December 7, 2015

VIA ELECTRONIC SUBMISSION

Consumer Financial Protection Bureau

Attn: Richard Cordray, Director; Mark Morelli, Attorney-Adviser, Office of Regulations

Re: Proposals Under Consideration to Limit Certain Practices for Payday, Auto Title, and Similar Loans

The Institute for Policy Integrity respectfully submits the following recommendations to the Consumer Financial Protection Bureau ("CFPB" or the "Bureau") regarding its proposals under consideration to limit certain practices for payday, auto title, and similar loans.[1]

The Institute for Policy Integrity at New York University School of Law[2] is a non-partisan think tank dedicated to improving the quality of government decisionmaking through advocacy and scholarship in the fields of administrative law, economics, and public policy.

While CFPB's proposals include a variety of promising ideas, the Bureau should take the following steps to ensure that it develops the best possible regulatory framework:

- First, as an additional regulatory tool, CFPB should consider using its authority under section 1032 of the Dodd-Frank Act to require better information disclosures. In particular, CFPB should consider requiring disclosures that specifically target common consumer errors. It should also consider requiring disclosures that inform consumers about more-affordable credit alternatives.

- Second, CFPB should more clearly define its goals. In particular, CFPB should distinguish between efficiency goals, such as correcting market failures, and distributional goals, such as addressing regressive cross-subsidies from less-financially-sophisticated to more-financially-sophisticated households. While CFPB should pursue both efficiency and distributional goals, defining its objectives more precisely will allow the Bureau to better evaluate its proposals.

- Third, in order to determine how its proposals affect economic efficiency, CFPB should consider their costs and benefits to society at large, and not just their costs and benefits to consumers and lenders, as is the Bureau's current practice.

- Finally, while CFPB has stated that it will not expand the proposals under consideration to cover pawn lending and overdraft services, the Bureau should nevertheless carefully consider the extent to which its proposals will push consumers to meet their credit needs through pawn lending, overdraft services, and other products and services not covered by its current proposals.

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[1] CONSUMER FINANCIAL PROTECTION BUREAU, SMALL BUSINESS ADVISORY REVIEW PANEL FOR POTENTIAL RULEMAKINGS FOR PAYDAY, VEHICLE TITLE, AND SIMILAR LOANS: OUTLINE OF PROPOSALS UNDER CONSIDERATION AND ALTERNATIVES CONSIDERED (2015), *available at* http://files.consumerfinance.gov/f/201503_cfpb_outline-of-the-proposals-from-small-business-review-panel.pdf [hereinafter "CFPB OUTLINE"].

[2] This document does not purport to present New York University School of Law's views, if any.

I. Summary of the Proposals Under Consideration

The proposals under consideration would regulate two categories of consumer financial products. First, the proposals would regulate "covered short-term loans," which are short-term credit products with contractual durations of 45 days or less, including: single-payment payday loans with one lump-sum payment typically due within a few weeks or a month; deposit-related credit products repayable within a short period of time (including deposit advance products); and some auto title loans where lenders place a non-purchase money lien on a consumer's vehicle. Second, the proposals would regulate "covered longer-term loans," which are longer-term credit products with an all-in annual percentage rate in excess of 36 percent for which the lender obtains a non-purchase money lien on the consumer's vehicle or the right to collect repayment from the consumer's account or paycheck.

The proposals under consideration would address four main concerns:

First, lenders' failure to assess whether consumers will be able to repay loans while meeting other financial obligations and living expenses results in many consumers taking out unaffordable loans. Accordingly, CFPB is considering requiring that lenders make careful ability-to-pay determinations before lending in most circumstances.

A second, related worry is that consumers who cannot repay their initial loans end up in a destructive cycle of reborrowing—in some cases incurring finance charges that exceed their original loan amounts. Thus, CFPB is considering limiting the circumstances under which lenders may repeatedly lend to the same consumer.

A third concern is that certain practices that lenders use to collect payment from consumers' accounts may cause substantial harm to consumers. To address this problem, CFPB is considering requiring lenders to give written notice to consumers before initiating collection attempts from their bank accounts. Further, lenders would be prohibited (without consent) from attempting to collect from a consumer's account after two consecutive attempts have failed.

Finally, CFPB is concerned about preserving consumer access to affordable short-term credit. Thus, CFPB is considering allowing any lender to offer loans on the terms of the NCUA *Payday Alternative Loan Program*, a highly structured lending program for consumers with low or no credit. Currently, that program is limited to federal credit unions.

II. As an Additional Policy Tool, CFPB Should Consider Information Disclosures

The proposals under consideration employ several innovative strategies. The academic literature suggests that these approaches may yield better results than more restrictive policy tools, such as interest rate caps or outright bans.[3] There is, however, an additional regulatory strategy that CFPB should consider: requiring better disclosures. CFPB has explicit authority to require information disclosures under section 1032 of the Dodd-Frank Act.[4] Moreover, as discussed below, empirical research suggests that better disclosure requirements for payday loans could benefit consumers. Accordingly, CFPB should consider information disclosures as a supplement to the proposals currently under consideration.

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[3] *See, e.g.*, Paige Marta Skiba, *Regulation of Payday Loans—Misguided?*, 69 WASH. & LEE L. REV. 1023, 1041-44 (2012).

[4] 12 U.S.C. § 5532(a).

CFPB Should Consider Information Disclosures that Respond to Common Forms of Consumer Error

According to the outline of proposals, CFPB's primary concern is that consumers are taking out loans they cannot afford.[5] As CFPB has suggested, one factor contributing to this phenomenon may be that payday and vehicle title lenders have little incentive to carefully underwrite their loans.[6] Another likely factor—one that the outline of proposals does not discuss—is consumer error.[7] Empirical research suggests that cognitive biases may induce payday borrowers to overestimate their ability to repay on time.[8] What's more, some have argued that payday lenders deliberately exploit such biases when providing information to consumers.[9]

When the problem is poor information processing, the best regulatory solution is often better information disclosure.[10] Indeed, "[p]roperly designed disclosure can significantly improve the operation of markets, leading consumers to make more informed decisions."[11] A 2011 study published in the *Journal of Finance* suggests that better disclosures on payday loans may help consumers avoid taking out loans they cannot afford. According to the study's authors, the key is to develop disclosures that respond to the "cognitive biases [and] limitations that surround the payday borrowing decision."[12]

The authors of this study conducted a randomized field trial to test the effectiveness of three different types of information disclosures. The first type provided consumers with additional information on a loan's annual percentage rate (APR) by "directly comparing the APR on a payday loan with the APR on other financial instruments that consumers are familiar with[, such as] car loan[s], credit card[s], and subprime mortgage[s]."[13] The idea behind this form of disclosure is that it would help prevent consumers from confusing bi-weekly fee structures with APRs. It would also provide a baseline for comparison, which, the empirical literature suggests, could help consumers appreciate the significance of the APR information that's in front of them.[14] The second form of disclosure used in the study compared payday loans and credit cards in terms of the typical cost (in dollars) of borrowing a fixed amount of money (for example, $300) over various timeframes. Again, by providing a baseline for comparison, this type of disclosure could help consumers better appreciate the true price of a payday loan. Furthermore, it could force consumers to overcome so-called "optimism bias"[15] by forcing them to consider the cost of a loan that extends beyond one pay period.[16] The third form of disclosure used by the authors provided information regarding the

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[5] CFPB OUTLINE at 3 ("Chief among [our] concerns is that lenders structure loans with payments that are often beyond a consumer's ability to repay, forcing the consumer to choose between default and repeated reborrowing.").

[6] *Id.* at 4 ("When lenders obtain non-purchase money liens on consumers' vehicles or the right to collect repayment from consumers' accounts or paychecks, lenders have less incentive to carefully underwrite the loans.").

[7] *See* Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*, 157 U. PA. L. REV. 1, 44-45 (2008); Marianne Bertrand & Adair Morse, *Information Disclosure, Cognitive Biases, and Payday Borrowing*, 66 J. FIN. 1865 (2011).

[8] Bertrand & Morse*, supra* note 7, at 1889.

[9] Bar-Gill & Warren, *supra* note 7, at 44.

[10] OFFICE OF MANAGEMENT & BUDGET, CIRCULAR A-4, at 9 (2003), *available at* http://www.whitehouse.gov/sites/default/files/omb/assets/omb/circulars/a004/a-4.pdf [hereinafter "CIRCULAR A-4"].

[11] OFFICE OF MANAGEMENT & BUDGET, 2009 REPORT TO CONGRESS ON THE BENEFITS AND COSTS OF FEDERAL REGULATIONS AND UNFUNDED MANDATES ON STATE, LOCAL, AND TRIBAL ENTITIES 37 (2009) [hereinafter "OMB 2009 REPORT"].

[12] Bertrand & Morse, *supra* note 7, at 1889.

[13] *Id.* at 1866.

[14] *Id.*

[15] Consumers that exhibit optimism bias consider only the best-case scenario. Empirical research suggests that many payday borrowers may exhibit optimism bias. *See* Bar-Gill & Warren, *supra* note 7, at 56.

[16] Bertrand & Morse, *supra* note 7, at 1866-67.

frequency with which the average consumer rolls over a payday loan before paying it back. This disclosure was designed to help consumers appreciate their statistical likelihood of paying back a loan on time.[17]

The authors found that all three forms of disclosure discouraged payday borrowing. The second form (comparing payday loans and credit cards in terms of dollar costs over various timeframes) had the biggest impact, reducing borrowing relative to the control group by 11 percent.[18] The study did not measure the effect of combining different forms of disclosure.

As the authors suggested, the fact that consumers responded to the way cost information was disclosed suggests that, currently, at least some payday borrowers are not making utility-maximizing decisions.[19] The study therefore provides evidence that better disclosure requirements could benefit potential payday borrowers. In light of this and other evidence,[20] CFPB should consider whether disclosure requirements would help it achieve its regulatory goals. In making this determination, CFPB should consider the likely costs and benefits of disclosure requirements relative to alternative forms of regulation. It should also analyze whether disclosure requirements would be effective in conjunction with other regulatory approaches. If CFPB decides to utilize disclosure requirements, it should consider whether different forms of disclosure could serve as complements to one another.

Disclosures Could Also Help Consumers Gain Access to Affordable Credit Alternatives

Disclosures could also address CFPB's concern over the preservation of consumer access to credit. Some consumers use payday loans because they lack affordable alternatives, but many use them simply because they are unaware of the alternatives that are available to them.[21] Undocumented immigrants and minorities are disproportionately represented in the latter group.[22] Accordingly, CFPB should consider requiring payday lenders to provide consumers with more information on alternatives. One option could be to put payday lenders' rates and terms on a graphic scale that implicitly compares them to competing products.[23] In combination or separately, lenders could be required to hand out a CFPB document that directs consumers to a government web site with information about alternative credit providers, their rates, and consumer eligibility.[24] Such

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[17] *Id.* at 1867.

[18] *Id.* at 1881-89.

[19] *Id.* at 1866.

[20] *See, e.g.*, John Campbell et al., *Consumer Financial Protection*, 25 J. ECON PERSP. 91, 91-94 (2011) (discussing consumer difficulty in understanding financial devices).

[21] *See* Edward Lawrence & Gregory Elliehausen, *A Comparative Analysis of Payday Loan Customers*, 26 CONTEM. ECON. POL'Y. 299, 300 (2008) (explaining some of the options for liquidity-constrained consumers to obtain credit); Sumit Agarwal, Paige Marta Skiba & Jeremy Tobacman, *Payday Loans and Credit Cards: New Liquidity and Credit Scoring Puzzles?*, 99 AM. ECON. REV. 412 (2009).

[22] Katherine Houren, *Achieving the American Dream in Debt*, 15 WASH. J. CIV. RTS. & SOC. JUST. 651, 670 (2009).

[23] Such an approach has been discussed previously in the context of energy efficiency labeling. *See Comment on Notice of Proposed Full-Fuel Cycle Analysis*, Appendix A, POLICY INTEGRITY (Oct. 19, 2010), *available at* http://policyintegrity.org/documents/10.19_.10_Comments_on_DOE_Full_Fuel_Cycle_.pdf.

[24] In extreme cases, mandatory disclosure requirements may constitute compelled speech in violation of the First Amendment. *See R.J. Reynolds Tobacco Co. v. FDA*, 845 F.Supp.2d 266 (D.D.C. 2012) (holding FDA's cigarette packaging graphic warning rules unconstitutional). *But see Discount Tobacco City & Lottery, Inc. v. FDA*, 674 F.3d 509 (6th Cir. 2012) (upholding a statute requiring graphic warnings for cigarette packaging). However, the Supreme Court has held that purely factual disclosure requirements are constitutional so long as they "are reasonably related to the State's interest in preventing deception of consumers." *Zauderer v. Office of Disciplinary Counsel of Supreme Court of Ohio*, 471 U.S. 626, 651 (1985). As one commentator notes,

> While the Court places a limit on disclosures by cautioning that "unjustified or unduly burdensome disclosure requirements might offend the First Amendment by chilling protected commercial

information sources could include information about online lenders, peer-to-peer lenders, overdraft services, credit unions, non-profit lenders, lending circles, pawn lenders, rent-to-own stores, and other payday loan providers. Even consumers who do not qualify for payday loans under CFPB's proposed rules might benefit from such disclosures because they will know what alternatives are available to them and which are most affordable.

III. CFPB Should More Clearly Define Its Goals

While CFPB has noted various concerns motivating its decision to develop the proposals under consideration, the Bureau should more clearly define the problems it seeks to address. In particular, CFPB should distinguish between concerns based on economic efficiency—in other words, market failures—and concerns based on distribution. While CFPB should pursue both efficiency and distributional goals, defining its objectives more precisely will allow the Bureau to better evaluate its proposals.

CFPB Should Identify the Market Failures It Seeks to Address

Market failures present one of the clearest rationales for regulatory action. The academic literature indicates that payday loans and similar consumer financial products may be associated with multiple forms of market failure. One such failure is cognitive error. Cognitive errors occur when mental processes, such as heuristics, induce people to make mistakes. As Elizabeth Warren and Oren Bar-Gill explain, "Consumer mistakes skew the demand function, inflating demand for products with underestimated risks. The inflated demand skews the market price and leads to allocative inefficiency."[25]

As indicated in Part II, above, the empirical literature describes several common errors that consumers may commit when taking out a payday loan. For example, payday borrowers may misinterpret APR information, causing them to underestimate the true cost of a loan.[26] Additionally, consumers may evaluate the cost of borrowing over too narrow a timeframe, focusing exclusively on the cost of one fee cycle despite being aware that the loan could take longer than one cycle to repay.[27] Relatedly, consumers may fail to anticipate future expenses that could render them unable to repay their loan after a single cycle.[28] In addition, consumers may exhibit time inconsistency, which occurs, for example, when a payday borrower takes out a loan with plans to repay it in full after a single cycle, but then decides that the smaller immediate cost of a rollover is more desirable.[29] CFPB should consider whether its goals include helping consumers avoid cognitive errors such as these.

Another form of market failure that may be associated with payday loans and similar consumer financial products is asymmetric information. When one party to a transaction has more or better information than the other, this can lead to an inefficient exchange.[30] Payday and auto title

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> speech," the Court's language suggests that the only First Amendment interest implicated by compelled commercial disclosures of purely factual information is the potential that the disclosure will prevent the speaker from engaging in protected, truthful commercial speech.

Jennifer M. Keighley, *Can You Handle the Truth? Compelled Commercial Speech and the First Amendment*, 15 U. PA. J. CON. L. 539, 548 (2012) (quoting *Zauderer*, 471 U.S. at 651).

[25] Bar-Gill & Warren, *supra* note 7, at 63.

[26] Bertrand & Morse, *supra* note 7, at 1889.

[27] *Id.* at 1873, 1889.

[28] *See* Bar-Gill & Warren, *supra* note 7, at 23 n.42; *see also id.* at 56 ("The payday loan product is arguably designed to take advantage of consumers' optimism bias and their consistent underestimation of the risk of nonpayment.").

[29] *See id.* at 36.

[30] *Id.* at 5.

borrowers may lack information about less expensive forms of credit that are available to them, or about the cognitive errors that they are likely to make in the course of accessing a loan. If payday and auto title lenders are aware that consumers lack this information, an information asymmetry would exist. CFPB should consider whether these or other information asymmetries are among the problems it seeks to address.[31]

In addition, payday loans and similar consumer financial products may be associated with externalities. Externalities occur when market transactions result in uncompensated costs or benefits to parties who are not directly involved in the transaction.[32] The legal and economic literature suggests that financial distress may create a variety of negative externalities. These include harm to children in financially distressed homes, harm to elderly relatives who may be forced to move out when money is tight, harm to other creditors in the event of bankruptcy, and harm to friends and family members who may have to bail out a financially distressed loved one.[33] Furthermore, a number of studies suggest that financial distress reduces worker productivity.[34] To the extent that payday loans and similar consumer financial products exacerbate financial distress, they may produce these and similar negative externalities.[35]

Of course, payday loans and similar products may also produce positive externalities. By expanding access to credit, such loans may—at least in some circumstances—reduce financial hardship, which could, for example, reduce crime rates. If avoiding externalities is one of CFPB's justifications for regulating payday, auto title, and similar forms of lending, CFPB should analyze carefully the link between such lending and financial distress. While some studies have found that payday lending does not exacerbate financial distress,[36] other studies have concluded that it does.[37] CFPB may wish to evaluate the literature and identify the studies it considers most reliable.

CFPB Should Identify the Distributional Concerns It Seeks to Address

The outline of proposals suggests that CFPB is concerned with the distributional impacts of payday, auto title, and similar forms of lending. Such concern appears well founded. Indeed, payday and vehicle title lending may give rise to multiple distributional concerns. For example, as Elizabeth Warren and Oren Bar-Gill argue, confusing financial products may result in a regressive cross-subsidy from less-financially-sophisticated to more-financially-sophisticated households.[38] In addition, research indicates that high-fee forms of credit are used disproportionately by racial minorities and military families.[39] Another study suggests that undocumented immigrants are particularly vulnerable to abuse by payday lenders.[40] CFPB should consider whether these or similar distributional concerns are among its reasons for regulating.

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[31] However, OIRA notes that the "mere possibility of poor information processing is not enough to justify regulation," and that any information processing problem "should be carefully documented." CIRCULAR A-4 at 5.

[32] Bar-Gill & Warren, *supra* note 7, at 58-59.

[33] *Id.* at 59-62.

[34] *Id.* at 62; *see also* Scott Carrel & Jonathan Zinman, *In Harm's Way? Payday Loan Access and Military Personnel Performance*, 27 REV. OF FIN. STUD. 2805 (2014).

[35] Bar-Gill & Warren, *supra* note 7, at 62.

[36] *See* Richard Hynes, *Payday Lending, Bankruptcy, and Insolvency*, 69 WASH. & LEE L. REV. 607, 614-15 (2012) (summarizing the literature and noting disagreement as to whether payday lending exacerbates financial distress).

[37] *See* Dennis Campbell, *Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures*, 36 J. OF BANKING & FIN. 1224 (2012); Brian T. Melzer, *The Real Costs of Credit Access: Evidence from the Payday Loan Market*, Q. J. OF ECON. 517 (2011).

[38] Bar-Gill & Warren, *supra* note 7, at 64-65.

[39] *Id.*

[40] Houren, *supra* note 22, at 670.

CFPB Should Evaluate Its Proposals In Terms of the Specific Goals It Identifies

Once CFPB has identified the specific concerns it seeks to address, it should evaluate its proposals and their alternatives according to their effectiveness at addressing such concerns. Indeed, only by evaluating its options in terms of precisely defined goals will CFPB be able to determine optimal regulatory strategy.

IV. CFPB Should Consider the Costs and Benefits of Its Rules to Society at Large

Any policy aimed at reducing market failures should be evaluated in terms of its economic costs and benefits.[41] Section 1022 of the Dodd-Frank Act requires CFPB to consider the costs and benefits of its proposed rules.[42] Specifically, section 1022 requires that, "[i]n prescribing a rule under the Federal consumer financial laws," CFPB "shall consider the potential benefits and costs to consumers and covered persons."[43] The term "covered persons" refers to entities that provide consumer financial products and services.[44] The term "consumers" refers to individuals who purchase such products and services in the market.[45] In past rulemakings, CFPB has followed its statutory mandate to consider the costs and benefits of its rules to consumers and covered persons.[46] However, in unnecessarily limiting its analysis to *only* consumers and covered persons, CFPB has missed an important opportunity to assess the impacts of its policies on society at large.

When CFPB's policies affect parties who are neither consumers nor covered persons, analyzing the impact to such parties improves transparency and provides CFPB with key information with which to evaluate its proposals. For example, a rule that provides financial protection to consumers may also reduce the negative externalities borne by consumers' friends and family members. Similarly, a rule that imposes costs on covered persons may also have negative downwind effects on other parts of the economy. In such cases, whether the rule is truly cost-benefit justified depends on whether all the social benefits outweigh all the social costs. Focusing narrowly on the costs and benefits to consumers and covered persons may not provide the full picture.

Furthermore, once an agency has determined that a proposed rule is likely cost-benefit justified, it should evaluate whether that rule is preferable to various alternatives. Considering the costs and benefits to all of society will be important to this determination as well. Two rules may affect consumers and covered persons similarly, but affect external parties in drastically different ways. In such a case, considering the costs and benefits to external parties would allow CFPB to meaningfully distinguish between otherwise equivalent alternatives.

Nothing in the Dodd-Frank Act prohibits CFPB from considering all the social costs and benefits of its proposed rules. While section 1022 prohibits CFPB from *ignoring* costs and benefits to consumers and covered persons, it does not prevent CFPB from considering additional economic

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[41] RICHARD L. REVESZ & MICHAEL A. LIVERMORE, RETAKING RATIONALITY: HOW COST BENEFIT ANALYSIS CAN BETTER PROTECT THE ENVIRONMENT AND OUR HEALTH 12 (2008) ("When considering any regulation aimed at increasing economic efficiency, a responsible regulator must estimate the economic costs and benefits. Otherwise, it is impossible to know at what point to stop spending money to achieve one goal and start spending to achieve another.").

[42] 12 U.S.C. § 5512(b)(2)(A)(i).

[43] *Id.*

[44] 12 U.S.C. § 5841.

[45] *Id.*

[46] *See, e.g.*, Amendments to the 2013 Mortgage Rules under the Real Estate Settlement Procedures Act (Regulation X) and the Truth in Lending Act (Regulation Z), 79 FED. REG. 74,176 (proposed Dec. 15, 2014) (to be codified at 12 C.F.R. pt. 1024, 1026).

effects.[47] In other words, section 1022 is best viewed as a floor, and not a ceiling. Indeed, the legislative history of the Dodd-Frank Act suggests that, in creating CFPB, Congress was in part motivated by the impacts of poor consumer financial protection on the overall economy. In particular, the Senate Committee Report suggests that the financial crisis—which imposed costs on all of society—was the primary impetus for the creation of CFPB.[48] In light of this legislative history, section 1022 of the Dodd-Frank Act should not be read to prevent CFPB from considering the full economic impacts of its rules.

Indeed, analyzing the effects of its rules on parties other than consumers and covered persons could help CFPB avoid legal challenges. A recent article in the *Yale Law Journal* notes that the United States Court of Appeals for the District of Columbia Circuit is increasingly requiring more rigorous cost-benefit analyses from financial regulators.[49] In addition, the Supreme Court recently held that an agency cannot determine that regulation is "appropriate and necessary" without first considering economic costs.[50]

Moreover, analyzing costs and benefits in terms of overall social welfare has been the favored approach of every president, both Democrat and Republican, since Ronald Reagan.[51] Indeed, under Executive Orders 12,866 and 13,563—issued by Presidents Clinton and Obama, respectively—executive agencies are required to analyze the net social impact of any significant regulatory action.[52] Executive Order 13,563 further emphasizes the importance of agency use of "the best available techniques to quantify anticipated present and future benefits and costs as accurately as possible."[53] While CFPB is an independent agency and thus not strictly bound by these orders,[54] in Executive Order 13,579, President Obama explicitly recommended that independent agencies follow the central principles of Executive Order 13,563, which includes conducting cost-benefit

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[47] *Cf. Ctr. for Biological Diversity v. Nat'l Highway Traffic Safety Admin.*, 538 F.3d 1172, 1197-98 (9th Cir. 2008) (holding that statute requiring agency to consider certain enumerated factors did not prohibit cost-benefit analysis based on overall social welfare).

48 S. REP. NO. 111-176, at 11 (2010) (noting that "the financial crisis was precipitated by the proliferation of poorly underwritten mortgages with abusive terms. followed by a broad fall in housing prices as those mortgages went into default and led to increasing foreclosures").

[49] John C. Coates IV, *Cost-Benefit Analysis of Financial Regulation: Case Studies and Implications*, 124 YALE L. J. 882, 909 (2015) (discussing a recent trend of judicial imposition of exacting cost-benefit analysis requirements on financial regulations); *see also Chamber of Commerce v SEC*, 412 F.3d 133 (D.C. Cir. 2005) (striking down an SEC rule because of failure to estimate certain difficult to quantify costs in a cost-benefit analysis); *Business Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011) (striking down a rule requiring public companies to include specific information in their annual disclosures because of inadequate cost-benefit analysis); *Goldstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006) (striking down a rule requiring registration of hedge fund advisors because of inadequate cost-benefit analysis); *Fin. Planning Ass'n v. SEC*, 482 F.3d 481 (D.C. Cir. 2007) (striking down a rule exempting broker-dealers from registration because of inadequate cost-benefit analysis); *PAZ Sec., Inc. v. SEC*, 494 F.3d 1059 (D.C. Cir. 2007) (striking down an order affirming expulsion of an NASD-member firm because of inadequate cost-benefit analysis); *Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166 (D.C. Cir. 2010) (striking down a rule treating a new class of securities market-linked annuities as securities because of inadequate cost-benefit analysis).

[50] *Michigan v. EPA*, 576 U. S. ___ (2015) (holding that EPA's decision that "costs should not be considered" when deciding whether to regulate power plants violated EPA's statutory mandate to regulate only if "appropriate and necessary."). Section 1022 of the Dodd-Frank Act provides that CFPB's general rulemaking authority consists of the power to "issue orders and guidance, *as may be necessary or appropriate* to enable the Bureau to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions thereof."

[51] *See generally* REVESZ & LIVERMORE, *supra* note 41, at 21-51.

[52] Exec. Order No. 12,866, 58 FED. REG. 51,735 (Oct. 4, 1993); Exec. Order No. 13,563, 76 FED. REG. 3,821 (Jan. 21, 2011) (reaffirming and expanding the principles of Exec. Ord. No. 12,866).

[53] *Id.*

[54] 44 U.S.C. § 3502(5) (listing CFPB as an independent regulatory agency); Exec. Order No. 12,866 § 3(b) at 51,735 (explaining that order does not apply to independent regulatory agencies).

analysis in terms of overall social welfare.[55] The Office of Management and Budget (OMB) has also encouraged independent agencies to follow the principles and requirements of the order.[56] Furthermore, the Administrative Conference of the United States ("ACUS") has recommended that independent agencies use the social-welfare method of cost-benefit analysis when developing major rules.[57]

Given the importance of analyzing policies in terms of overall social welfare, as well as the fact that the Dodd-Frank Act does not prevent CFPB from doing so, CFPB should analyze its rules aimed at efficiency in terms of their potential costs and benefits to society at large. CFPB should do so not only for the proposals currently under consideration, but as a general practice moving forward.

V. In Light of Potential Substitution Effects, CFPB Should Consider Developing Its Payday Loan Rules in Coordination with Rules Covering Alternative Forms of Credit

One concern stressed in the literature on payday lending regulation is the possibility that consumers without access to credit through payday lending will be forced to rely on less convenient, more costly forms of credit.[58] These potentially harmful substitutes include overdraft services, pawn lending, and rent-to-own services.[59] Overdraft services in particular can carry costly, unpredictable fees.[60]

CFPB could minimize such substitution effects by expanding the scope of its proposals to encompass both payday loans and likely substitutes for such loans. However, the Bureau has indicated that it is not considering imposing regulatory requirements on other categories of loans as part of this proceeding.[61] CFPB should nevertheless carefully consider the extent to which its proposals will encourage consumers to substitute alternative forms of credit for payday loans. If possible, estimates of any costs or benefits associated with those substitutions should be incorporated into the Bureau's assessment of the total costs and benefits of its proposals.

VI. Conclusion

The proposals under consideration include promising and creative regulatory solutions. As an additional regulatory tool, CFPB should consider issuing information disclosure requirements. Better information disclosures could help payday and vehicle title loan borrowers overcome common cognitive biases. They could also help consumers identify more-affordable credit alternatives.

In addition, CFPB should more clearly define the problems it seeks to address. In particular, CFPB should distinguish between concerns regarding markets failures and concerns regarding distribution. Insofar as market failures are among the problems CFPB seeks to address, the Bureau

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[55] Exec. Order No. 13,579, 76 FED. REG. 41,587 ("Executive Order 13563 set out general requirements directed to executive agencies concerning public participation, integration and innovation, flexible approaches, and science. To the extent permitted by law, independent regulatory agencies should comply with these provisions as well.").

[56] OFFICE OF MANAGEMENT AND BUDGET, 2014 REPORT TO CONGRESS ON THE BENEFITS AND COSTS OF FEDERAL REGULATIONS 33 (2014), *available at* https://www.whitehouse.gov/sites/default/files/omb/inforeg/2014_cb/draft_2014_cost_benefit_report-updated.pdf.

[57] ACUS Recommendation 2013-2. Specifically, ACUS recommends that independent agencies "consider the appropriateness of the analytical guidance provided in OMB Circular A-4 when developing regulatory analyses for major rules." The social-welfare approach to cost benefit analysis is fundamental to the guidance provided in OMB Circular A-4.

[58] *See* Skiba, *supra* note 3, at 1045; Hynes, *supra* note 36, at 620.

[59] *See* Hynes, *supra* note 36, at 620.

[60] *See* Skiba, *supra* note 3, at 1045.

[61] CFPB OUTLINE at 7.

should be sure to consider the all the potential costs and benefits of its proposed rules, not merely the costs and benefits to consumers and covered persons, as is its current practice.

Finally, CFPB should pay careful attention to the potential substitution effects of its proposed rules. Although CFPB has made the decision not to expand the current proposals to cover products such as pawnshop loans and overdraft protections, CFPB should nevertheless be strategic about how and when it rolls out its rules to ensure that consumers are not unnecessarily harmed by substitution effects.

Respectfully submitted,

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