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Highlights

Highlights of GAO-13-180, a report to congressional requesters

Why GAO Did This Study

The 2007-2009 financial crisis threatened the stability of the U.S. financial system and the health of the U.S. economy. To address regulatory gaps and other problems revealed by the crisis, Congress enacted the Dodd-Frank Act. Federal regulators will need to issue hundreds of rules to implement the act. Industry representatives, academics, and others generally have supported the act's goal of enhancing U.S. financial stability, but implementation of certain of the act's provisions has led to much debate. These experts have expressed a wide range of views on the potential positive and negative effects that the act could have on the U.S. financial system and broader economy.

GAO was asked to examine the (1) losses associated with the recent financial crisis; (2) benefits of the act for the U.S. financial system and the broader economy; and (3) costs of the act's reforms. GAO reviewed empirical and other studies on the impacts of financial crises and the Dodd-Frank reforms, as well as congressional testimonies, comment letters, and other public statements by federal regulators, industry representatives, and others. GAO obtained and analyzed data on agency resources devoted to the act's implementation. GAO also obtained perspectives from regulators, academics, and representatives of industry and public interest groups through interviews and an expert roundtable held with the assistance of the National Academy of Sciences. GAO provided a draft of this report to the financial regulators for review and comment and received technical comments, which were incorporated as appropriate.

View GAO-13-180. For more information, contact A. Nicole Clowers at (202) 512-8678 or clowersa@gao.gov.

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FINANCIAL REGULATORY REFORM

Financial Crisis Losses and Potential Impacts of the Dodd-Frank Act

What GAO Found

The 2007-2009 financial crisis has been associated with large economic losses and increased fiscal challenges. Studies estimating the losses of financial crises based on lost output (value of goods and services not produced) suggest losses associated with the recent crisis could range from a few trillion dollars to over $10 trillion. Also associated with the crisis were large declines in employment, household wealth, and other economic indicators. Some studies suggest the crisis could have long-lasting effects: for example, high unemployment, if persistent, could lead to skill erosion and lower future earnings for those affected. Finally, since the crisis began, federal, state, and local governments have faced greater fiscal challenges, in part because of reduced tax revenues from lower economic activity and increased spending to mitigate the impact of the recession.

While the Dodd-Frank Wall Street Reform and Consumer Protection Act's (Dodd-Frank Act) reforms could enhance the stability of the U.S. financial system and provide other benefits, the extent to which such benefits materialize will depend on many factors whose effects are difficult to predict. According to some academics, industry representatives, and others, a number of the act's provisions could help reduce the probability or severity of a future crisis and thereby avoid or reduce the associated losses. These include subjecting large, complex financial institutions to enhanced prudential supervision, authorizing regulators to liquidate a financial firm whose failure could pose systemic risk, and regulating certain complex financial instruments. In contrast, some experts maintain these measures will not help reduce the probability or severity of a future crisis, while others note that their effectiveness will depend on how they are implemented by regulators, including through their rulemakings, and other factors, such as how financial firms respond to the new requirements. Quantifying the act's potential benefits is difficult, but several studies have framed potential benefits of certain reforms by estimating output losses that could be avoided if the reforms lowered the probability of a future crisis.

Federal agencies and the financial industry are expending resources to implement and comply with the Dodd-Frank Act. First, federal agencies are devoting resources to fulfill rulemaking and other new regulatory responsibilities created by the act. Many of these agencies do not receive any congressional appropriations, limiting federal budget impacts. Second, the act imposes compliance and other costs on financial institutions and restricts their business activities in ways that may affect the provision of financial products and services. While regulators and others have collected some data on these costs, no comprehensive data exist. Some experts stated that many of the act's reforms serve to impose costs on financial firms to reduce the risks they pose to the financial system. Third, in response to reforms, financial institutions may pass increased costs on to their customers. For example, banks could charge more for their loans or other services, which could reduce economic growth. Although certain costs, such as paperwork costs, can be quantified, other costs, such as the act's impact on the economy, cannot be easily quantified. Studies have estimated the economic impact of certain of the act's reforms, but their results vary widely and depend on key assumptions. Finally, some experts expressed concern about the act's potential unintended consequences and their related costs, adding to the challenges of assessing the benefits and costs of the act.