics and bank regulators’ technical staff routinely analyze the impact of regulatory changes on individual banks and the economy. In any event, such a calculation is not only simply better than operating in total darkness, but essential for attempting to evaluate what crisis-driven regulation has wrought.

The availability of new information at the time a second vote on a statute is required for it to remain in force does not guarantee that legislators will engage in a serious reassessment, rather than a pro forma review, of course. To increase the likelihood that new information will be conscientiously acted upon, two other components should be included in a sunset provision, in addition to an expiration date and evaluative criteria: establishment of a sunset review panel to perform the review along with a timetable for action. A sunset review panel should be tasked to recommend what action—repeal, reenactment, or revision—Congress should take, and a timetable should set out the interval in which a panel recommendation would be considered by the House of Representatives (“House”) and Senate committees with jurisdiction over the legislation, after which the panel’s recommendation would be

84. See Davis, supra note 58, at 396-98.
85. BREYER, supra note 64, at 365-66.
86. Id. at 366-67.
automatically discharged as a bill for a floor vote if the committees do not themselves bring it, or an amended version, to the floor.87

The sunset review panel should consist of independent experts, who are neither government employees nor officials, and be empowered to obtain information from relevant regulatory agencies and firms to undertake its review. The advantage of independent experts is that they tend to self-identify more strongly with professional norms and are more concerned about reputational damage if peers perceive them to be doing the bidding of interest groups or party politics than are government employees who are in a hierarchical chain of command. For the review panel to be both politically accountable and independent, it should be appointed by Congress and the President, paralleling the practice used for creating blue ribbon government panels. Although Congress could establish a standing blue ribbon review panel, which would reduce the cost to future Congresses of forming a panel, reviews would be more effective if undertaken by panels created specifically for the legislation to be evaluated, as the relevant expertise is likely to vary with a statute’s focus. For example, expertise in macroeconomics would be pertinent for reviewing much of Dodd-Frank, but not Sarbanes-Oxley.

To ensure that the sunset process is meaningful, the authorizing legislation would need to include adequate funding for a review. Budgets of prior congressionally-appointed blue ribbon investigatory panels could be used to provide guidance. Given budgetary concerns, Congress could impose a fee on the relevant sector affected by the legislation to cover a review panel’s operating cost. It could also mandate that governmental research organizations, such as the Congressional Research Service or General Accountability Office, and the relevant regulatory agencies, provide evaluations of the sunsetting regulations to the panel, for use in its review. But that would probably not substantially reduce the expense of a sunset review, as the panel would likely want to conduct its own evaluation de novo.

87. Id. I am advocating a modified version of a proposal of Justice (then-Professor) Breyer for review of federal regulatory programs for waste and inefficiency. See id. Breyer rejected a sunset approach because he was concerned that a congressional minority could “destroy” an existing program by preventing a bill from coming out of a committee or by filibustering or otherwise blocking a floor vote to reapprove a majority-supported program. Id. His proposal, therefore, would continue a program were Congress not to adopt a recommendation. See id. Breyer’s proposed automatic discharge eliminates the issue of committee blocking, but not, of course, minority blocking on the floor. See id. But, sunset could be retained and the latter issue eliminated with a rule for sunset review analogous to the reconciliation process applicable to budget legislation, which limits debate and bypasses filibusters.
The rationale for this review mechanism—an expert panel and a timetable—is that the threat of a required floor vote on a recommendation made by outside experts would compel a higher quality reassessment of a statute by all concerned, and, in particular, by congressional committee members who know they cannot prevent a vote on a recommendation they might otherwise be able to oppose merely by inaction. It should also better incentivize review panel members, as they would know that a floor vote on their work product is assured. The use of a review panel has a further benefit of reducing the time required by legislators and their staff to engage in a sunset review, as the panel would collect data and perform the analyses necessary for the legislature's reassessment. It would thereby mitigate a key operational problem experienced by states in their 1970s sunset reviews that led several states to abandon the procedure: legislators, particularly in states where they were part-time, did not have the time or resources to engage in the demanding process of reviewing numerous state agencies.\(^{89}\)

A variant of legislative sunset, which would reduce even further demands placed on Congress of a required review, would be to impose the sunset review on agencies implementing the regulation. In this alternative, crisis-driven financial legislation would mandate agency reassessment of regulations implemented under the statute, with an automatic expiration in five years, unless they are found to be cost-effective, and with the technical analysis undertaken by independent experts, rather than agency staff, to minimize potential bias from an agency's being too closely involved in the rules it administers to evaluate them objectively.\(^{89}\) Further, to guard against an agency's inherent bias in interpreting the independent experts' analysis in support of the regulatory status quo or its agenda, a congressional vote on the agency's determination should be required in an administrative sunset review regime.

The availability of sunsetting as a well-known technique in the congressional playbook suggests a puzzle: why, given the compelling informational benefit from sunsetting crisis-driven financial regulation, has Congress chosen not to do so? I offer three possible explanations, one prudential, one political, and one pragmatic. First, there may be a prudential concern that a sunset law would impose costs on firms and individuals by decreasing regulatory certainty, given an expiration date. I

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88. Kearney, supra note 60, at 55.
do not find this to be a plausible explanation. In the financial regulation context, the multi-year interval before a sunset is often long enough for the completion of business planning surrounding the regulated financial investments and instruments, especially given how rapidly the financial environment changes. The business planning affected by financial regulation, in short, does not typically consist of projects with a long development lead, such as the research and development of a pharmaceutical drug. Furthermore, experience teaches otherwise. The CFTCs being a sunset agency, with the possibility that it would cease to exist, along with its regulatory framework, did not hinder a remarkable degree of innovation in financial derivatives that were under the agency’s jurisdiction.\(^90\)

Second, and in my judgment, a more compelling explanation, sunsetting imposes political costs on legislators because it shifts decisional control over the content of a statute from current legislators to a future Congress.\(^91\) That creates a strong disincentive to permit a second look. This might have been especially so in the case of Dodd-Frank, enacted by a Congress with very large Democratic majorities not likely to be of the same margin in the future, because it contains provisions of great interest to Democrats’ core political supporters but with minimal support in the broader electorate, and that, more likely than not, would not have survived separate up or down votes. Instances of this type of provision are the requirement that public companies hold shareholder votes on executive compensation (a labor union issue, which had been introduced as a bill in prior sessions, but had languished in the Senate),\(^92\)


\(^91.\) Although sunset laws can also be seen as a mechanism by which current Congresses control future Congresses—by forcing legislation to be considered, see Gersen, *supra* note 57, at 266—it seems to me that an enacting majority, particularly if it is risk-averse, would be far more concerned about preserving the legislation it has enacted than influencing the agenda of a future Congress, especially given uncertainty over what a future Congress might do to its “landmark” law. To the extent that sunsetting decreases the present value of a statute to constituents, it could impose a further political cost by lowering “rents” (such as campaign contributions) legislators can obtain from interest groups seeking a provision’s enactment. I do not emphasize this cost as there is dispute in the literature over whether sunsetting decreases or increases such “rents.” See, e.g., id. at 280-81 (recognizing that although there is no theoretical reason to think interest groups should prefer more durable legislation, short-term measures, such as, sunsetting provisions, have lower value, e.g., interest groups will pay less for their enactment, given the risk of future repeal); Kysar, *supra* note 57, at 365 (contending that sunsetting increases rents because interest groups must lobby for legislation’s renewal).

and the requirement of affirmative action in hiring by federal financial agencies and any business (e.g., banks and law firms) regulated by, or participating in programs or contracts of the agencies (a black caucus issue, advocated by Representative Maxine Waters, a member of the House committee responsible for drafting the bill). Legislators, recognizing that the crisis environment guaranteed passage of a bill, opportunistically worked to include those provisions, and would not have wanted to tempt fate with a subsequent reconsideration that might cull their legislative contributions.

Finally, human nature and practical concerns of party leadership would seem to have a role in explaining the puzzle. Lawmakers drafting emergency financial statutes may think, out of hubris, that they have indeed crafted landmark legislation, which is the best of all possible regulatory solutions. As a consequence, the idea of including a sunset provision would not cross their minds, and if suggested, would most likely be perceived as a rebuke of their work product, rather than a needed mechanism for improving rules that are bound to be imperfect. In addition, drafters tend to personally identify with legislation, especially when it bears their names. In such a setting, legislators would perceive sunsetting as potentially diminishing or threatening what they consider to be their “legacy.” Reinforcing such foibles of human nature, party leadership rarely has a strategic interest in entertaining a need to employ sunsetting in financial legislation enacted in a crisis, for it is typically supported by large majorities with the backing of the media and a panicked public. Such pragmatic considerations would seem to explain why the USA PATRIOT Act had a sunset provision, but Sarbanes-Oxley, enacted less than a year later, did not. Not only was the USA PATRIOT Act an administration bill with no legislator’s name attached, but also, party discipline alone could not lock up passage because a sufficient number of members in both parties felt uneasy over its considerable expansion of law enforcement powers, provisions also considered problematic by the media.

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Given that lawmakers' incentives often work at odds with sunsetting, a key item on an agenda for improving the quality of financial regulation decision-making, then, is the development of public awareness and suasion to overcome those hurdles. A starting point would be to educate the media, political elites, and public concerning what is needed for value-enhancing financial regulation: that sunsetting, at least in this context, is good governance. The view that sunsetting and good government go hand in hand was, for a brief time, widely shared by political elites, when then-President Jimmy Carter espoused the approach and Common Cause assisted the Colorado state legislature in drafting a sunset statute.  

Because there is a literature indicating that the media can, and does, influence policy outcomes by affecting an issue's salience, pursuing a media educational campaign to foster an ethos of sunsetting would seem to be an excellent initial strategy for advancing sunsetting on the legislative agenda. However, this task will not be easily accomplished. To affect public opinion, the benefits of sunsetting would need to be concretized in a vivid example or event, for the literature further suggests that public attention is more likely to be engaged, and thereby influenced, by concrete issues, such as the drama of human interest stories, rather than abstractions. In keeping with this observation, the media tends to cover items of interest and information in the form preferred by its audience.

B. Opening Financial Regulation Up to Experimentation

The harmonization premise of contemporary international financial regulation is inhospitable to regulatory innovation: notwithstanding an absence of an enforcement mechanism, nations agreeing to comply with the Basel accords implement the standards through domestic legal processes (in the United States, for instance, through administrative rule-making), incorporating them into domestically-enforceable obligations. As a consequence, negotiations over changes to the accord tend to be intense and extended, as nations vie for provisions that

96. Kysar, supra note 57, at 353.
97. Romano, Does the Sarbanes-Oxley Act, supra note 11, at 255-58.
will advantage or, at least not disadvantage, domestic financial institutions, and that are consistent with national policies. Such an understandably politically-infused process makes the outcome less than ideal and revision cumbersome, and at the same time it blocks experimentation or encourages violations of the accord.

Yet, the dynamic environment in which financial institutions operate calls for a nimble regulatory apparatus that can both adapt to new products and accompanying risks, and safeguard the international financial system from systemic regulatory error. Regulatory experimentation and diversity are safety valves that address both concerns. But, to introduce the capacity for regulatory diversity into international financial regulation, the Basel architecture needs to be altered: experimentation deviating from the accord’s strictures should be permitted and encouraged, albeit in a structured fashion, to mitigate the possibility that a nation’s experiment could adversely impact system-wide stability.

A mechanism for introducing diversity and experimentation into the international financial regulatory architecture, while safeguarding against an increase in systemic risk, is a peer review process, with three components. First, a nation wishing to adopt a rule or regulatory approach different from that taken by Basel would submit to a Basel Committee—designated committee of peer regulators—a proposal which would include a description of the proposed departure accompanied by an econometric forecast (or formal modelling, where the requisite data for forecasting are unavailable) of its effect on financial system stability. Second, the review process in which a committee would evaluate a proposal, seeking further information or undertaking its own economic analysis, would operate with a presumption of approval: unless it found concrete evidence that the proposed departure would increase systemic risk, and thereby, adversely affect financial system stability, a departure would be approved. Third, approved departures would be subject to ongoing monitoring and periodic reassessment, so that approvals could be withdrawn, for instance, when an approved regulatory departure is seen to have a negative systemic impact, which could not have been ascertained in an initial review, or

101. Romano, *For Diversity*, supra note 7, at 26. For elaboration of the proposed procedural mechanism, including cost implications for international financial institutions, see id. at 26-48, 57-61.

102. *Id.* at 26-28.

103. *Id.* at 31-34.
when the regulatory impact has changed with new economic and technological conditions.\textsuperscript{104}

All of the documentation in the three stages of the review process should be made publicly available. A transparent decision process should improve the quality of regulatory decision-making, as participants will have a stronger incentive to provide well-reasoned justifications, with analytical support, for their positions on deviations from Basel requirements, and other nations will be able to learn from that experience and thereby be better able to make informed regulatory choices. The transparency of the ongoing review process offers a critical additional benefit to that of the initial review procedure: it provides a mechanism for comparing the efficacy of the Basel regime to departures from it. Because the reassessment should provide data on the effectiveness of alternative regulation, it will also encourage a reevaluation of the Basel requirements by other nations, and emendations to Basel itself.

I have provided a thumbnail sketch of how regulatory experimentation could be introduced into international financial regulation; but experimentation could also be incorporated into domestic financial legislation. It is the genius of the federal organization of the U.S. government that makes it quite amenable to such an approach.\textsuperscript{105} Moreover, structuring financial regulation to be more hospitable to experimentation is consistent with a contemporary trend in economics to introduce experimentation into policymaking, as the gold standard for policy evaluation.\textsuperscript{106} Michael Greenstone advocates implementing regulatory initiatives through a process that either starts with small-scale randomized experiments or permits states to implement different regulatory approaches.\textsuperscript{107} The expectation is that coverage would be expanded nationwide were these initial experiments successful, essentially on a cost-benefit metric.\textsuperscript{108} Although this approach, as Greenstone notes, is most feasible for “environmental, health, labor market, and safety regulations”—where discrete programs can be implemented using randomized trial experiments or “quasi” experiments, on the model of Food and Drug Administration testing requirements for new drugs\textsuperscript{109}—there is, I think, an analogue in the financial setting. That

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\bibitem{104} Id. at 38-40.
\bibitem{105} ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATE LAW 4-6 (1993).
\bibitem{106} E.g., Michael Greenstone, Toward a Culture of Persistent Regulatory Experimentation and Evaluation, in NEW PERSPECTIVES ON REGULATION 113, 114-15, 118-19 (David Moss & John Cwertko eds., 2009).
\bibitem{107} Id. at 120.
\bibitem{108} Id. at 115, 120.
\bibitem{109} Id. at 114, 116, 118-20, 125.
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could be done by providing agencies with expanded exemptive and waiver power and an accompanying directive to use the authority to permit individual or classes of institutions to operate under different regulatory arrangements.110

Congress has, in fact, used such an approach in crisis-driven financial legislation, but it has been limited in scope. For example, Sarbanes-Oxley’s mandate of independent audit committees (by requiring the SEC to direct stock exchanges to prohibit the listing of any firm without an independent committee) states that the SEC can establish exemptions to the statutory criteria of director independence.111 Such an approach could be more broadly applied, and agencies instructed to implement rules along the lines of a small-scale experiment, with

110. In critiquing my advocacy of sunsetting crisis-driven financial regulation, Coffee contends that I “never discuss” what he considers the “most feasible remedy,” agency exemptive authority. Coffee, *The Political Economy*, supra note 63, at 1035. This is an astonishing, false assertion. Both of my papers that Coffee critiques for this ostensible omission explicitly discuss agency exemptive authority. In my 2005 article, I suggested that the easiest way to revamp misconceived provisions in Sarbanes-Oxley was for the SEC to use its exemptive authority, but noted that it was not likely to do so. Romano, *The Sarbanes-Oxley Act*, supra note 1, at 1595, 1602 & n.214. This Article advocates congressional directives to agencies to use such authority in implementing emergency regulation. See *supra* Part I. I consider explicit instruction necessary because history teaches that the SEC will not voluntarily use its exemptive powers to remedy flawed rules that it has adopted in implementing emergency legislation. See Romano, *The Sarbanes-Oxley Act*, supra note 1, at 1595, n.214. The well-known cognitive bias to favor the status quo aids in explaining why agency exemptive power alone is not, as Coffee contends, an effective means of revising flawed legislation. Indeed, Coffee’s principal example of the administrative process’s remedying flawed legislation refutes his contention: Congress mandated the exemption of non-accelerated filers from Sarbanes-Oxley’s internal controls auditor attestation requirement because the SEC failed to do so. Coffee’s odd assertion regarding my supposed ignorance of the SEC’s exemptive authority is part of a piece: his paper contains numerous misstatements of my position regarding emergency-based legislation. To take an example, Coffee attempts to suggest that my critique of crisis-driven financial legislation is directed at Sarbanes-Oxley’s creation of the PCAOB, and the direction to the SEC to adopt attorney conduct standards. Coffee, *Political Economy*, supra note 63, at 1036-37, 1046. But my 2005 article critiquing Sarbanes-Oxley was directed solely at corporate governance mandates, for which the best available empirical evidence indicates they would not have remediated the accounting frauds that motivated the legislation. Romano, *The Sarbanes-Oxley Act*, supra note 1, at 1529, 1595. Neither the PCAOB’s creation, nor the attorney conduct standards, is mentioned in my article because, of course, as the regulator of auditors, the PCAOB has no relation to corporate governance mandates, nor does the regulation of attorney conduct. Id. Coffee’s strategy would seem to be to minimize the meliorating properties of sunset review by implying that the position entails treating every provision in crisis-driven legislation as equally wrongheaded. E.g., Coffee, *Political Economy*, supra note 63, at 1023. But blanket repeal is not the gist of sunset proposals. The point of sunsetting is to produce a more deliberative drafting process that weeds out the ill-founded from the wise, a reflection impossible to undertake in the heat of a crisis, and not likely, thereafter, to be willingly undertaken by an agency, given limited time and resources, as well as bureaucratic inertia, which work hand in glove with the aforementioned status quo bias to blunt reconsideration.

incremental expansion only after a cost-benefit analysis undertaken by independent experts.

One means by which experimentation could be implemented within a waiver setting is by permitting a firm, or class of firms, to request a regulatory waiver, and by not leaving the matter solely up to an agency’s initiative. The standard for approval of an exemption could be an assessment of minimal adverse impact on the statutory objective (e.g., on systemic risk or financial statement fraud, objectives, respectively, of Dodd-Frank and Sarbanes-Oxley). Because an agency could be expected to be predisposed to believe that whatever regulation exists is good and hence to oppose exemptions, it could be required to accept, or at least to have to rebut in a meaningful way, an analysis of the proposed waiver provided by independent experts. Maintenance of the statutory purpose would be safeguarded by having the agency engage in ongoing monitoring and review of approved waivers, to make sure no adverse impact developed. And, paralleling Greenstone’s contemplated regulatory reform process were the waivers deemed successful, the agency would be expected to extend them to more, or all, firms or sectors.112 Where the proposed waiver is a private sector initiative, the firms could be required to cover the agency’s cost of evaluating and administering the experiment.

The interaction between statutory experimentation through waivers and required sunset reviews can, however, be complicated. When exempted firms are non-random, one cannot evaluate properly either the impact of the waiver with an eye to generalization, or the efficacy of the regulation under sunset review, for the analysis would be subject to selection bias, as covered and excluded firms would not be comparable. For instance, firms that request a waiver would most likely be those that would be most adversely affected by a rule. This difficulty could be addressed if regulatory waivers were constructed as natural experiments, in which firms receiving a waiver were selected by lot.113 But, such an

112. See Greenstone, supra note 106, at 115.

approach would, in my judgment, in many instances, be politically infeasible and inappropriate, as it could seriously interfere with market competition, where the exempted firms' operating cost would be less than that of the regulated firms. In addition, if the exemption was for a limited time frame—for instance, until the "experiment" would be evaluated by the agency for its effectiveness—then firms' behavior may not represent how they would respond to a permanent rule, as they strategize to affect the outcome. In short, there is an inherent tension between sunset reviews and experimentation. But, I do not believe the potential conflict is sufficient to reject the proposed dual-pronged regulatory approach.114 Given the sunset review panel's expertise, it should be well attuned to the selection issue and able to recalibrate the analysis when undertaking its regulatory evaluation in the context of experimental data.

Although I believe that a review mechanism permitting departures from, and thereby, introducing experimentation and diversity into financial regulation requirements, and especially into the Basel international financial regulatory regime, is quite feasible, as with sunsetting, there are powerful incentives working against its adoption. Financial regulators, in particular, confront determined lobbying by banks and legislators to harmonize rules in order to not impact negatively, large internationally-focused domestic banks. This is, in essence, an attempt to legislate modern-day mercantilism which ought to be resisted. In addition, regulators may be subject to a status quo bias, leading them to evaluate waiver requests adversely, particularly those that are most innovative, and legislators, out of hubris, may resist permitting deviation from mandates.115 This is, then, another area in which a media and public educational campaign, on the value-added of financial regulation experimentation and diversity, will be critical.

114. Greenstone, it should be noted, recommends automatic sunsets along with experimentation in his regulatory reform agenda, and does not view them to be in tension. Greenstone, supra note 106, at 120-21, 123. This is most likely because he envisions experiments undertaken on a randomized, small-scale basis, which would not be likely to interfere, but rather would assist in the cost-benefit evaluation of the sunset review he contemplates. See id. at 120. In addition, he advocates automatic sunset for all regulations, many of which would not have been subjected to experimentation. See id. at 123.

Determining how to regulate financial institutions effectively is challenging under the best of circumstances, given the uncertain and dynamic environment in which they operate. What would appear to be an optimal regulatory policy can become a serious mistake as new risks materialize as financial institutions and products interact with regulation in unanticipated ways. Yet, Congress typically legislates on financial matters in a crisis environment, which is not conducive to high-quality decision-making. International financial regulators have not fared better, as their focus on harmonizing global financial regulation has limited the generation of information on regulatory alternatives, and hindered the making of a nimble and adaptable rulemaking process better suited to the environment.

There is a useful legislative tool that could mitigate legislative failure in the field of financial regulation: a sunsetting statute. One could also make headway in improving the quality of decision-making in international financial regulation through adoption of a structured peer review process that permits regulatory experimentation and diversity, subject to procedural safeguards. Experimentation and diversity could be incorporated into the legislative process as well, by Congress’s directing agencies to use regulatory exemptive and waiver powers to foster such objectives. In tandem with sunsetting, the greater flexibility arising from use of such tools would facilitate timely updating of the legislative and regulatory architecture, which is a matter particularly appropriate to financial regulation.

A POSTSCRIPT ASSESSMENT OF THE IRON LAW OF FINANCIAL REGULATION

As this Article has contended, there is an “Iron Law” of major U.S. financial regulation: (1) enactment is invariably crisis driven, adopted at a time when there is a paucity of information regarding what has transpired; (2) resulting in “off-the-rack” solutions often poorly fashioned to the problem at hand; (3) with inevitable flaws given the dynamic uncertainty of financial markets; (4) but arduous to revise or repeal given the stickiness of the status quo in the U.S. political framework of checks and balances. The ensuing one-way regulatory ratchet generated by repeated financial crises has produced not only costly policy mistakes accompanied by unintended consequences, but

116. See supra Parts II–III.
also a regulatory state whose cumulative regulatory impact produces, over time, an increasingly ineffective regulatory apparatus.

This Postscript analyzes the experience with regulators’ implementation of Dodd-Frank since the publication of the chapter from which the Article is taken. The analysis bolsters the Article’s contention regarding the inherent problems in crisis-driven financial legislation and the corresponding benefit for improving decision-making that would be obtained from employing, as best practice, the legislative tools of sunsetting and experimentation to such legislation and its implementing regulation. While it would be foolhardy to claim that application of these tools would produce the optimal regulatory policy, it is plausible to conclude that their use would advance means-ends rationality by better coupling the two, substantially raising the quality of decision-making by providing a feedback loop measuring and remedying regulatory errors. The depressing travails of Dodd-Frank’s implementation, which make plain the statute’s shortcomings, will, it is to be hoped, focus attention on how, going forward, we can achieve more effective financial regulation by including in crisis-driven legislation, the safeguards of sunsetting and experimentation.

P.I. DODD-FRANK ACT: A REGULATORY MORASS

Four years after enactment, all 280 of Dodd-Frank’s specified rulemaking deadlines had elapsed with 45% having been missed, and of the Act’s 398 rulemaking requirements, slightly more than half (52%), had been finalized, while nearly one-quarter (24%) had not yet even been proposed. Of course, the vast number of required rules and complexity of issues would of their own accord impede implementation. But rulemaking has also moved at a glacial pace due to intensive lobbying by affected parties who, given the stakes in the legislative delegation to agencies of the task of reconfiguring financial markets and institutions, have understandably sought to shape regulatory outcomes to their advantage.

The regulatory morass occasioned by Dodd-Frank might on first impression suggest to some that sunsetting is inapposite for the complexity of contemporary emergency legislation because its delegated rulemaking would not, in fact, be in place in time to be assessed when a

117. See supra Parts II–III.A.
118. See supra Part III.
sunset review would have to commence. I draw a contrary conclusion. In my judgment, the protracted rulemaking experience of Dodd-Frank only further strengthens the case for sunsetting. First, the stakes for interested parties would be lowered, and hence lobbying less intense and prolonged, if regulation had to be reassessed and put to a legislative vote at a future date.120 The affected parties would be assured of a second chance to make their case, so to speak, at a time when far more information would be available to indicate whether proponents’ claims or critics’ concerns were well-founded, and they could be assured that, at a specified point in time, unintended adverse consequences could be attended to and reversed or mitigated by legislation adopting (or more likely, instructing implementation of) a better regulatory solution. A specified timetable, expert counsel, and streamlined voting procedures accompanying a legislative vote on whether to retain or modify the expiring legislation and implementing regulation should go a long way to ensuring such an outcome.121

Second, when a rule cannot be crafted within a reasonable time frame of a multi-year interval prior to a sunset review, a fair inference is that the statutory delegation was poorly devised or entirely misconceived, in the first instance. Rulemaking is not intended to be interminable. If a proposed rule has not been implemented by the time set for sunsetting, the sunset review could, of course, automatically be postponed to a specified date after implementation. But, legislators could also reasonably draw a negative inference regarding a rule’s appropriateness or efficacy from an agency’s inability to implement it in timely fashion. A protracted implementation could plausibly suggest that a proposed rule has raised broad-based concern that it would create severe market dislocations and would fail a cost-benefit test, as opposed to its being due to dilatory tactics by interest groups, because it is reasonable to suppose that regulators have a strong incentive to

120. Experimentation could provide a further benefit of mitigating concerns expressed by commentators that rulemakers subject to a cost-benefit standard, such as the SEC, cannot meet the rigors of judicial review, following the invalidation of the proxy access rule discussed supra, in notes 30-32 and accompanying text. It has been advocated that SEC rules that are adopted on an experimental or sunsetting basis could be subjected to a lower level of judicial scrutiny because a more finely tuned cost-benefit analysis could be undertaken with the knowledge gleaned from the experiment when the rule comes up for the required renewal. See, e.g., Zachary J. Gubler, Experimental Rules, 55 B.C. L. REV. 129, 143-47 (2013); Yoon-Ho Alex Lee, Essay, An Options-Approach to Agency Rulemaking, 65 ADMIN. L. REV. 881, 897-98 (2013).

121. See supra notes 84-88 and accompanying text (sketching procedures necessary to render sunsetting effective).
implement statutory directives expeditiously to avoid being called to task by Congress for failure to do so.

More fundamentally, Dodd-Frank and the regulatory apparatus it imposes have generated controversy, disappointment, and alarm at nearly every turn. For instance, it fails to address key factors widely-acknowledged to have contributed to the financial crisis, such as runs on shadow banks, whose liabilities were collateralized with securitized mortgages, and GSEs that guaranteed those securitized mortgages.\(^{122}\) Rather than address shadow banking and the GSEs explicitly, the focus of the statute directed at the subprime mortgage market’s contribution to the crisis is a requirement that mortgage securitizers retain five percent of the securities of non-qualified mortgages.\(^{123}\) This provision is informed by a mistaken premise, however, as securitizers did retain risk pre-crisis, holding substantial amounts of mortgage-backed securities on their balance-sheets.\(^{124}\) As Ryan Bubb and Prasad Krishnamurthy note, banks’ retention of securitized mortgage risk contributed to the financial crisis, jeopardizing banks’ liquidity, and ultimately, solvency.\(^{125}\) Consequently, this particular Dodd-Frank provision advances a perverse

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122. For the critical importance of the shadow banking sector in sparking the global financial crisis, see GARY B. GORTON, SLAPPED BY THE INVISIBLE HAND: THE PANIC OF 2007, at 45, 58 (2010); and for the importance of the GSEs, see Viral V. Acharya et al., The Dodd-Frank Wall Street Reform and Consumer Protection Act, in REGULATING WALL STREET: THE DODD-FRANK ACT AND THE NEW ARCHITECTURE OF GLOBAL FINANCE 9 (2011). As Foote et al. stated, the GSEs:

were major players in the lending boom of the 2000s, even if much of [the] lending occurred outside of their traditional guarantee business [i.e., were privately originated]. Specifically, both Fannie Mae and Freddie Mac indirectly invested heavily in risky mortgages by buying AAA tranches of subprime and Alt-A mortgage-backed securities and holding these securities in their retained portfolios . . . [i]n many of the boom years, account[ing] for half of the subprime AAA-rated securities.


124. See, e.g., Viral V. Acharya & Matthew Richardson, Causes of the Financial Crisis, 21 CRITICAL REV. 195, 200-01 (2009); Foote et al., supra note 122, at 19 (noting that six of the top ten institutions with subprime losses "not only securitized subprime mortgages, they actually owned companies that originated them"). For a critique of the efficacy of this provision, as well as Dodd-Frank’s requirement that mortgage originators judge an applicant as having the ability to pay for the loan, see Ryan Bubb & Prasad Krishnamurthy, Regulating Against Bubbles: How Mortgage Regulation Can Keep Main Street and Wall Street Safe — from Themselves, 163 U. PA. L. REV. (forthcoming 2014) (manuscript at 22-23, 30-31, 42-43) (on file with the Hofstra Law Review).

125. Bubb & Krishnamurthy, supra note 124 (manuscript at 40-42).
regulatory strategy for which it would appear to aggravate, not diminish, systemic risk created by mortgage securitizations. In addition, Dodd-Frank inadequately responds to the aftereffects of the crisis—taxpayer bailouts of “too-big-to-fail” financial institutions. Although legislators enacting Dodd-Frank have emphatically insisted that the statute has ended “too-big-to-fail” and taxpayer bailouts, having included a section addressed to the resolution of large financial institutions, many commentators maintain that it has not, in fact, resolved the “too-big-to-fail” syndrome and could well exacerbate it.

126. Id. (manuscript at 30-32). The risk retention provision may prove to be a relatively minor constraint in the overall scheme of things, however. That is because financial regulators are adopting the Consumer Financial Protection Bureau’s (“CFPB”) definition of a “qualified” mortgage, which does not include a down payment requirement, has a lax debt to income ratio requirement of forty-three percent plus includes numerous exemptions from these and other requirements, such as limits on interest rates and prohibition of balloon payments, for small and rural area banks (some of which are statutory), and for government agency-insured loans. CFPB, 12 C.F.R. § 1026.43(e)(vi) (2013). Although the definition proposed in 2011 for a qualified mortgage under the risk retention provision by bank regulators, the SEC, and the Department of Housing and Urban Development (“HUD”) had far more substantial requirements, such as a twenty percent down payment and seventy-five percent debt-to-income ratio, that was not to be. Credit Risk Retention, 76 Fed. Reg. 24,090, 24,123-24 (proposed Apr. 29, 2011). The agencies were lobbied by legislators, the housing industry, consumer advocacy groups, and community activists, to adopt instead, as the risk-retention definition of a qualified mortgage, the CFPB’s definition of a qualified mortgage, and they did exactly that in a re-proposed rule issued in 2013, Credit Risk Retention, 78 Fed. Reg. 57,927, 57,989 (proposed Sept. 20, 2013), and finalized in 2014. Further, HUD designated all of its mortgages as qualified, and stated that its standards conform to the CFPB’s definition. Qualified Mortgage Definition for HUD Insured and Guaranteed Single Family Mortgages, 78 Fed. Reg. 75,215, 75,215-16 (Dec. 11, 2013). Consequently, the pool of mortgages falling into the non-qualified category for risk retention purposes will be small, and many qualified mortgages will carry considerable default risk. As Peter Wallison and Edward Pinto put it, assessing the CFPB’s definition: “[N]either Dodd-Frank nor the new QM [qualified mortgage] rule has changed anything significant. Political pressure to continue lending to borrowers with weak credit standing has trumped common sense underwriting standards.” Peter J. Wallison & Edward J. Pinto, New Qualified Mortgage Rule Setting Us up for Another Meltdown, WASH. TIMES, Mar. 3, 2013, http://www.aei.org/article/economics/financial-services/housing-finance/new-qualified-mortgage-rule-setting-us-up-for-another-meltdown. Bubb and Krishnamurthy’s critique of the risk-retention rule could, however, suggest that a lax definition is for the better from the perspective of financial institution stability. Bubb & Krishnamurthy, supra note 124 (manuscript at 30-31). This is an issue that a sunset review and regulatory experimentation could arbitrate.

127. E.g., Cezary Podkul, Is ‘Too Big to Fail’ Really Over? Rep. Barney Frank Says Yes but Others Disagree, WASH. POST, July 15, 2011, http://www.washingtonpost.com/blogs/political-economy/post/is-too-big-to-fail-really-over-rep-barney-frank-says-yes-but-others-disagree/2011/07/15/gIQAPMoSGI_blog.html (“Rep. Barney Frank, . . . one of the law’s chief architects . . . insisted several times that ‘too big to fail’ was over” and reprimanded a bank regulator for suggesting that banks’ unique role in the economy justifies a public safety net that is “unlikely ever to be provided at zero public cost.”).

The basis for such a contention is that by identifying systemically important financial institutions ("SIFIs") and subjecting them to a special regime that permits their being bailed out upon approval by designated government actors, it simply codifies too-big-to-fail and thereby does not diminish the likelihood of such an occurrence, despite legislators’ contrary insistence. As Peter Wallison puts the net effect of these provisions, Dodd-Frank extends the Federal Deposit Insurance Corporation’s policy of paying off unsecured bank depositors to all large financial institutions, as well as non-bank institutions that are classified as SIFIs.

But, at the same time as ignoring or inadequately addressing critical issues related to the financial crisis, the statute will be imposing considerable costs on non-financial companies, which could well be in a multiple of billions of dollars, due to time-consuming disclosure requirements whose regulatory objectives have no connection to the financial crisis, the ostensible focus of the legislation (disclosures regarding conflict minerals, payments to foreign governments for oil and gas development, and the ratio of CEO compensation to that of the median employee). Even the proponents of those provisions did not


130. Wallison, Dodd-Frank, supra note 129.

believe that the issues informing their proposals had a connection to the financial crisis: the legislative majority simply opportunistically took advantage of including provisions that were desired by key constituent interest groups and that had scant chance of independent enactment (as evidenced by the stalled progress of related bills and the subsequent controversy over those rules’ implementation).  

Including provisions unrelated to the financial crisis in Dodd-Frank was also used strategically to secure a sponsoring legislator’s vote, which a lead drafting legislator deemed necessary for the bill’s passage.  

132 A conflict minerals bill, which among other provisions required companies to certify their imported products were conflict mineral free, had languished in the House since its introduction in November 2009, as had a Senate bill requiring disclosure, among other measures, introduced in April 2009. Library of Cong., Bill Summary & Status: 111th Cong. (2009-2010) H.R. 4128 All Information, THOMAS, http://thomas.loc.gov/cgi-bin/bdquery/z?dlll:h.r.04128 (last visited Nov. 23, 2014); Library of Cong., Bill Summary & Status: 111th Cong. (2009-2010) S. 891 All Information, THOMAS, http://thomas.loc.gov/cgi-bin/bdquery/z?dlll:SN00891 (last visited Nov. 23, 2014). Similarly, a bill requiring resource extraction issuers to disclose payments to foreign governments had not progressed beyond its introduction in September 2009. Library of Cong., Bill Summary & Status: 111th Cong. (2009-2010) S.1700 All Information, THOMAS, http://thomas.loc.gov/cgi-bin/bdquery/z?dlll:s.01700 (last visited Nov. 23, 2014). Senator Robert Menendez, who is closely identified with organized labor and was the sponsor of the CEO pay ratio provision, had introduced a bill requiring the pay-ratio-disclosure in February 2010, among other provisions concerning executive compensation, and was unable to obtain even a single cosponsor. Jerry Markon & Dina ElBoghdady, Pay Rule Still Unwritten amid Corporate Push, WASH. POST, July 7, 2013, at A1; Library of Congress, Bill Summary & Status: 111th Congress (2009-2010) S.3049 All Information, THOMAS, http://thomas.loc.gov/cgi-bin/bdquery/z?dlll:s.03049 (last visited Nov. 23, 2014) (follow “All Information” hyperlink). He also did not attempt to rationalize the provision’s inclusion as remedying a cause of the financial crisis. See Letter from Robert Menendez, U.S. Senator, to Honorable Mary L. Schapiro, Chairwoman, U.S. Sec. & Exch. Comm’n (Jan. 19, 2011) (on file with the Hofstra Law Review). In a letter dated January 19, 2011, urging the SEC to implement the pay ratio disclosure rule within the year, Senator Menendez stated that he “wrote this provision so that investors and the general public know whether public companies’ pay practices are fair to their average employees, especially compared to their highly compensated CEOs.” Id. In a more recent press release of March 2013 “reiterating” the need for the SEC to enact a rule, he shifted the rationale by noting that “excessive compensation schemes provided part of the fuel for the financial crash” while focusing on, as the rationale for the disclosure, “income inequality . . . [o]ver the last decade,” with “soaring” CEO wages compared to “workers[’] . . . stagnant wages” and declining “median family income,” a subject matter that, although surely of concern, is not conventionally thought to be connected to the global financial crisis of 2008-2009. Press Release, Robert Menendez, Menendez Calls on SEC to Expedite Adoption of CEO-to-Median Pay Disclosure Rule (Mar. 12, 2013) (on file with the Hofstra Law Review).  

133 As Markon and ElBoghdady report, the pay ratio provision was included in the bill to obtain Senator Menendez’s vote. Markon & ElBoghdady, supra note 132. Senator Menendez was a member of the Senate committee drafting what became the Dodd-Frank legislation, and prior to the pay ratio provision’s inclusion, he was quoted as expressing hesitation over supporting the bill, although the concerns he mentioned in the press report related to improving provisions concerning bailouts. Jessica Brady & Anna Palmer, Senators, K Street Not Sold on Dodd’s Reform Bill, ROLL CALL (Mar. 16, 2010, 12:00 AM), http://www.rollcall.com/issues/55_104/-44214-1.html.
SEC has had to devote time and resources to address rules quite unrelated to both the financial crisis and the agency’s core mission, a diversion further exacerbating the delayed implementation of rules with at least an ostensible nexus to the crisis, such as those relating to security-based swaps and asset-backed securitizations, along with the Volcker rule prohibiting financial institutions’ proprietary trading. Those rules’ statutory deadlines have long since been missed.\(^{134}\)

The present appalling legislative and regulatory state of affairs should not be a surprise, for as this Article has emphasized, emergency financial legislation is inherently ill-suited for addressing crises, given information difficulties: the politics of financial crises requires acting before sufficient information can be developed on what might be the wisest course of action, and thereby provides an opportunity for well-positioned political actors opportunistically to advance an agenda that is tangential to the crisis at hand and may well be inapposite given the best available data.\(^{135}\) Sunsetting such legislation, which is informed by the judgment of a panel of legislatively-appointed experts, would mitigate this situation, as the panel’s evaluation and recommendations would direct legislators’ attention to the extant evidence of a policy’s impact.

But the making of Dodd-Frank is considerably more dismal than that of well-intentioned legislators, operating in a panic, making mistakes. In a parody of the textbook behavioral response to a financial crisis, an eyewitness account of the enactment of Dodd-Frank, in which every action and reaction of Congressman Barney Frank and his staff were tracked, relates that Congressman Frank objected to the appointment of a commission to study the causes of the crisis—which was being advocated by members of Congress and commentators—as a “distraction,” and was reconciled to its creation only upon ensuring the commission’s work would be completed after legislation responding to the crisis could be enacted.\(^{136}\)

\(^{134}\) There are, of course, additional reasons for the SEC’s delayed implementation of the Volcker rule besides its having to focus attention elsewhere: the need to coordinate the drafting of a rule across multiple agencies, and the complexity of the substantive issues, which is discussed in Part P.IIA, infra. The SEC’s final rule implementing the Volcker rule (coordinated with banking regulators and the CFTC) was adopted on December 10, 2013 and published in the Federal Register on January 31, 2014. Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds, 79 Fed. Reg. 5536, 5539 & n.13, 5806 (Jan. 31, 2014).

\(^{135}\) See Romano, The Sarbanes-Oxley Act, supra note 1, at 1591, 1594 (recognizing that Sarbanes-Oxley substantive corporate governance mandates, advocated by policy entrepreneurs, were adopted despite empirical literature tending to suggest that they would be ill-conceived, as they would not improve corporate performance or audit quality, the stated statutory objective).

\(^{136}\) ROBERT G. KAISER, ACT OF CONGRESS: HOW AMERICA’S ESSENTIAL INSTITUTION
We are further provided with insight into Congressman Frank’s understanding of how to respond to the financial crisis by this description of his perspective on the crisis: it was that “the causes of the Great Crash were already well understood,” and that it was due to “irresponsible financiers and anti-regulation Republicans.” Such a cartoonish contention could only be made by a poorly-informed and highly-partisan political actor with a sound bite understanding of the complexity of what was, after all, a global financial crisis. Indeed, Congressman Frank’s simple-minded view of the crisis followed straightforwardly from his world view: he was one of the representatives most to the extreme left on the U.S. political spectrum, as indicated by his dw-nominate score, a widely-used ideology measure developed from roll call votes by political scientists Keith Poole and Howard Rosenthal. In the 111th Congress enacting Dodd-Frank, only 36 of...
435 representatives had ideology scores to the left of Congressman Frank, and similarly, in the 110th Congress, the session prior to Dodd-Frank’s enactment, only 35 representatives’ scores were to his left.139

The failure of Dodd-Frank to address key contributing factors to the crisis related to government policies, such as the GSEs, was to be expected when an individual who had strong ideological priors, and hardly an empirically-oriented problem-solver, “alone would decide what was in, and what was out” in the shaping of the legislation in the House.140 In keeping with this synoptic characterization of Congressman Frank’s perspective, he did not make an earnest effort to forge a coalition across the aisle, as that was not in his nature and he did not have to, given large Democratic majorities in both chambers and a president from his party. Dodd-Frank was consequently enacted on a virtual party-line vote, in contrast to the typical crisis-driven legislation, which garners broad bipartisan support.141

There is an additional factor besides policy preferences of the agenda setters that informs the absence of any provision concerning the GSEs. As detailed in numerous sources, the GSEs were munificent contributors to election campaigns, as well as glad-handers to constituents, such as community organizers and activists, who in response lobbied legislators on the GSEs’ behalf.142 An extensive


140. KAISER, supra note 136, at 153. It was also convenient to blame the financial crisis on the private sector and political opponents, for that deflected blame away from Congressman Frank’s own contribution to the crisis, as he was an ardent supporter of the failed housing and easy credit policies.

141. No Republicans voted for the bill in the House, although several Democrats also voted against the bill, and only three Republicans voted to agree to the conference report, the vote resolving differences across the chambers, and thus, enacting the legislation. Final Vote Results for Roll Call 413, HOUSE.GOV (June 30, 2010, 6:54 PM), http://clerk.house.gov/evs/2010/roll413.xml; Final Vote Results for Roll Call 968, HOUSE.GOV (Dec. 11, 2009, 2:28 PM), http://clerk.house.gov/evs/2009/roll968.xml. In the Senate, similarly, all but one Democrat and only four (three) Republicans voted for the Senate’s version of the bill (conference report). U.S. Senate Roll Call Votes 111th Congress-2nd Session, SENATE.GOV (July 15, 2010, 2:29 PM), http://www.senate.gov/legislative/LIS/roll_call_lists/roll_call_vote_cfm.cfm?congress=111&session=2&vote=00208; U.S. Senate Roll Call Votes 111th Congress-2nd Session, SENATE.GOV (May 20, 2010, 8:25 PM), http://www.senate.gov/legislative/LIS/roll_call_lists/roll_call_vote_cfm.cfm?congress=111&session=2&vote=00162. Sarbanes-Oxley, by contrast, was enacted with overwhelming bipartisan support, unanimously approved in the Senate, and with only three House Republican members voting against it. See Romano, Does the Sarbanes-Oxley Act, supra note 11, at 238.

142. GRETCHEL MORGENSEN & JOSHUA ROSNER, RECKLESS ENDANGERMENT: HOW OUTSIZED AMBITION, GREED, AND CORRUPTION LED TO ECONOMIC ARMAGEDDON 68-69 (2011) (noting that “Fannie Mae was highly creative when it came to ‘encouraging’ its higher-level executives to donate to political campaigns”). Morgenson and Rosner detail Fannie Mae’s public
analysis of the GSE fiasco concludes that “[Congressman] Frank was a perpetual protector of Fannie [Mae], and those in his orbit were rewarded by the company,” as it provided employment for Frank’s friends and made sizeable contributions to his mother’s nonprofit organization. Frank was, of course, not alone in his staunch support of the GSEs in the years leading up to the crisis, as the GSEs’ largesse was ubiquitous. This venal political environment helps in explaining Dodd-Frank’s peculiar silence on the GSEs and government housing policy.

While the political largesse of the GSEs has ceased with their placement under government conservatorship, there has still been no legislative response to the considerable risk to the fisc and the economy at large that they and government housing policies pose. Numerous bills since Dodd-Frank’s enactment have, however, been introduced

relations campaign earmarking $1 trillion in spending on affordable housing between 1994 and 2000 which would “commit so much money to low-income housing . . . that no one would dare to criticize its other activities,” and its placing “partnership offices” in towns and cities throughout the country which “cemented the company’s relationships with members of Congress.” Id. at 59-61.

143. Id. at 69. Congressman Frank’s cozy relationship with the GSEs, and consequent opposition to reining them in pre-crisis, has been extensively documented. Id. at 7, 68-69, 246-47, 256-59.

144. Id. at 69-71. Senator Chris Dodd, one of the GSEs’ “most strident defenders,” was also one of several legislators who received favored treatment for home mortgages from Countrywide Financial, the subprime mortgage originator closely associated with the GSEs, as they had common legislative interests; it was an equally vigorous campaign contributor and lobbyist. Id. at 186-87, 304. Although Senator Dodd’s voting record indicates he was to the left of the center of his party, he was not an outlier, as was Congressman Frank, among his chamber compatriots: in the 111th Congress that enacted Dodd-Frank, there were more than 20 Democrats with a dw-nominate score to the left of his score and over 30 Democrats with a score to his right, while in the Senate of the 110th Congress, which was nearly evenly divided by party, there were 21 Democrats with scores to his left. See Senate_110 Rank Ordering, VOTEVIEW.COM, http://voteview.com/SENATE_SORT110.HTM (last visited Nov. 23, 2014); Senate_111 Rank Ordering, VOTEVIEW.COM, (last visited Nov. 23, 2014). As these are chamber-derived scores, one must be cautious in interpreting these data as indicating that Frank was considerably more to the left of the political spectrum than Dodd, because we cannot say whether the center of the Senate and House Democrats would be identical placed on a left-right political scale. Poole and Rosenthal have estimated a “joint space” model for the dw-nominate scores, using the votes of representatives who moved on to the Senate. POOLE & ROSENTHAL, supra note 138, at 26-30. Although this model fits House members better than it does the Senate, in the joint space ranking, Frank’s being considerably far more to the left than Dodd is again borne out: there are only 36 members whose dw-nominate score is to the left of Frank’s, while there are 169 with scores to the left of Dodd’s, among all members of the 111th Congress. House_111 Rank Ordering, supra note 139. For the legislator dw-nominate score estimates from the joint space model and an explanation of the methodology, see Royce Carroll et al., “Common Space” DW-NOMINATE Scores with Bootstrapped Standard Error (Joint House and Senate Scaling), VOTEVIEW.COM (Feb. 6, 2013), http://voteview.com/dwnomjoint.asp.

145. See MORGENSEN & ROSNER, supra note 142, at 68-71.

146. See id. at 304-05.
regarding the GSEs, with a bipartisan bill that would replace the GSEs with a new federal agency that would guarantee all mortgages having been voted out of a Senate committee by a close vote. Some commentators have contended that the bill is a solution far worse than the problem it ostensibly seeks to solve. Such criticism underscores how difficult implementing a policy to control the risk of loss generated by the GSEs and existing housing policies will be politically. But that is not why the GSEs were not addressed in Dodd-Frank; they were omitted because agenda-setting legislators had been ardent supporters of the agencies, did not consider them a problem, and would not have wanted to see policies they advocated undone.

The protracted implementation of Dodd-Frank has led some commentators to assert that the regulatory process has been captured by banking interests. That is a possibility. It would, of course, be inconceivable for the financial industry not to engage in intensive lobbying over Dodd-Frank’s proposed rules, given the immense financial stakes. But, there is an alternative, equally plausible,

147. The bill was introduced by Senators Tim Johnson (Democrat) and Mike Crapo (Republican), and voted out of committee by a thirteen to nine vote, with several members of both parties voting against it. Tray Garrison, Johnson-Crapo Reform Bill Voted to Senate Floor, HOUSINGWIRE (May 15, 2014), http://www.housingwire.com/articles/30016-johnson-crapo-reform-bill-voted-to-senate-floor.

148. See Phil Gramm & Peter Wallison, Worse than Fannie and Freddie, WALL ST. J., Apr. 17, 2014, at A15; Garrison, supra note 147 (citing reservations regarding the bill by former Treasury Secretary Timothy Geithner and House Financial Services Committee Chairman Jeb Hensarling).

149. See supra notes 143-44 and accompanying text.

150. See Arthur E. Wilmarth, Jr., Turning a Blind Eye: Why Washington Keeps Giving in to Wall Street, 81 U. CIN. L. REV. 1283, 1302, 1304-05 (2013). For capture-thesis critiques of Dodd-Frank and its implementation, see Nolan McCarty et al., Political Bubbles: Financial Crises and the Failure of American Democracy 76-77, 79-80, 81, 83, 85-86, 89 (2013) (discussing statutory and regulatory implementation); Coffee, The Political Economy, supra note 63, at 1067-72 (discussing regulatory implementation of executive compensation provisions). For capture-thesis explanations of the origins of the financial crisis and regulatory actions taken during it, see James R. Barth et al., Guardians of Finance: Making Regulators Work for Us 85-91 (2012) (suggesting regulators’ lax, deregulatory policies were the principal contributors to the financial crisis, and can be explained either by regulatory capture by large banks or regulators’ subscribing to simplistic free-market ideologies, and placing greater emphasis on ideology than capture explanation); Adam J. Levitin, The Politics of Financial Regulation and the Regulation of Financial Politics: A Review Essay, 127 HARV. L. REV. 1991, 2041-49 (2014) (contending that because they were captured by banks, regulators both mistakenly deregulated financial institutions and failed to regulate consumer financial products, causing the crisis, and by engaging in forbearance, had to bail out banks at greater cost during the crisis). The intellectual pitfall for the pre-crisis capture explanation is that it mechanically assumes that all deregulation (or all deregulation not opposed by industry) is a function of capture and ill-advised. Theoretically, this is an open-ended question and short of an empirical inquiry, it is not possible to ascertain whether the narrative is accurate.

151. Although it would not reach the level of a fiduciary breach, it would be irresponsible for
explanation for the present state of affairs: the sheer complexity and numerosity of required rulemakings under Dodd-Frank, which at times requires coordination across multiple agencies, would contribute to slowing down any specific rule’s enactment quite apart from the additional hurdle of interest group lobbying.

Moreover, lobbying has been deliberately built into the rulemaking process, and serves a critical function related to information and accountability, albeit the process can, no doubt, morph into regulatory capture. Namely, the notice and comment rulemaking procedure under which Dodd-Frank’s required rules’ enactment proceeds, as established by the Administrative Procedure Act (“APA”), intentionally encourages such a dialogue: agencies are expected to be responsive to issues raised by interested parties in rulemaking deliberations and informed by their input, as the bureaucracy is thought not to be well situated to be adequately conversant with business practices, and consequently, not attuned to the imposition of unanticipated compliance costs. In addition, the APA was modified by the Negotiated Rulemaking Act, in which Congress further authorized direct bargaining between agencies and interested parties to develop proposed rules. While business groups are the most frequent public participants in pre- and post-proposal rulemaking, scholars studying the administrative process find that the data is “not sufficient” to establish capture, nor whether business groups’ greater interest in rulemaking evidences “their defensive posture, or simply greater sophistication.”

Given the ambiguity in the impact of public participation in the rulemaking process, it is most important to note that were regulators implementing Dodd-Frank captured by the industry, then adopting this Article’s recommendation of sunsetting crisis-driven regulation would management of financial firms to not seek to defend their institutions against regulation which they believed to be both counterproductive and injurious to their firms’ financial position.

153. § 553; see KERWIN & FURLONG, supra note 29, at 168–69 (recognizing that the purpose of public participation in rulemaking is to provide agencies with information and legitimacy). Consistent with informational needs, agencies frequently initiate contact with interest groups to obtain guidance on potential rules. KERWIN & FURLONG, supra note 29, at 200. Although the APA does not state what an agency must do with public comments (except to require a statement of basis and purpose for adoption of a rule, § 553(c)), agencies typically discuss the comments in the preamble to rules, and ignore significant comments at peril of the rule’s reversal by a reviewing court. Id. at 67.
154. §§ 561–570.
155. KERWIN & FURLONG, supra note 29, at 194–95. Moreover, case studies of rulemaking find that business groups’ positions are not monolithic, id. at 195, paralleling the earlier noted lack of unity regarding legislation. See supra notes 76–78 and accompanying text.
be even more desirable than earlier advocated. The highly public legislative reassessment, replete with hearings and independent expert analyses, accompanying the process of sunset review, would draw attention to captured agencies, and so reassert, not undermine, democratic accountability and decision-making. Moreover, the public review of agency decisions subject to sunsetting should incentivize an agency to resist industry capture from the outset, as it would be aware that its actions would necessarily be evaluated thereafter, and possibly overturned.

P.II. DODD-FRANK AND THE LEGACY OF CRISIS-DRIVEN LEGISLATIVE RESPONSES

Crisis-driven legislation often adopts “off-the-rack” solutions along with open-ended delegation to regulatory agencies as legislators, who perceive a political necessity to act quickly, adopt ready-to-go proposals offered by the policy entrepreneurs to whom they afford access.\(^1\)\(^5\)\(^6\)\(^5\)\(^7\) Dodd-Frank exemplifies the difficulties that are created by these conventional crisis-driven legislative strategies in the Volcker rule, which prohibits banks’ proprietary trading, and creation of the Consumer Financial Protection Bureau (“CFPB”).

A. Problematic Delegation: The Volcker Rule

The statutory provision known as the Volcker rule illustrates both that delegation in crisis-driven legislation can be particularly problematic and that, in turn, inapt congressional directives can contribute to protracted rulemaking. The provision restricts banking entities from engaging in specific risky activities, including proprietary trading and investment in hedge funds and private equity funds, which have often been among banks’ more profitable lines of business.\(^1\)\(^5\)\(^7\) It has arguably been the most contentious and protracted implementation of Dodd-Frank’s regulatory directives, no doubt exacerbated by the broad discretionary delegation; as one commentator has put it, there are “broad gaps and ambiguities on key definitional issues,” the resolution of which

156. See supra notes 14-20 and accompanying text.
157. 12 U.S.C. § 1851(a)(1) (2012). Non-bank institutions designated as SIFIs are not subject to the ban, but are subject to heightened capital requirements and other restrictions regarding such activities. § 1851(a)(2). For the proposed rule’s expected adverse impact on banks’ bottom line, see Kimberly D. Krawiec, Don’t “Screw Joe the Plummer: “ The Sausage-Making of Financial Reform, 55 ARIZ. L. REV. 53, 60-68 (2013).
much rides on, not the least, banks’ business models. Accordingly, the lengthy gestation period has been asserted to provide the opportunity for industry capture (that is, for industry delaying tactics and resistance to wear down, or otherwise convince, regulators to adopt definitions favorable to banks).

A comprehensive study by Kimberly Krawiec of pre-proposal stage agency contacts and comments regarding the Volcker rule found that the vast majority of contacts were by industry and, while the vast majority of comments were by members of the public, those comments were uninformative, non-substantive form letters (a campaign organized by public interest groups), whereas the much smaller set provided by the industry were carefully drafted, addressing technical issues related to the rule. Certainly, such findings are intuitive: given the highly technical nature of the rule, the general public could not be expected to provide informative comments, whereas industry representatives would have the expertise to do so. While the study at times intimates that the data is consistent with a capture story, Krawiec does not conclude that the data evince capture. Rather, she notes that there were important, informed “countervailing” voices weighing in during the pre-proposal period—Senators who sponsored the rule and Paul Volcker himself—and that the political science literature suggests that the input of such individuals can provide an effective counterbalance to that of industry in agency

158. Krawiec, supra note 157, at 67. Among the ambiguities and gaps that need interpretation are the definition of “trading account,” and the scope of statutory exemptions to the ban on proprietary trading and the ban on fund investments. Id. at 65-66.

159. See id. at 69-70.

160. Id. at 58-59. This is also not a unique situation. Studies of rulemaking by the Environmental Protection Agency (“EPA”) similarly find that pre-proposal stage contacts are overwhelmingly dominated by industry (although some of those contacts are initiated by the agency as information requests). Wendy Wagner et al., Rulemaking in the Shade: An Empirical Study of EPA’s Air Toxic Emission Standards, 63 ADMIN. L. REV. 99, 125-26, 143 (2011). EPA rulemaking studies further report that a majority of comments submitted during the rulemaking process are by industry and that the number of comments from industry is positively correlated with a rule’s projected cost (crudely measured as above or below $100 million), while the number of comments from the public increases with newspaper coverage (issue salience) and is unaffected by a rule’s projected cost. Id. at 139-40. Krawiec suggests that the latter finding may explain the higher proportion of public comments in her data (that is, that the Volcker rule is a high salience provision). Krawiec, supra note 157, at 83.

161. Krawiec finds one datum surprising: no sector of the financial industry, such as institutional investors, who might have been “expected to fight any weakening” of the rule’s “protections that supposedly accrue to their benefit,” participated in the pre-proposal stage. Krawiec, supra note 157, at 84. An explanation of their non-participation that I believe is plausible is that the provision did not benefit investors (or as she puts it, albeit as an open question, that the rule’s benefits to investors were “overstated”). Id.

162. Id. at 82-84.
decision-making.\textsuperscript{163} And, she leaves the question open for, as she recognizes, it is difficult to glean much in the way of a bottom line on industry capture without examining the constellation of comments and contacts in the later rulemaking stages, nor, more importantly, how, if at all, pre-proposal concerns raised by industry affected the proposed rule, which will be subjects of her future research.\textsuperscript{164}

More important, an assertion that the prolonged implementation of the rule, or a finding that issues raised in the pre-proposal stage influenced the proposed rule, demonstrates industry capture, and would sweep aside what is, in fact, deep and genuine intellectual disagreement on both the efficacy and workability of the Volcker rule.\textsuperscript{165} For example, distinguishing between illegal proprietary trading and legal market making, can, to put it mildly, be a formidable task.\textsuperscript{166} Yet, such a distinction is in the statutory formulation. Indeed, the Volcker rule's substantive requirement poses such severe implementation challenges that the United Kingdom deliberately adopted instead a retail ring-fencing approach to constrain banks' risk-taking, which requires separating into different entities an institution's retail banking and related services from its wholesale and investment banking businesses, thereby, in theory, isolating retail banking services, and hence taxpayers, from losses on trading activities and other wholesale banking risks.\textsuperscript{167} With sunsetting, legislators' attention, with the assistance of an expert review panel, would be directed to reassessing the proprietary trading

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\item \textsuperscript{163} \textit{Id.} The study of EPA rulemaking also does not conclude that the numerical dominance (or as the authors put it, "imbalance") of industry contacts and comments during the rulemaking process "has a meaningful impact on . . . the . . . rules," but after considering arguments why it might not have such an effect, concludes that the evidence "does not rule out" that possibility. Wagner et al., \textit{supra} note 160, at 147. Reviewing the several case studies of pre-proposal comments, which all find business groups did not obtain their desired objective, Kerwin and Furlong conclude that given the small number of such studies, "no easy generalization" about the overall influence of business can be drawn. Kerwin & Furlong, \textit{supra} note 29, at 212.

\item \textsuperscript{164} Krawiec, \textit{supra} note 157, at 82.

\item \textsuperscript{165} Charles A. Piasio, \textit{It's Complicated: Why the Volcker Rule Is Unworkable}, 43 SETON HALL L. REV. 737, 738-40 (2013). It also would ignore the built-in source of delay, as noted earlier, from the need for the rule to be coordinated across multiple regulators. For a discussion of the difficulties of policy implementation when there are multiple decision points, with the Volcker rule as an example, see Peter H. Schuck, \textit{Why Government Fails So Often and How It Can Do Better} 236-39 (2014).

\item \textsuperscript{166} Krawiec, \textit{supra} note 157, at 65-68; Piasio, \textit{supra} note 165, at 761.

\item \textsuperscript{167} Timothy Edmonds, \textit{The Indep. Comm'n on Banking, The Vickers Report} 3, 7 (2013) (explaining the Independent Commission on Banking's ring-fencing recommendation and rejection of Volcker rule); Jeremy Hill & Edite Ligere, Debevoise & Plimpton LLP Client Update, Financial Services (Banking Reform) Bill - Expect the Unexpected (Feb. 7, 2013) (on file with the Hofstra Law Review) (indicating that the U.K. government will implement the recommendations of the Independent Commission on Banking and bill introduced that does so).
\end{itemize}
prohibition and a comparative assessment by experts could be undertaken concerning which approach, prohibition or ring-fencing, was more effective, as well as whether such rules make much sense in the first place. Such an inquiry would raise the quality of decision-making.

Compounding the challenge of implementing the Volcker rule beyond its sheer intractability, is the fact that it is one of many Dodd-Frank "solutions" to conjectural problems, for as former Treasury Secretary Timothy Geithner succinctly put it, "Proprietary trading by banks played no meaningful role in the crisis."\footnote{M. F. GEITHEIN, STRESS TEST: REFLECTIONS ON FINANCIAL CRISES 414 (2014).} Although legislation plainly should seek to anticipate future financial crises and not solely address past ones, directing the focus of regulatory efforts on resolving known and pressing regulatory issues over speculative ones is self-evidently a more rational and prudent regulatory agenda, given scarcity in agency time and resources.

Notwithstanding a protracted drafting effort, there were still large unintended adverse consequences that became immediately apparent upon the Volcker rule's promulgation. Within a month, an interim rule was further adopted to provide an exception to the final rule's treatment of specified derivative instruments (collateralized debt obligations backed by trust-preferred securities) to mitigate an adverse impact on small and medium-sized banks, the principal holders of such assets. Without the exception, the banks would have had to take large losses writing down the securities, placing them at risk of violating capital requirements.\footnote{Matthew Goldstein, Regulators Ease Volcker Rule Provision on Smaller Banks, N.Y. TIMES, Jan. 15, 2014, at B2; Rob Blackwell, Volcker Rule Fix Will Aid Large and Small Banks, AM. BANKER (Jan. 14, 2014, 5:38 PM), http://www.americanbanker.com/issues/179_10/volcker-rule-fix-will-aid-large-and-small-banks-1064926-l.html.} The Rube Goldberg-like Volcker rule, which is over 900 pages, will, no doubt, produce further surprises, in addition to imposing substantial compliance costs.\footnote{Steve Culp, Final Volcker Rule Leaves Banks Facing Compliance Hurdles, FORBES (Dec. 17, 2013, 3:23 PM), http://www.forbes.com/sites/steveculp/2013/12/17/final-volcker-rule-leaves-banks-facing-compliance-hurdles (summarizing lengthy set of activities companies must undertake to "bring themselves into compliance with the Volcker rule"). Adding to the cost, at least in the immediate future, is the considerable uncertainty over how to comply with the rule, as the rule raises a host of interpretative questions without a transparent process for how to obtain clarity from enforcement agencies, including the issue whether when one agency provides an interpretation, other agencies will concur. Id.; see also Margaret E. Tahyar, Volcker Rule: Observations on Interagency FAQs, OCC Interim Examination Guidelines, HARV. L. SCH. F. CORP. GOVERNANCE & FIN. REG. (June 20, 2014, 9:02 AM), http://blogs.law.harvard.edu/corpgov/2014/06/20/volcker-rule-observations-on-interagency-faqs-occ-interim-examination-guidelines.} This is yet another consideration for why sunsetting would be of value in this context. The
Office of the Comptroller of the Currency estimates that the Volcker rule could cost the banking entities that it supervises upwards of $4 billion, a figure challenged by an SEC commissioner as, in all likelihood, far too low. As he put it: “Based upon the fact that this is not a serious analysis, I have no way to evaluate whether they are even in the right ballpark.” Sunsetting would provide an opportunity for Congress to obtain a handle on the true scope of the cost, and accordingly, revise the rule or direct regulators to do so, in order to produce a more cost-effective implementation or to adopt an entirely different approach to the problem.

One might contend that sunsetting is unnecessary for a salient rule such as the Volcker rule because it would attract congressional attention for consideration under the Congressional Review Act (“CRA”), under which, before a rule can take effect, it must be submitted to each chamber of Congress for review under an expedited legislative process that permits enactment of a joint disapproval resolution which, when signed by the president (or a veto is overridden), repeals the rule. However, as evidenced by the experience under the CRA—since enactment in 1996, only one rule has been disapproved and only two other disapproval resolutions have ever been passed by one chamber—the CRA is not an effective substitute for sunsetting.


172. Id.


174. §§ 801–802. The joint resolution must be adopted within sixty days of the submission, subject to extension if Congress is not in session. § 802(a). The statute requires consideration in the Senate under fast-track procedures, preventing a resolution from being held up in committee or filibustered. § 802(c)–(d). While there are no special procedural requirements for the House, a chamber receiving a disapproval resolution from the other chamber cannot bottle it up in committee. § 802(f)(1).

175. MORTON ROSENBERG, CONG. RESEARCH SERV., RL30116, CONGRESSIONAL REVIEW OF AGENCY RULEMAKING: AN UPDATE AND ASSESSMENT OF THE CONGRESSIONAL REVIEW ACT AFTER A DECADE 6 (2008) (stating that, as of March 31, 2008, Congress had received reports on 731 major rules and 47,540 non-major rules under the statute, 47 joint resolutions concerning 35 rules were introduced, and only one rule was disapproved, while 2 other rules were disapproved by the Senate alone). Moreover, the circumstances of the 1 disapproved rule, the Occupational Safety and Health Administration’s (“OSHA”) 2001 ergonomics standard, are considered to be “unique” and unlikely to be repeated. First, it was an extremely controversial proposal, due to its projected imposition of extremely high costs on business. Second, Congress had delayed adoption of any ergonomics standard for over a decade by appropriations riders. Third, the political situation changed completely within the statutory 60-day period for review, as the rule was adopted when the Clinton presidency was a lame duck, after the intervening election had given the Republicans
The problems with the CRA are considerable. First, the CRA permits only an up or down vote on a rule in its entirety, while at the same time prohibiting an agency from reissuing a “substantially similar” rule if a rule has been disapproved. This structure deters legislators from voting for a disapproval resolution, due to genuine concern that it would create an administrative vacuum, which could especially be a problem with a long and complicated rule, such as the Volcker rule, where parts of the rule may well be desirable to retain. Sunset review, by contrast, permits legislative tailoring: besides the yes or no approach of the CRA, a rule can be revised, retained, or repealed only in part. The ability to tailor regulation would facilitate a more deliberative review process than the CRA, by eliminating the contention that a rule must be left intact to prevent a regulatory void. Yet, as noted in the original chapter, although commentators skeptical of the value of sunsetting have missed it, sunsetting can be structured so as not to create a similar regulatory vacuum: the proposed action timetable to discharge a review panel’s recommendation from committees with jurisdiction and use of budget reconciliation procedures for consideration by the Senate eliminates regulatory repeal due to deliberate congressional inaction or obstruction by a legislative minority. Second, there is no mechanism

control of the presidency and both congressional chambers. Id. at 6, 14-15. Whether the rule could have been repealed without the CRA is unclear (the Republican control of the Senate was not filibuster-proof, although the disapproval resolution was supported by some Democrats), but as one commentator put it:

Because of the unique circumstances surrounding ergonomics, we cannot generalize from the impact of the CRA on ergonomics to conclude that the CRA has a significant impact on the regulatory process. . . . Even with [the conditions of a Republican presidency and Congress and many lame duck regulations], Congress did not attempt to overturn any of the many other major regulations issued by the Clinton administration in its waning months . . . .


176. ROSENBERG, supra note 175, at 22-23, 34-35.

177. Id. at 35. For instance, opponents of the resolution disapproving the ergonomics standard contended that it would not be possible for OSHA to write another rule were the resolution to pass. Shapiro, supra note 175, at 696.

178. See supra notes 86-87 and accompanying text. For critiques of sunsetting as facilitating repeal due to the legislative process, see Coffee, The Political Economy, supra note 63, at 1023-24, 1033; Brett McDonnell, Dampening Financial Regulatory Cycles, 65 FLA. L. REV. 1597, 1676 (2013). A total repeal due to Congress following the recommendation of an independent review panel should, by contrast, not be a matter of concern, as it is improbable that the process would be “captured,” the concern of Coffee and McDonnell regarding a failure by Congress to renew a statute, Coffee, The Political Economy, supra note 63, at 1023-24; McDonnell, supra, at 1636, due to the public nature of the process and the composition of the panel. Indeed, the independent panel’s sunset review would function more effectively than the expert studies that McDonnell favors, McDonnell, supra, at 1636-37, because its recommendations would have real bite. See supra notes
in the CRA by which Congress can readily obtain additional information to assess a rule, as would be provided by a sunset review’s panel of independent experts, which, again, should render decision-making of higher quality under sunsetting.\textsuperscript{179}

Finally, non-compliance with the requirements of the CRA is rampant, with agencies having failed to submit to Congress for review well over 1000 rules from 1998 to 2008, 101 substantive final rules in 2008 alone.\textsuperscript{180} Without notice of a rule, Congress cannot review it, yet neither the CRA, nor Congress through subsequent action, devised a mechanism by which un-submitted rules can be identified or compliance enforced.\textsuperscript{181} Agency non-compliance, and hence, absence of congressional review, would not occur under a sunsetting regime, given the starkly different default: a rule stays in existence if Congress does not act under the CRA, whereas it expires if Congress fails to act under sunsetting. In short, sunsetting provides a forcing mechanism for action that the CRA lacks, and combined with similar fast-track legislative procedures, the possibility of a minority preventing action will be vastly reduced. Although in theory, the CRA is an admirable concept through which Congress could exercise substantive control over poorly devised regulation, in practice, it has failed spectacularly, as commentators have noted, interpreting its disuse as evidence of total ineffectiveness.\textsuperscript{182}

B. Off-the-Rack Solutions: Reshuffling Bureaucratic Boxes and the Consumer Financial Protection Bureau

An illustration of the problematic nature of “off-the-rack” solutions fashioned in crisis-driven legislation is Dodd-Frank’s creation of the CFPB, which consolidated into one agency functions that had been

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\item[179.] For example, the statute requires an agency to provide a cost-benefit analysis with the submission of the rule and the Comptroller General (“CG”) to assess the agency’s compliance with that requirement, but the CG interprets the requirement narrowly: it simply reports whether the required cost-benefit analysis is present, and does not substantively evaluate an agency’s analysis. Rosenberg, supra note 175, at 3.
\item[180.] Sean D. Croston, Congress and the Courts Close Their Eyes: The Continuing Abdication of the Duty to Review Agencies’ Noncompliance with the Congressional Review Act, 62 ADMIN. L. REV. 907, 908 (2010) (citing Curtis W. Copeland, Cong. Research Serv., Report No. R40997, Congressional Review Act: Rules Not Submitted to GAO and Congress (2009)). As Croston notes, that estimate is likely to be an understatement, because an earlier congressional report suggested that “thousands” of rules had not been submitted for review. Id.
\item[181.] For possible reasons why Congress has not acted to remedy the compliance failures, see id. at 909-11.
\item[182.] Rosenberg, supra note 175, at 14-15; Croston, supra note 180, at 908.
\end{itemize}
\end{footnotesize}
allocated across seven federal agencies pre-crisis.\textsuperscript{183} Reshuffling bureaucratic boxes is a tried and true legislative response to crises. This is because it is a high visibility “solution”—it demonstrates that legislators are “doing something” in a way that is relatively easy for a poorly informed public to observe—and it combines two favored legislative responses to crises—an “off-the-rack” response conjoined with a delegation strategy, for the agency will bear responsibility for policy failures rather than legislators.\textsuperscript{184}

As often occurs with “off-the-rack” legislative responses to financial crises, Dodd-Frank’s administrative reorganization mismatches problem and solution because the U.S. regulatory architecture, and, in particular, absence of a designated consumer-product regulator, did not contribute to the financial crisis. For instance, housing bubbles produced severe financial crises in Iceland, Ireland, and Spain, despite the absence of subprime mortgage securitizations in those nations.\textsuperscript{185} In addition, there were meltdowns of financial institutions operating under distinctly different regulatory architectures (e.g., under both the multi-regulator, decentralized U.S. regime and the United Kingdom’s centralized one).\textsuperscript{186}


\textsuperscript{184} See supra notes 17-20, 28-35 and accompanying text. A number of financial regulatory agencies have been created in response to financial crises: the Federal Deposit Insurance Corporation (“FDIC”) in the Glass-Steagall Act, which responded to the bank failures in the 1930s and the Great Depression; the SEC in the Securities Exchange Act of 1934, which responded to the stock market crash of 1929 and the Great Depression; the PCAOB in the Sarbanes-Oxley Act, which responded to the 2001-2002 accounting scandals involving Enron and other companies; but also the Financial Stability Oversight Council in Dodd-Frank. The approach has also been used in response to nonfinancial crises, the most recent and notable example being the creation of the Homeland Security Department in the Homeland Security Act of 2002, in response to the September 11th terrorist attacks. And it would seem to be a stock response to crises beyond U.S. borders as well: the European Union created three new EU-level supervisory agencies in the wake of the crisis.

\textsuperscript{185} Carmen M. Reinhardt & Kenneth S. Rogoff, \textit{This Time Is Different: Eight Centuries of Financial Folly} 242, 244-45 (2009). For an analysis debunking the contention that the resets on exploding adjustable-rate mortgages caused a wave of foreclosures ushering in the financial crisis, see Foote et al., supra note 122, at 35-36.

\textsuperscript{186} While the regulatory structures differed substantially across nations, international bank capital requirements were harmonized under the Basel accords, and elsewhere I have contended that international harmonization contributed, in some measure, to the global financial crisis, by incentivizing banks to follow similar business strategies. See Romano, \textit{For Diversity}, supra note 7, at 13-20. But, the Basel accords did not harmonize how regulators should respond to bank failures, and different regulatory architecture did not produce quicker or cleaner resolutions to the global financial crisis.
Given the simultaneous regulatory failures and crises in nations with disparate financial products, markets, and regulatory structures, it is improbable that any bureaucratic reorganization would address the causes of the recent financial crisis, let alone prevent a future one.  

More particularly, it is quite implausible that the recent financial crisis would have been averted had there been an independent federal agency regulating consumer financial products: in discussing in his memoir the Administration’s decision to reorganize the government bureaucracy in the area of consumer protection, former Treasury Secretary Geithner does not mention the financial crisis once as a rationale or cause for the proposal. Rather, he refers to the President’s passion for “defending ordinary families from financial abuse,” dating back to outrage at his credit card rates when he was a community organizer, and to presidential aides’ political considerations, which included pleasing activists in the political base who were dissatisfied with Administration policies and promoting an issue that would resonate with the general public, thereby building support for the rest of the bill.

As is also quite typical for many components of crisis-driven legislation, the idea of a single federal agency with regulatory authority specifically over consumer financial products was not a new proposal carefully tailored to address an identified problem related to the financial crisis. Rather, it had been floated as a proposal by a policy entrepreneur prior to the onset of the crisis. Then-law professor Elizabeth Warren had advocated such an entity in a short 2007 article, by analogy to the federal agency protecting consumers from harm by physical products. The Bush Administration had similarly proposed such an entity in a March 2008 plan to consolidate the multiple regulators of financial institutions.

187. In addition, most of the new agency’s jurisdiction is over products and institutions that had no connection to the crisis. See, e.g., Todd Zywicki, The Consumer Financial Protection Bureau: Savior or Menace?, 81 GEO. WASH. L. REV. 856, 861-62 (2013). As Zywicki notes:

[T]here is absolutely no evidence that failures in consumer protection actually contributed in a major way to the crisis—indeed, many of the financial service providers swept under the CFPB’s umbrella, such as payday lenders and providers of cash remittances, had nothing at all to do with the financial crisis.

Id. at 861.

188. Geithner, supra note 168, at 403-04. The CFPB’s lax definition of a qualified mortgage, see supra note 126, and the fact that none of the subprime products sold to consumers were newly invented in the years before the financial crisis, Foote et al., supra note 122, at 35-36; supra note 117, further support the text’s counterfactual contention that had the CFPB predated the crisis, the financial meltdown still would have occurred.

which had been crafted prior to the onset of the financial crisis as a strategy to improve capital market competitiveness (but then repositioned as a solution to the financial crisis in the waning days of the Bush presidency). 190

Warren shortly thereafter co-authored a more extensive law review article with Oren Bar-Gill, which sought to provide a theoretical justification for her original proposal, fleshing out why consumers of financial products could need regulatory protection using concepts from behavioral economics. 191 Underscoring the fact that the genesis of the idea for the agency was independent of the financial crisis, the bulk of the 100 page-long article’s analysis focuses on consumer credit cards, which had no role in the financial crisis, with only a page or so discussing mortgages. 192 But the Bar-Gill and Warren article was identified by the Obama Administration as the source of its inclusion of such an agency in its legislative reform proposal to address the financial crisis. 193

The law review article did not, however, provide any institutional detail concerning the agency’s structure, except to state that it should be either an independent agency or a division within an existing agency, such as the Federal Reserve or Federal Trade Commission, while the Obama Administration proposal advocated creating an independent executive branch agency with a director and board of which one member would be the head of a prudential regulator. 194 Adapting the Administration proposal, the statute established an entity with a unique autonomous structure for a U.S. administrative agency. The CFPB is organized similarly to a cabinet department in the executive branch with a solitary director (in contrast to independent agencies that are typically structured as bipartisan commissions), but it is entirely independent of the executive: it was placed within the Federal Reserve System

192. Id. at 33-43, 46-55.
194. TREASURY DEP’T WHITE PAPER, supra note 193, at 55-56, 58; Bar-Gill & Warren, supra note 191, at 98.
("Fed") and in contrast to cabinet department secretaries, who serve at the President’s whim, the director has statutory removal protection (that is, serves a fixed term and can be removed only “for cause”).

Even more unique, the CFPB is also financially independent of Congress as it is not subject to the appropriations process: the director sets his own budget, which is funded by the Fed (capped at twelve percent of the Fed’s total operating expense). Moreover, Federal Reserve Board governors may neither intervene in the CFPB’s affairs; review or delay implementation of its rules; nor consolidate the bureau, its functions or responsibilities with any other office or division of the Fed. This regulatory setup has a bizarre whiff of a Kafkaesque bureaucracy, as the agency is formally insulated from democratic accountability.

195. 12 U.S.C. §§ 5491(a)-(b)(1), 5492(c)(2) (2012). As Todd Zywicki describes the evolution of the agency’s structure in the House bill, the agency was to be “a multimember commission funded in part by congressional appropriations,” but that was criticized, particularly by Republicans, who objected to the expense of creating a new agency, and the response, appearing in the Senate bill, was to “turn the agency into a bureau of the Federal Reserve.” Zywicki, supra note 187, at 860-61.


197. 12 U.S.C. § 5497(a), (c) (2012). Other regulatory agencies that are independently funded and not subject to the appropriations and budget processes—which tend to be prudential regulators of financial institutions such as the FDIC, as well as the Fed—have multimember structures. See Kirti Datla & Richard L. Revesz, Deconstructing Independent Agencies (and Executive Agencies), 98 CORNELL L. REV. 769, 793 tbl.3 (2013) (listing agencies with multimember structures); see also U.S. GENERAL ACCOUNTING OFFICE, GAO-02-864, SEC OPERATIONS: IMPLICATIONS OF ALTERNATIVE FUNDING STRUCTURES 11-12 (2002) (listing agencies with truly independent funding). In addition, in contrast to the broad grant of authority to the CFPB, those other agencies have narrower, and more technical purposes—prudential regulation and the setting of monetary policy—mitigating the accountability concerns raised by an agency’s independence from the appropriations process. See Note, supra note 196, at 1823-24.


199. Although the director must file semi-annual reports with Congress, there is little action Congress can take to alter policies with which it disagrees, unless the agency requires additional funds beyond the amount that it obtains from the Fed and fines that it imposes on regulated entities, and must request a supplemental congressional appropriation, as permitted under the statute. Zywicki, supra note 187, at 888-89. There is an inflation index adjustment for the CFPB expenses, § 5497(a)(2)(B) and as yet the CFPB has not sought supplemental funds: it requested less from the Fed to fund its operations than the transfer cap for fiscal year 2014 and projected it would do so as well for fiscal year 2015, whose respective budget caps are $608.4 million and an estimated $618.7 million. CONSUMER FIN. PROT. BUR., STRATEGIC PLAN, BUDGET, AND PERFORMANCE PLAN AND REPORT 20 (2014), available at http://www.consumerfinance.gov/strategic-plan-budget-and-performance-plan-and-report. Moreover, as discussed infra, at notes 204-28 and accompanying text, the director has been able to circumvent Congress’s effort to impose accountability in the specification of criteria to be used in rulemaking, which the courts could enforce, by regulating
The CFPB’s unique independent structure is combined with wide-ranging authority that is inherently in conflict with prudential regulation aimed at reducing bank failure, underscoring the reality that creation of the agency was an “off-the-rack” solution quite unrelated to the financial crisis. For instance, the statutory mission is to “ensur[e] that all consumers have access to markets for consumer financial products and services” that are “fair, transparent and competitive.”\textsuperscript{200} Such an objective suffers from the twin faults of over- and under-inclusiveness with regard to improving the financial regulatory architecture. It is under-inclusive by failing to target the market and product igniting the global financial crisis, the shadow banking sector, an institutional, not retail, market, and securitized mortgages, which were neither a consumer credit, nor even a retail, product. Yet, it is over-inclusive as the CFPB is given authority to regulate all forms of consumer credit, and not simply subprime mortgages, which were the only retail product implicated in the crisis (as the increase in subprime defaults was a trigger of the shadow banking run).\textsuperscript{201}

More importantly, the CFPB’s overlapping supervisory authority with banks’ prudential regulators is in intrinsic conflict given their distinctly different missions: safety and soundness of banks and the financial system versus consumer protection. Indeed, the CFPB’s supervisory process “flip[s] the safety and soundness [regulatory] paradigm on its head” by directing the most intensive scrutiny to banks’ most profitable financial products and services.\textsuperscript{202} Recognizing that the differing regulatory objectives of this dual supervisory system would lead to inevitable conflict, the statute permits banks to request that agencies coordinate if there is a supervisory conflict and, if they fail to coordinate, to appeal to an ad hoc panel of three regulators, which includes one regulator from each of the agencies that failed to coordinate.\textsuperscript{203} But, this setup is not a satisfactory resolution of the supervisory tension as such an appeals process would be both costly to

\textsuperscript{200} 12 U.S.C. § 5511(a) (2012).

\textsuperscript{201} For the contention that whatever the contribution of subprime mortgages to the financial crisis it was entirely unconnected to consumer protection issues and implicated solely prudential—safety and soundness—regulatory concerns, because consumers were rationally responding to incentives provided by lenders who were making unwise loans, and not consumers’ misunderstanding of the loan terms, see Zywicki, \textit{supra} note 187, at 910.


undertake and uncertain in outcome, given the panel composition (as it will likely only shift venue without resolving the turf battle the agencies could not negotiate in the first place), factors that discourage its use.

The most troubling aspect of the CFPB’s insulation from congressional oversight, however, is that it has facilitated policymaking that evades democratic accountability and that, on occasion, has been of questionable lawfulness. Namely, the CFPB has used notice and comment rulemaking only when it was statutorily required to adopt a rule.\(^{204}\) On virtually all other occasions, as far as I can determine, it has instead engaged in rulemaking by subterfuge, through the use of guidance (statements of “expectations”) and enforcement actions. These strategies enable the agency to evade not only engaging in the informed and transparent decision-making process that Congress sought in enacting the APA, but also complying with the specific criteria Congress enumerated in Dodd-Frank regarding factors it wished to inform the CFPB’s rulemaking, including a cost-benefit standard, as Congress did not similarly specify criteria for CFPB orders, guidance or enforcement actions.\(^{205}\)

The use of guidance and enforcement actions, rather than rulemaking, to effect regulatory policy further sidesteps an important safeguard of congressional delegation, which is maintained by judicial review. Political scientists have emphasized that a key mechanism by which Congress controls administrative agencies is its specification of administrative procedures.\(^{206}\) Because it cannot predict what regulatory issues will arise, and therefore, what substantive mandates to enact or require agencies to implement, Congress designs procedures that “assign

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\(^{204}\) Besides substantively mandated rules, e.g., 12 U.S.C. § 5532(b), (f) (2012) (mandating that the CFPB propose for public comment rules and model disclosures that integrate mortgage loan disclosures under the Truth in Lending Act and the Real Estate Settlement Procedures Act), the agency has also engaged in rule-making on a few other occasions when it could not otherwise exercise authority over specific institutions or products and a rule was necessary to establish its jurisdiction (that is, it had to follow a rulemaking procedure as prescribed by the statute), e.g., Defining Larger Participants of the Automobile Financing Market and Defining Certain Automobile Leasing Activity as a Financial Product or Service, 12 CFR §§ 1001, 1090 (2014) (expanding regulatory jurisdiction to define as a “covered market,” “a market for automobile financing,” automobile leases as “covered products,” and nonbank automobile lenders as “covered persons”). Because this market and the institutions offering these financial products and services would not be subject to the agency’s authority in the absence of its adopting a rule defining them to be covered, 12 U.S.C. § 5514 (2012), it could not regulate their activity by issuing a guidance document or bringing an enforcement action, its typical mode of operation as discussed in the text, and had no choice but to follow the prescribed rule-making process.


relative degrees of importance" to constituents, to participate in, monitor, and appeal the outcome of, administrative decisions. In creating the CFPB, Congress added specific procedural content going beyond APA general rulemaking procedures, specifying that the agency must consider the costs and benefits, not only to consumers, but also to the providers and offerors of financial products and services, in its rulemaking. Without judicial enforcement of those procedures, interested parties (e.g., constituents) cannot constrain agency outcomes to those Congress desired and political control over agencies is crippled. Using guidance to effectuate policymaking eviscerates the balance struck by Congress to maintain control over the agency because courts rarely characterize guidance as agency action subject to judicial review.

What I have described critically regarding the CFPB’s regulatory strategy could be considered totally prosaic as agencies regularly engage in the same regulatory strategies—statements of guidance and enforcement actions—to avoid the arduous strictures of notice and comment rulemaking, and administrative law scholars have long debated the degree to which this should be a matter of concern. But there is a crucial difference between generic agencies and the CFPB that should render the CFPB’s use of such tactics far more unsettling. An agency subject to an annual appropriations process, in contrast to the CFPB, cannot maneuver as freely, and aggressively use such strategies because congressional committees have leverage to enforce accountability through imposition of budgetary restrictions and non-statutory directives and instructions regarding specific expenditures.

207. Id. at 244, 264–66.
208. § 5512(b)(2).
209. McCubbins et al., supra note 206, at 263.
210. It is difficult to obtain judicial review of guidance decisions, as courts typically do not consider them to be final agency action—as required for standing by the APA—or otherwise ripe for review. Nina A. Mendelson, Regulatory Beneficiaries and Informal Agency Policymaking, 92 Cornell L. Rev. 397, 411 (2007). If an agency’s guidance is viewed as having “binding” effect, then a court may deem it a “legislative rule[]” and uphold a challenge against the agency for not following the notice and comment process. Nicholas Bagley & Helen Levy, Essential Health Benefits and the Affordable Care Act: Law and Process, 39 J. Health Pol. Pol'y & L. 441, 454 (2014). This area of law is, to put it mildly, quite murky; as one article puts it, “the line separating policy statements from legislative rules is not crisp,” and courts generally do not second-guess agencies’ choice of regulatory tool. Id.; see Lisa Schultz Bressman, Beyond Accountability: Arbitrariness and Legitimacy in the Administrative State, 78 N.Y.U. L. Rev. 461, 534 (2003).
211. Mendelson, supra note 210, at 403–10.
212. For a general discussion of the competing considerations, see Bressman, supra note 210, at 541–44, and for a discussion of the considerations focused on guidance documents, see Mendelson, supra note 210, at 406–13.
accompanying budget legislation. The incentive effect of the CFPB’s unique organizational structure upon its choice of policy tools could, as I think it should, be revisited were financial regulation subject to sunsetting.

Two examples will suffice to illustrate the CFPB’s problematic employment of regulatory strategies that enable it to obtain the outcome it desires regarding regulated entities’ behavior, without the use of rulemaking. First, the agency staff believed that credit card add-ons, such as payment for lost wallet protection, had little or no value and should not be sold. This is, of course, possible, but a contested assertion.

For a discussion of appropriations committee oversight techniques, and their use to delay the SEC’s implementation of the Sarbanes-Oxley Act’s internal controls provision to small firms, see Romano, Does the Sarbanes-Oxley Act, supra note 11, at 284-86. For a parallel notion that the structural accountability of an agency affects its incentives to engage in robust informed decision-making, and is a matter of policy concern, see Catherine M. Sharkey, State Farm ‘with Teeth:’ Heightened Judicial Review in the Absence of Executive Oversight 110-11 (N.Y.U. Sch. of Law Pub. Law & Legal Theory, Working Paper No. 14-15, 2014), available at http:lsr.nellco.org/nyuplltwp/463 (contending that the factual determinations of independent agencies that are not subject to executive oversight should receive less judicial deference because they have insufficient incentives to engage in comprehensive cost-benefit analysis, compared to agencies which know their rules must be reviewed by the Office of Information and Regulatory Affairs in the Office of Management and Budget).

Congress could, of course, revisit the CFPB’s structure without sunsetting. Indeed, Republicans have introduced several bills, see Andrew J. Buczek & Haydn J. Richards, Jr., House Financial Services Subcommittee Holds Legislative Hearing on CFPB Proposals, CONSUMER FIN. SERVS. L. BLOG (May 27, 2014), http://www.cfs-lawblog.com/House-Subcommittee-Hearing-CFPB-Proposals, one of which passed the House on a nearly party line vote, to restructure the agency. Final Vote Results for Roll Call 85: Consumer Financial Protection Safety and Soundness Improvement Act of 2013, HOUSE.GOV (Feb. 27, 2014, 6:39 PM), http://clerk.house.gov/evs/2014/roll085.xml (showing that all Republicans and ten Democrats voted for the Bill). But no bill restricting the CFPB, including the house-passed one, has moved in the Senate, and President Obama would surely veto any such legislation. As a practical matter, the many veto points in the legislative process, render reorganization of the CFPB questionable in the absence of either another crisis leading to calls for a bureaucratic rearrangement, or an election sweep in which the Republican Party, whose members uniformly opposed the agency’s creation, took control of both chambers and the presidency.

Although the agency’s objections to the products were stated in terms of the use of “deceptive” or “high-pressure” marketing tactics, What Are Credit Card “Add-on Products,” CONSUMER FIN. PROT. BUREAU (Mar. 1, 2013), http://www.consumerfinance.gov/askcfpb/1541/what-are-credit-card-add-products.html, the detailed procedures it identified for banks’ marketing of such products to not be considered deceptive were so burdensome that it is plain that the agency’s goal was to eliminate the products entirely, an objective that was achieved. See infra note 218 and accompanying text.

As Alan Schwartz has noted, a problem with substantive rules restricting consumer contracts (as opposed to disclosure regulation) is that both rational and irrational consumers may prefer the same contracts, such as a credit card add-on, but as the regulator can observe only contracting choices, not preferences, it cannot distinguish irrational from rational consumers by simply observing market choices. As a consequence, restricting the consumer’s ability to contract (e.g., purchasing the add-on), may decrease, not increase welfare, as it might be rationally chosen.
Rather than adopt a rule prohibiting or restricting their sale, it brought three enforcement actions against credit-card providers for improper marketing and published a list of “expectations”—what it would look for in evaluating the product. In response to those agency actions, the three largest banks, followed by other institutions (none of whom were the subject of the enforcement actions), “voluntarily” cancelled the products. It is inconceivable that the CFPB’s heavy-handed use of its powers is the approach that Congress had in mind when it directed the agency to consider the “potential benefits and costs to consumers and covered persons [financial institutions], including the potential reduction of access by consumers to consumer financial products or services resulting from such rule,” as it conveyed a preference that the agency engage in cost-benefit analysis and not restrict the financial products available to consumers.

Second, the CFPB staff believes that data indicates that automobile dealers charge higher interest rates to women and minorities than to white men (although it did not make public the supporting data, which was derived from proxies—not actual sales data—to estimate discriminatory dealer practices, because the ethnicity of car buyers is not recorded). But, Dodd-Frank expressly prohibited the agency from regulating automobile dealers. The agency, therefore, adopted the

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218. See Karen Weise, The Consumer Finance Watchdog Is Having an Impact, BLOOMBERG BUSINESSWEEK (Jan. 10, 2013), http://www.businessweek.com/printer/articles/90258-the-consumer-finance-watchdog-is-having-an-impact. The three banks subject to the enforcement actions—one of which was for failure to supervise a third-party vendor and not for any failures in its own marketing—were required to pay in aggregate $101.5 million and $435 million in refunds to customers. Id.


220. Kim B. Perez, Note, The CFPB “Indirectly” Regulates Lending Through Auto Dealers, 18 N.C. BANKING INST. 399, 418 (2014) (showing that the CFPB guidance bulletin relied on mathematical proxies for race and ethnicity, using Social Security Administration and Census Bureau data to estimate the probability someone is of a racial or ethnic minority based on their surname and geographic location, and then used the proxies to determine where consumers might experience discrimination based on interest rates that proxy-determined minorities received); Your Car Dealer Must Be a Racist, WALL ST. J., Nov. 15, 2013, at A14.

221. 12 U.S.C. § 5519 (2012). The statute contains exceptions to the exclusion of auto dealers from the CFPB’s regulatory authority, but none of the exceptions apply to auto loans that the dealer provides through a bank or that are securitized, the subject of the guidance.
tactic of providing warning or "guidance" in a bulletin issued to banks, which are subject to its authority, that it would enforce anti-discrimination laws against banks that purchased auto loans from auto dealers, claiming that a disparate impact is sufficient to find a violation (as the agency did not have any evidence of discriminatory intent by the dealers). 222

The guidance further suggested that banks could avoid an enforcement action if they imposed controls on, and monitored, dealer markups, and then took prompt corrective action against miscreant dealers, or, better yet, if they charged flat fees to eliminate dealer discretion as to the interest rate, which was the industry practice regarding dealer compensation (lenders shared profits with dealers as a function of the loan's interest rate). 223 Banks rationally responded to the "guidance," which was provided in the shadow of an implicit supervisory threat of adverse regulatory action if they did not comply, by telling dealers that if they did not comply, they would impose flat fees (which was the CFPB's desired objective). 224

The discrimination standard that the CFPB applied in the bulletin, a disparate impact rather than disparate treatment (i.e., intent) standard, in all likelihood, as confirmed by the government's litigation strategy, would not stand up to judicial review. The Supreme Court's jurisprudence has evolved to require an intent standard, and as a consequence, in recent years, whenever the Court has granted certiorari on a disparate impact challenge, the federal government has settled to avoid a possible adverse decision that rejected the disparate impact rationale. 225 Also problematic is the CFPB's interpretation in the bulletin of who is a "creditor" under the fair lending law. Although the agency contended that it was not reinterpreting or making new "law," which

222. See generally CONSUMER FIN. PROT. BUREAU, INDIRECT AUTO LENDING AND COMPLIANCE WITH THE EQUAL OPPORTUNITY ACT (2013) [hereinafter CONSUMER FIN. PROT. BUREAU, INDIRECT]; CFPB to Hold Auto Lenders Accountable for Illegal Discriminatory Markup, CFPB (Mar. 21, 2013), http://www.consumerfinance.gov/newsroom/consumer-financial-protection-bureau-to-hold-auto-lenders-accountable-for-illegal-discriminatory-markup. No doubt, the CFPB's disparate impact approach looks to a decades-old series of settlements of Department of Justice ("DOJ") prosecutions under the fair lending laws that were based on a disparate impact standard. See Zywicki, supra note 187, at 923. The disparate impact standard is a controversial theory, which the DOJ has assiduously avoided subjecting to Supreme Court review. See infra note 225 and accompanying text.

223. CONSUMER FIN. PROT. BUREAU, INDIRECT, supra note 222, at 4-5.

224. Your Car Dealer Must Be a Racist, supra note 220. The agency brought enforcement actions against four banks under the Bulletin. Perez, supra note 220, at 399 & n.5.

225. Perez, supra note 220, at 424. As Perez notes, the statutes under which the Supreme Court has upheld a disparate impact are those that contain the word "affect," language not contained in the lending statute. Id. at 423.
conveniently eliminated the need for following rulemaking procedures, the interpretation would seem to a fair-minded observer, in fact, to be quite novel, as neither auto dealers’ markups nor indirect lenders had previously been understood to fall within the statutory definition.\footnote{226}{Id. at 412-14. The CFPB’s claim regarding the lack of novelty was provided in response to a query from members of Congress concerning why it had acted on the subject by issuing guidance rather than a rule. \textit{Id.} at 412-13.}

By engaging in backdoor rulemaking through use of guidance (its supervisory authority over banks), the CFPB sought to restrict auto dealers’ negotiations with customers with regard to financing terms, and to impose a significant change in their business model, as the vast majority of auto sales are financed.\footnote{227}{As the Wall Street Journal explained, flat fees cap dealers’ profits on loans, and thereby, limit their flexibility to lower an interest rate on one sale to compete with an offer from another dealer and to raise an interest rate on another sale to boost profits. \textit{Your Car Dealer Must Be a Racist}, supra note 220.} This was done, despite an express restriction of jurisdiction over the subject matter, while employing a highly problematic, possibly lawless, interpretation of the statute and without publicly disseminating the data upon which its decision was based. Had the CFPB engaged in rulemaking, it would have had to explain itself and publicly release the data to justify the rule (if only to seek to avoid a defeat were it to be challenged in court).\footnote{228}{See Perez, supra note 220, at 415. It seems probable that the cost-benefit criteria would not have been easily satisfied as the dealer compensation policy promoted by the guidance may well increase lending costs. As Perez notes, if dealer discretion on rates is maintained, then banks must engage in substantial monitoring, imposing considerable costs, which will increase the rate of interest banks require, and if instead discretion is replaced with flat fees, then dealers will lose the flexibility of trading interest rates off against purchase price, with the upshot that they will be less likely to offer lower purchase prices. \textit{Id.} at 425-27. Were a bank to challenge an enforcement action brought against it for not complying with the guidance, then the agency would have to justify the rule just as it would have had to do for a challenged rulemaking. But, as is typical for financial institutions subject to regulatory enforcement actions, it does not appear that any entity has chosen to litigate, rather than settle.}

It is possible that the CFPB’s determinations that credit card add-ons and auto dealer interest rate markups are questionable products and practices that should be prohibited are correct, although I am skeptical of such a conclusion.\footnote{229}{See \textit{id.} at 425-26 (discussing benefits to consumers from dealer participation in lending, including data indicating that interest rates on indirect loans even with a dealer markup, were one percent lower than rates on direct bank loans).} But, these are large and substantive policy matters that are most properly calibrated through rulemaking, with public participation, as contemplated by Congress, in which the agency has to develop a record and publicly justify its decisions, that is, provide evidence that credit card add-ons have no or little value and that auto dealers are discriminating.
Most important, these two examples are instances where both sunsetting and experimentation would have been of considerable benefit. Namely, sunsetting would reduce the possibility that the CFPB could persistently evade the more demanding notice and comment procedures. For if the agency were a sunset agency, then when Congress had to revisit its authorization, it could impose specific rulemaking requirements, or restrict the scope of the CFPB’s authority, and, further, reevaluate whether the structure of the agency made much sense in the first place. The agency would also have an incentive to behave responsibly, knowing that its decisions would be publicly scrutinized by legislators during reauthorization, a context in which there could be serious consequences to the agency for questionable conduct, in contrast to their present posture. Moreover, restrictions on credit card add-ons and imposing flat fees on auto dealers are the type of regulation for which well-crafted experiments could prove to be fruitful: a subset of banks could be randomly selected to adopt such policies, and another subset could be randomly selected to take a different approach, such as improved disclosure, and the findings then used to inform policymaking.

It would be a mistake to conclude that implementation difficulties and problematic regulation are occasional occurrences that can be ameliorated over time, by regulators dutifully ironing out flaws, and thereby negate a need for sunsetting. Experience teaches otherwise: the status quo is sticky, whether it be legislatively or administratively.

230. McCarty et al. assert that Congress is the problem in resolving financial crises, contending that it does not enact effective reform regulation because of interest group lobbying and polarized politics. McCARTY ET AL., supra note 150, at 57-61, 72-75. While this Article similarly contends that Congress’s emergency financial legislation is deeply problematic, the explanation of its failure articulated here is altogether different from McCarty et al. Their analysis assumes that the cause of the financial crisis was a “Republican” ideology of free markets and deregulation and, consequently, that legislative and regulatory initiatives of congressional Democrats are presumptively superior to the status quo, with the proviso that they should not provide regulatory discretion because industry will capture implementation. Id. at 38-42, 123-26. As students of the recent financial crisis are well aware, there is, in fact, plenty of blame to go around regarding the crisis across the political spectrum and across all institutions, public and private. See, e.g., supra notes 137, 140. Moreover, given the global scope of the crisis—with banks imploding in countries with diverse political leadership and regulatory institutions—what occurred cannot, in a simple-minded fashion, be ascribed solely to the “ideology” of a particular domestic political party. For a list of common fundamentals across diverse nations characterizing the financial crisis, such as real estate bubbles, current account deficits, and large capital inflows (factors experienced in Iceland, Ireland, New Zealand and Spain, as well as the United States), see REINHART & ROGOFF, supra note 185, at 242-45.

231. For a brief discussion regarding the concern that firms in an experiment may act strategically, see supra notes 113-14 and accompanying text.
formulated. Regulations are rarely revisited and it takes an inordinately long time, sometimes decades, despite a policy consensus regarding the inappropriateness of a particular regulatory solution, for legislators to address the issue.232

In fact, congressional mandates to agencies to reevaluate existing regulations on a regular basis would appear to be totally ignored with impunity.233 A study of the statutory requirement that agencies periodically review existing rules for their impact on small business found that most of the time agencies did not even conduct the required review, and when they did, they rarely took any action beyond publishing a notice that the review had been conducted, or they revised regulations to increase, rather than reduce, as the statute intended, the burden on small firms.234 Moreover, even when regulators are repeatedly prodded by Congress to revisit a specific regulation that is thought to be flawed, regulators are congenitally conservative and tend to resist.235 And their technical staff—positioned in an organizational hierarchy in which there can be adverse professional consequences if they are not responsive to their superiors’ preferences—cannot be relied upon to produce a balanced assessment concerning whether a rule should be revised or repealed, even if they have a sophisticated appreciation of a problem. It is simply in the nature of agency staff reports to perceive the task at hand as rationalizing agency policy. The report of an independent sunset review panel of experts would not suffer from that problem. The panel’s experts would not be beholden to a bureaucracy and would have professional reputations at stake, along with presumed diversity in perspectives, given the appointment process, that would minimize the possibility of a purely rationalizing report.

Agency use of experts when compelled by judicial review is no less likely to be problematic. An illustration demonstrating the difficulty of relying on internal experts’ evaluation is its use by the SEC to support an effort to require mutual fund boards to have a supermajority of independent directors. After the rule was rejected by the U.S. Court of Appeals for the D.C. Circuit for not having met a requisite cost-benefit standard,236 the Commission had its Office of Economic Analysis

232. See, e.g., supra notes 10-12 and accompanying text.
234. Id. at 1215, 1218-19.
235. For an illustration of this tendency from Sarbanes-Oxley, see text accompanying notes 82, 242.
undertake a literature review to assist in the remanded rulemaking.\textsuperscript{237} Although the report is a careful evaluation of the literature, in a supplemental memo, the Chief Economist sought to explain it away, as it was inconsistent with the premise of the proposed rule.\textsuperscript{238} The memo explained that, despite the absence of evidence in the literature that more independent boards reduced fees or improved performance, a failure to find a relation does not mean there is no relation, given the limits of standard statistical methods.\textsuperscript{239} This observation is correct so far as it goes, but it also proves too much, as we must do the best that we can with the information that we possess when a judgment must be made. It is self-evident that the Chief Economist felt pressed to interpret the data in the report in the supplemental memo to assist the agency’s effort to build a record that would support retaining the original rule and that could pass judicial scrutiny.

C. A Note on Sarbanes-Oxley’s Lessons for Dodd-Frank

It could be asserted that the Sarbanes-Oxley Act is a good contrast to Dodd-Frank because its regulatory requirements were implemented in short order after enactment. Yet, Sarbanes-Oxley provides a cautionary tale for relying on an agency to revisit a crisis-driven legislative directive: in the SEC’s problematic implementation of section 404,\textsuperscript{240} the requirement that managers certify the effectiveness of their firm’s internal controls, and that auditors attest to that certification. Complying with section 404 was quite costly for all companies, but disproportionately far more so for smaller firms, and the SEC initially postponed the provision’s application to the smallest firms (market cap under $75 million), but declined to adopt the recommendation of its own advisory committee to exempt those firms permanently.\textsuperscript{241} Small firms

\textsuperscript{237} Memorandum from Chester Spatt, Chief Econ., to Inv. Co. File S7-03-4, at 1-2, 12-23 (Dec. 29, 2006) (on file with the Hofstra Law Review).
\textsuperscript{238} Romano, Does the Sarbanes-Oxley Act, supra note 11, at 300.
\textsuperscript{239} Id.
\textsuperscript{241} For a detailed narrative of the saga of the SEC’s approach to section 404, see Romano, Does the Sarbanes-Oxley Act, supra note 11, at 239-44. The SEC’s original estimate of per-firm annual compliance costs of $91,000 was wildly inaccurate by orders of magnitude and despite declining from early per-firm compliance costs in excess of $1 million, it is still well above that amount. OFFICE OF ECON. ANALYSIS, STUDY OF THE SARBANES-OXLEY ACT OF 2002 SECTION 404 INTERNAL CONTROL OVER FINANCIAL REPORTING REQUIREMENTS 4-5 (2009) [hereinafter OEA, STUDY OF 404], available at http://www.sec.gov/news/studies/2009/sox-404_study.pdf; Romano, Does the Sarbanes-Oxley Act, supra note 11, at 240-41.
had a better hearing in Congress, which threatened the SEC with budgetary restrictions were it to let the delayed application expire as planned, and in response, then-SEC Chairman Christopher Cox agreed to maintain the postponement and conduct a cost-benefit study of the statute, and the budget restriction was accordingly eliminated from the appropriations bill in conference.\(^{242}\)

The promised study of section 404's effects was undertaken by economists in the SEC's Office of Economic Analysis, and completed under Cox's successor, but when data indicated a negative impact on small firms, the SEC's accountants apparently found the findings objectionable, and presumably the Chairwoman did too, for the report attempts to provide a positive assessment, and only by combing through the 100-plus page study can one piece together the negative findings.\(^{243}\)

More to the point, when in Dodd-Frank, after eliminating the provision's applicability to the smallest firms, Congress instructed the SEC to conduct a study of the compliance burden of section 404 for small firms that Dodd-Frank did not exempt (market cap between $75 and $250 million),\(^{244}\) this time the analytical work was given to the Office of the Chief Accountant, and not the economists, ensuring the study would—as it predictably did—advise against extending the exemption to more firms.\(^{245}\)

A recent article by John C. Coates IV and Suraj Srinivasan reviewing the empirical academic literature that has sought to assess the impact of Sarbanes-Oxley over the past decade, and concluding that

\(^{242}\) Romano, *Does the Sarbanes-Oxley Act*, supra note 11, at 284.

\(^{243}\) *See generally* OEA, STUDY OF 404, *supra* note 241. It was rumored that the release of the SEC study was delayed so that the text could be recrafted to place the statute in a positive light. Some evidence of the commission's disapproval of the original study is that the agency's publication clearance review process would appear to have delayed the release of a scholarly paper derived from the study's data: the paper was only recently published, years after the SEC study was completed and Congress had taken action on section 404. *See generally* Cindy R. Alexander et al., *Economic Effects of SOX Section 404 Compliance: A Corporate Insider Perspective*, 56 *J. ACCT. & ECON.* 267 (2013). The SEC accountants' objections are not surprising, as the recommendation of the SEC's advisory committee to exempt small firms was vigorously opposed by the two accountants on the committee, a position at one with the profession's financial interest. *E.g.*, Romano, *Does the Sarbanes-Oxley Act*, supra note 11, at 240 n.39, 241 (indicating accountants on the advisory committee dissented from recommendation to exempt small firms and providing data that audit fees tripled as a percentage of revenue for small public companies before and after Sarbanes-Oxley).


“[o]n balance, research on the Act’s net social welfare remains inconclusive,”\textsuperscript{246} does not alter this Article’s evaluation of the need for sunsetting that statute, along with other crisis-driven financial legislation. Although I believe that Coates and Srinivasan’s assessment of the literature is mistaken as it both overstates potential benefits and downplays or misses research with negative findings,\textsuperscript{247} this Postscript is not the proper forum for providing a critique of their literature review. For accepting Coates and Srinivasan’s assessment and conclusion, for argument’s sake, only serves to bolster this Article’s advocacy of the importance of engaging in experimentation for financial regulation. Namely, the inability to conclude that Sarbanes-Oxley has produced a net benefit highlights how crisis-driven regulation could benefit from experimentation. If the SEC had structured implementation of the statute’s provisions, such as the independent audit committee mandates

\begin{itemize}
\item \textsuperscript{247} For example, the authors omit from their review, articles indicating that Sarbanes-Oxley’s cost outweighs the benefits for foreign cross-listed firms—firm samples that tend to provide cleaner results than using samples of U.S. firms because they can provide controls of comparable companies not affected by the statute. E.g., Xi Li, \textit{The Sarbanes-Oxley Act and Cross-Listed Foreign Private Issuers}, 58 J. ACCT. & ECON. 21, 23-24, 37 (2014); Kate Litvak, \textit{The Effect of the Sarbanes-Oxley Act on Non-US Companies Cross-Listed in the US}, 13 J. CORP. FIN. 195, 196-98 (2007); Kate Litvak, \textit{The Long-Term Effect of the Sarbanes-Oxley Act on Cross-Listing Premia}, 14 EUR. FIN. MGMT. 875, 880, 919 (2008). In addition, despite the seemingly modest conclusion quoted above, the text of the literature review places the statute in a more positive light. See Coates IV & Srinivasan, supra note 246, at 31, 59-60. This is conveyed through statements that seemingly broadly discredit prior critiques of Sarbanes-Oxley related to its impact on corporate law, but that are then followed by qualifiers cabining the broad statements to reference only one provision, or only one out of many critics’ contentions, such that a non-specialist could easily miss the caveat and pick up only the broader statement. Id. at 14. For example, the authors state that data on firms’ disclosures of material weaknesses under section 404, suggests that for a significant number of public companies, SOX’s section 404 has functioned at least in part in a ‘comply or explain’ fashion, contrary to strong characterizations of that part of the law as ‘mandating’ corporate governance changes.” Id. But, a consumer of the literature reviewing the pre-publication article gleans from that statement the following mistaken conclusion: “Another concern was SOX would change financial regulation from disclosure to prescriptive command-and-control. But the authors conclude that it is a ‘comply or explain’ regime.” Peter van Doran, \textit{Working Papers. Corporate Accounting, SOX After Ten Years: A Multidisciplinary Review}, in \textit{REGULATION} 68 (2014). He missed the critical word “part” qualifying the sentence, which was referencing a disclosure provision that was not one of the many mandatory corporate governance provisions that are the source of that specific criticism of Sarbanes-Oxley, nor did Coates and Srinivasan identify any of those provisions as “comply or explain” and not mandatory ones. See, e.g., Romano, \textit{The Sarbanes-Oxley Act}, supra note 1, at 1529, 1533, 1538, 1540, 1594-95 (critiquing move to mandatory rules in Sarbanes-Oxley, that consisted of audit committee requirements, corporate loan prohibition, prohibition of auditor provision of non-audit services, and officer certification of financial statement accuracy).
\end{itemize}
or auditor attestation requirements, as randomized experiments, then we could have more accurately measured the net benefit or cost of the requirements.248

Accepting their assessment and conclusion for argument’s sake also underscores the need for sunsetting. Sunsetting would provide the agency with an incentive to get things right and to operate with less of a closed bureaucratic mindset regarding experimentation when implementing emergency-driven legislation,249 as the agency would need to develop the highest quality information available. For if, in a sunset review occurring seven to ten years after implementation (the time range of Coates and Srinivasan’s assessment) the net benefit were still inconclusive, then substantial revision of the delegating statute, reversing the agency’s previous endeavors would be a more probable outcome.

P.III. CONCLUSION

The post-enactment experience of the two most recent crisis-driven statutes concerning financial regulation, Dodd-Frank and Sarbanes-Oxley, underscores the importance of including in such legislation, mechanisms—sunsetting and regulatory experimentation—to ensure that there will be a serious, comprehensive reassessment after a fixed period, and that information regarding the impact of regulatory alternatives can be gathered in the interim to aid in the reassessment. The implementation

248. The article by Coates and Srinivasan adopts the position on regulatory experimentation I advanced in Regulating in the Dark, reprinted herein at supra Part III.B. See Coates IV & Srinivasan, supra note 246, at 57-58 (arguing that increased randomized trials would allow for a greater ability to assess causal effects of the Sarbanes-Oxley Act).

249. The one instance of a randomized experiment undertaken by the SEC, involving the short sale uptick rule, was directed at a long-standing regulation, and not undertaken to ascertain how best to implement a new, crisis-driven legislative directive. See supra note 113. The SEC has supported pilot programs, which are sometimes referred to as “experiments.” See Dave Michaels, Exchanges Get Test to Curb Dark Trading in SEC Program, BLOOMBERG (June 25, 2014), http://www.bloomberg.com/news/2014-06-24/exchanges-get-test-to-curb-dark-trading-in-sec-program.html (describing new SEC initiative to permit exchanges to test restrictions on the tick size of small stocks approach to tick size as “experiment”). However, they are not always experiments in the sense used here, as they do not always compare the outcomes of controlled and “treated” firms, chosen by random, to permit a gold standard evaluation of the program. Still, they have an experimental flavor, in that by being structured as a pilot, the program’s outcomes will be evaluated to determine if it should be retained (and thus expanded to all firms) or rescinded. Pilot programs are not always agency-inspired. The newly launched tick size pilot program, for instance, follows upon the recommendation of an SEC advisory committee following an agency report on the impact of decimalization ordered by Congress, along with a GAO report and a report of a Treasury Department task force. SEC. & EXCH. COMM’N, ORDER DIRECTING THE EXCHANGES AND THE FINANCIAL INDUSTRY REGULATORY AUTHORITY TO SUBMIT A TICK SIZE PILOT PLAN 6-8, 10-12 (2014). Moreover, paralleling the uptick experiment, SEC pilot programs also address long-standing regulations.
of the statutes has been replete with instances of the sort of errors that inevitably arise from crisis-driven legislation, as it is enacted at a time when information necessary to devise suitable solutions is unavailable. That state of affairs permits agenda-setting legislators to adopt preferred policy entrepreneurs' "off-the-rack" solutions, which are often not well-matched to the problems at hand, along with extensive, albeit poorly-thoughtout, delegation, which result in costly market adjustments and adverse unintended consequences with questionable social benefits. Still, sunsetting and regulatory experimentation are not panaceas. Legislators must conscientiously revisit the statute and its implementation, with the assistance of the analyses of independent experts, and regulatory experiments must be well-crafted to inform a reassessment. Nonetheless, sunsetting and regulatory experimentation are the best tools we possess to mitigate the perils that arise when one is regulating in the dark.