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by RALPH L. STIFFLER KROG*

I. LEGISLATIVE INTENT

The Electronic Funds Transfer Act[1] , which was passed on the last day of the ninety-fifth Congress as Title XX of the Financial Institutions Regulatory and Interest Rate Control Act of 1978, imposes on the Federal Reserve Board the requirement of performing a cost-benefit analysis on any proposed regulations affecting electronic funds transfer systems.[2] One article has called this requirement "especially significant as a barometer of changing congressional attitudes toward consumer protection legislation . . . something never before required in this type of law."[3]

Section 904(a) of the EFT Act[4] requires the Board to make

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1. 15 U.S.C. § 1693 *et seq.* (1978 Supp.).
2. *Id.*
3. Bradell & Olliff, *The Electronic Fund Transfer Act: A Primer*, 40 OHIO ST. L.J. 531, 541 (1979).
4. (a) The Board shall prescribe regulations to carry out the purpose of this title. In prescribing such regulations, the board shall:

(1) consult with the other agencies referred to in section 917 and take into account, and allow for, the continuing evolution of electronic banking services and the technology utilized in such services; and

(2) prepare an analysis of economic impact which considers the costs and benefits to financial institutions, consumers, and other users of electronic fund transfers, including the extent to which additional documentation, reports, records, and other paper work would be required, and the effects upon competition in the provision of electronic banking services among large and small institutions and the availability of such services to different classes of consumers, particularly low-income consumers;

(3) to the extent practicable, the Board shall demonstrate that the consumer protections of the proposed regulations outweigh the compliance costs imposed upon consumers and financial institutions;

three specific evaluations when prescribing EFT regulations. The first consideration is allowing for the continuing evolution of electronic funds transfer mechanisms. The second is the requirement that the Board perform a cost-benefit analysis. This analysis must include the cost of paperwork, the effect that the regulation will have on smaller financial institutions and their ability to compete, and the regulation's effects on the availability of services to low-income consumers. The final requirement is that the Board must show, to the extent possible, that the consumer protections provided by the regulations outweigh the compliance costs to the financial institution.

These requirements appeared for the first time in a floor amendment proposed by Senator William Proxmire, Chairman of the Senate Committee on Banking, Housing and Urban Affairs, on October 12, 1978—just eight days after the bill was reported favorably out of committee.[5] Senator Schmitt spoke in favor of these amendments as restraints on unwritten regulations. He included in the record a prepared statement of support by Senator Tower.[6]

The economic analysis requirements were written to address complaints raised by Senators Schmitt, Tower, Morgan, Garn and Lugar in their dissent from the Senate committee's favorable recommendation of S. 3499 (the previous Senate version of the EFT Act).[7] The major objection which these senators voiced in their *Additional Views* was that there had been no showing of an abuse or evil requiring congressional action, and therefore, the bill was premature. A further objection was that the costs of compliance with the Act could easily outweigh the benefits to consumers and society. Some of the known costs of the Act and any accompanying regulations were legal fees for interpretations, retraining of employees, destruction of old forms and—most expensive—computer programming changes.

Some other fears of premature and overzealous regulations were that (1) excessive paperwork would impede the development of new and more efficient payment mechanisms; (2) smaller financial institutions would be put at a competitive disadvantage; (3) this would inhibit market entry; (4) higher service charges would operate to deny low-income consumers easier access to sav-

(4) any proposed regulations and accompanying analysis shall be sent promptly to Congress by the Board.

15 U.S.C. § 1693b(a) (1978 Supp.).

5. 124 CONG. REC. S18,144, S18,460.

6. *Id.* at S18475-76.

7. ADDITIONAL VIEWS OF SENATORS SCHMITT, TOWER, MORGAN, CARN AND LUGAR, S. Rep. 1273, 95th Cong, 2d Sess. 52 (1978).

ings accounts; and (5) financial institutions would raise charges on checking accounts.[8] The senators also had specific objections to the stop-payment mechanism, the error resolution procedure, and the consumer and criminal liability provisions, among others. However, it was their fear of excessive regulatory costs and the distortions that these costs would produce in the competitive financial services marketplace that resulted in the drafting of section 904(a).

Section 904(a) can be read most easily as a requirement that the Board perform a balancing test, and that some of the known costs of regulatory compliance be included as counterweights to the consumer benefits intended by the rules. Since the costs of compliance must necessarily be passed on to the consumer, the problem facing the Board is how much protection should the consumer be required to buy? If the Board sets very high standards and proposes rules with high compliance costs, then fewer financial institutions will offer EFT services and fewer customers will use them. This will result in society continuing to foster relatively expensive and inefficient payment modes. If the Board sets the standards too low, consumers will suffer from abuses. A careful reading of the section and its legislative history shows that it was the intent of Congress to require the Board to consider costs, both procedurally by preparing an economic analysis, and substantively by showing that the benefits will outweigh the costs.[9]

II. POSSIBLE IMPLICATIONS

Since there had been no judicial interpretation of section 904(a) of the EFT Act, it will be necessary to analyze its potential implications by hypothetical example and analogy to other, similar federal legislation.

Suppose the Federal Reserve Board prescribed rules[10] which adversely affected an entity. Suppose also that the rules were adopted (or modified) without an accompanying economic analysis, or that the economic analysis was clearly deficient and therefore the balance of costs and benefits was clearly an arbitrary decision—at least from the affected entity's viewpoint. Arguably, the affected party[11] would not be without a remedy and could file suit in federal court. The issue before the court in this hypothetical case would be

8. *Id.* at 55.

9. 15 U.S.C. §§ 1693b(a)(2) & (3) respectively, *reprinted at* note 4 *supra*.

10. Electronic Funds Transfer, 12 C.F.R. § 205 (1980).

11. This article does not analyze the question of standing, but assumes that at least a financial institution subject to these regulations would have standing to maintain such an action. Perhaps a customer of the regulated institution or a class of such customers would also have standing.

essentially identical to the issue presented in the numerous cases brought under the National Environmental Policy Act,[12] *i.e.*, whether the court should grant judicial review of the agency's decision, and if so, to what extent should it review the decision?

The cost-benefit analysis requirement incorporated into the EFT Act is not new in federal legislation. It was first imposed on the Army Corp of Engineers in the Flood Control Act of 1936.[13] Several other agencies also use it, *e.g.*, the Nuclear Regulatory Commission,[14] the Soil Conservation Services[15] and the Bureau of Reclamation.[16] Under each of these acts, the costs and benefits are quantified and compared, with costs as the base unit. If the resulting ratio is greater than one, then a project—a dam, or a levee—is submitted to Congress for the appropriation of funds, and final approval.[17]

Prior to society's increased environmental consciousness this was a fairly straight-forward application of simple economics. The kinds of factors considered in the cost analysis were the costs of materials, labor, land and money. The benefits would included hydroelectric power, recreational facilities, navigation, employment, channelization, soil conservation, land reclamation, and the project's useful life expectancy.[18] All of these factors are fairly objective and, though no doubt subject to some disagreement, are all quantifiable.

Congress passed the NEPA in 1969. One of its most important goals was to "establish specific *action-forcing* procedures for the implementation of [the new national environmental policy]."[19] The action-forcing procedure is the now famous environmental impact statement (EIS). Section 102(2)(B) of the NEPA requires federal agencies to "develop methods and procedures . . . which will insure that presently unquantified environmental amenities and values may be given appropriate consideration in decision-making along with economic and technical consideration."[20] This requirement meant that the factors to be used in the agency's decision-making process were no longer objective, and not always quantifiable.

Federal courts were granted judicial review of administrative

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12. 42 U.S.C. §§ 4321-47 (1976) [hereinafter NEPA].
13. 33 U.S.C. § 701 (a) (1976).
14. 43 U.S.C. § 2133 (1976).
15. 16 U.S.C. § 1003(3) (1976).
16. 43 U.S.C. § 412 (1976).
17. *See, e.g.*, 33 U.S.C. § 701-1 (1976).
18. 38 Fed. Reg. 24778-869 (1973). *See also* 42 U.S.C. § 1962a *et seq.*.
19. F. ANDERSON, NEPA IN THE COURTS 1 (1973); emphasis added.
20. 42 U.S.C. § 4332 (1976).

agency decisions in the Administrative Procedure Act (APA).[21] A court can set aside an agency decision if it is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.[22] Cost-benefit ratios and how an agency determined them was at one time considered a strictly legislative function, and the courts refused to review them.[23] This was pre-NEPA, when the factors were fairly objective. After NEPA and the APA, courts began to look more closely at the substance of the factors used in agency decisions.

In 1971, Judge Bazelon of the District of Columbia circuit said:

> We stand on the threshold of a new era in the history of the long and fruitful collaboration of administrative agencies and reviewing courts. For many years, courts have treated administrative policy decisions with great deference, confining judicial attention primarily to matters of procedure. On matters of substance, the courts regularly upheld agency decisions, with a nod in the direction of the "substantial evidence" tests, and a bow to the mysteries of administrative expertise. Courts occasionally asserted, but less often exercised, the power to set aside agency action on the ground that an impermissible factor had entered into the decision, or a crucial factor had not been considered. Gradually, however, that power has come into more frequent use, and with it, the requirement that administrators articulate the factors on which they base their decisions.[24]

While most of the cases which have reviewed cost-benefit analyses have relied upon interpretations of the NEPA,[25] all have necessarily rely upon the APA as well. As the United States Supreme Court said in *Citizens to Preserve Overton Park v. Volpe*:[26]

> Section 701 of the [APA] provides that the action of each "authority of Government of the United States" . . . is subject to judicial review except where there is a statutory prohibition on review or where "agency action is committed to agency discretion by law." . . . This is a very narrow exception, . . . applicable in those rare instances where "statutes are drawn in such broad terms that in a

21. 5 U.S.C. § 702 (1976).

22. *Id.* § 706(2)(A).

23. *See cases cited in* Comment, *Judicial Review of Cost-Benefit Analysis Under NEPA*, 53 NEB. L. REV. 540 (1974); Note, *Cost-Benefit Analysis in the Courts*, 9 GA. L. REV. 417 (1975).

24. Environmental Defense Fund v. Ruckelshaus, 439 F.2d 584, 597 (D.C. Cir. 1971).

25. *See, e.g.* Calvert Cliffs Coordinating Comm. v. Atomic Energy Comm'n, 449 F.2d 1109 (D.C. Cir. 1971). *Calvert Cliffs* is consistently cited as the first case to recognize a heightened judicial duty to review substantive agency decisions under the NEPA. *See* Annot., 17 ALR FED. 1 (1973).

26. 401 U.S. 402 (1971).

given case there is no law to apply."[27]

As a result, it is fairly certain that federal courts have the power to review an agency's cost-benefit analysis. However, there is considerable disagreement as to the extent of that review. The two sides label their positions "procedural review" and "substantive review."[28] Those favoring procedural review would only require that a cost-benefit analysis be performed and would not examine the methods and factors even for reasonableness. Those favoring substantive review would examine the agency's decision on the merits. The middle ground, if it exists, would permit judicial review of an agency decision to determine if the methods and factors used in the cost-benefit analysis were arbitrary, capricious, or an abuse of discretion.

> If the balance struck by the agency is within a zone of reasonableness, though it is not the one the court would itself have preferred it will be sustained, and this is the traditional standard of administrative law. If the agency's decision, or even the decisional approach, is considered by the court to be obtuse or purblind, to be, in legal terms, outside the zone of reasonableness, the particular formula of judicial review will not be likely to preclude judicial inhibition or remand.[29]

The only real difficulty would arise when a court, which accepted limited procedural review, refused to consider evidence on the reasonableness of the factors used in a cost-benefit analysis. In the past, such refusal has usually been based on the characterization of the cost-benefit analysis as a legislative function.[30] Such a characterization, however, is not likely for the EFT Act's economic analysis since the balancing is done entirely by the agency, *i.e.,* there is no need to return to Congress for an appropriation of funds, and because of *Overton Park*'s interpretation of the APA supporting judicial review of agency decisions.[31]

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27. *Id.* at 410.

28. Several articles have commented on the scope of judicial review under the NEPA. *See* Note, *Cost-Benefit Analysis, Judicial Review, and the National Environmental Policy Act*, ENVIRONMENTAL L. REV. 363 (1977); Note *The Least Adverse Alternative Approach to Substantive Review Under NEPA*, 88 HARV. L. REV. 735 (1975). *See also* F. ANDERSON, note 19 *supra*.

29. Leventhal, *Environmental Decisionmaking and the Role of the Courts*, 12 U. PA. L. REV. 509, 529 (1974).

30. Sierra Club v. Froehlke (Kickapoo River), 345 F. Supp. 440 (W.D. Wis. 1972), *aff'd on other grounds*, 486 F.2d 946 (7th Cir. 1974); Warm Springs Task Force v. Gribble (Warm Springs Dam), 375 F. Supp. 240 (N.D. Cal. 1974); Environmental Defense Fund v. Froehlke (Cache River), 473 F.2d 346, 356 (8th Cir. 1972).

31. Another reason that courts refused to review cost-benefit ratios in NEPA cases was the debate over whether the NEPA requires inclusion of a formal cost-benefit ratio in the EIS. Trout Unlimited v. Morton, 509 F.2d 1276 (9th Cir. 1974) is a lead-

Another reason not to expect such a characterization is because the economic analysis is the action-forcing requirement of the EFT Act, similar to the EIS in the NEPA. Clearly, a court has the obligation to grant review when someone claims that the Federal Reserve Board has not complied with the Act's requirements.

In its last statement on the subject, the United States Supreme Court limited the scope of judicial review in a way that may seriously handicap one who desires to challenge an economic analysis as the basis for a regulation. In *Vermont Yankee Nuclear Power Corporation v. Natural Resource Council, Inc.*,[32] the Court held that federal courts do not have the power to review and overturn agency rule-making proceedings on the basis of the use *vel non* of a procedural device by the agency, where the agency at least met the statutory minimum. The Court was interpreting the affect of the APA and NEPA on agency rule-making proceedings.

Rule-making proceedings could probably be distinguished from environmental impact statements, cost-benefit analyses, and agency decisions to proceed with construction of a project, which are the proceedings usually under attack in NEPA cases. The clear requirement in the EFT Act of an economic analysis, to the extent of listing factors to be included, might very well give the judiciary expanded scope in determining the necessary statutory minimum. Unfortunately, the EFT Act specifies that the economic analysis is to be done as part of the rule-making procedure.

When courts in NEPA cases have examined the agency's cost-benefit analysis, they have occasionally found serious defects. In *Environmental Defense Fund v. Tennessee Valley Authority (Tellico Dam I)*,[33] the court complained that the cost-benefit analysis "consist[ed] almost entirety of unsupported conclusions."[34] In *Montgomery v. Ellis*[35] the trial court found that on a very marginal project (cost-benefit ratio of 1.5 to 1), the agency had used an arbitrarily low interest rate, an inflated project life span (twice the agency's usual (life span), and was claiming recreational benefits for lakes that would not be accessible to the public. These examples illustrate the possibility that courts will examine the methods and the

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ing case which held that a formal cost-benefit analysis was *not* required in an EIS. Calvert Cliffs Coordinating Comm' v. Atomic Energy Comm'n, 449 F.2d 1109 (D.C. Cir. 1971) is the leading case for the opposite conclusion.

32. 435 U.S. 519 (1977).

33. 339 F. Supp. 806 (E.D. Tenn. 1972).

34. *Id.* at 809.

35. 364 F. Supp. 517 (M.D. Ala. 1973). *See also* Sierra Club v. Froehlke (Wallisville Project), 359 F. Supp. 1289 (S.D. Tex. 1973).

factors used by the Federal Reserve Board in its EFT cost-benefit analysis when it is challenged as arbitrary.

III. EFFECT OF THE REQUIREMENT

Prior to launching an attack on the Board's rules and regulations, one must understand how the Board is to proceed under the Act. The Board interprets its cost-benefit analysis obligation as follows:

> Section 904(a)(2) of the Act requires the Board to prepare an analysis of the economic impact of the regulations that the Board issues to implement the Act . . . . The analysis must consider the costs and benefits of the regulation to suppliers and users of EFT services, the effects of the regulation on competition in the provision of electronic fund transfer services among large and small financial institutions, and the effects of the regulation on the availability of EFT services to different classes of consumers, particularly low-income consumers.[36]

Note that the Board does not believe it necessary to produce a numerical cost-benefit ratio. Even a cursory glance at the economic analysis, however, will reveal that the Board is quite conscious of costs, market effect, alternative procedures for compliance and comments on proposed rules. Rather than attempting to examine all of the regulations, this section will focus on one provision, the documentation requirement of pre-authorized transfers to a customer's account.[37]

Section 906(b) of the Act[38] requires a financial institution to provide positive or negative notice to the consumer for any pre-authorized deposits (*e.g.*, the direct deposit of a Social Security or payroll check), unless the payor provides such notice. Prior to the EFT Act, the Treasury Department was engaged in the direct deposit of Social Security checks without providing monthly notice to the beneficiaries, primarily because of the cost of such notice. One report estimated the cost at 17¢ per transaction or $25 million annually.[39] A plain reading of the Act requires the financial institution to give notice, not the government. The Board found itself with the obligation of regulating this practice.

The first proposed regulation appeared as a choice of one of five

36. 44 Fed. Reg. 18,468, 18,474 (1979). The Board goes on to point out that the analysis assumes no economic impact if the regulations are less restrictive than current industry practice or state law. *Id.*.

37. 12 C.F.R. § 205.10 (a).

38. 15 U.S.C. § 1693d(b) (1978 Supp.).

39. 45 Fed. Reg. 8,261 (1980).

alternatives.[40] The least expensive of these choices was provision for telephone notice whenever a consumer requested it. This service was one that almost all financial institutions already provided.

The next version made several changes.[41] The Board dropped one alternative as too burdensome (notice only on overdraft), and modified the telephone notice option to require the financial institution to inform the customer of his right to receive written notice, permitting the consumer to choose the form of notice. Under this option, the financial institution was permitted to impose a "reasonable" charge for paper notice. The proposed regulation also added an interpretation that a pay slip would be sufficient notice for the direct deposit of paychecks.

The final rule was adopted and the economic impact analysis was published on January 30, 1980.[42] The board obviously had been influenced by the results of the economic impact analysis. The analysis concluded that the cost of notice to financial institutions would be at least 20¢ per transaction, or $29 million annually. The cost to the government would be lower due to economies of scale. "The cost of providing positive or negative notice would substantially eliminate the benefit of automatic direct deposit systems because the cost of the notices would exceed the savings from not producing and mailing paper checks."[43]

The final rule provides for either positive or negative written notice, or telephone notice. The financial institution, not the consumer, has the option of which method to use, because otherwise each financial institution would have to be prepared to provide all possible methods. The consumer cannot demand paper notice. Essentially the Board returned to the status quo that existed prior to enactment of the EFT Act.

The Board had another source of information on the economic impact of this regulation, namely the comments of the financial institutions on the proposed rule. They stated that if the proposal was adopted, they would withdraw from the direct deposit program, and

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40. The alternatives are (i) sending notice whenever a transaction occurs; (ii) sending notice whenever a regularly scheduled transaction does not occur; (iii) using the monthly statement as notice if it is mailed within two days of the transaction; (iv) providing a telephone number which the customer can call to determine if the transaction took place; (v) sending notice only when failure of the transaction to occur causes an overdraft but the institution must pay all items presented (to limit of the amount of the scheduled item) and cannot charge for the overdraft. 44 Fed. Reg. 25,862 (1979); 12 C.F.R § 205.8(c)(1)(i)-(v) (proposed).

41. 44 Fed. Reg. 59,479 (1979).

42. 45 Fed. Reg. 8,238 (1980).

43. *Id.* at 8,261.

force the government to spend the millions of dollars to mail checks directly to the recipients.[44]

The Board used its broad powers to make the regulation less costly than the Act, on its face, would seem to require. Had the Board not modified its earlier proposal, the direct deposit program would have been in jeopardy. The economic impact analysis gave the Board the information it needed to make the necessary decision. Throughout the rule-making process the Board's concern with compliance costs was reflected in its comments.[45] The factors on which the board based its decision were clearly articulated, and appear quite sound, considering the difficulty of the task facing the Board.

> Each time EFTA or Regulation E requires a [financial institution] to make a disclosure, send a notice, or undertake some other procedure, an associated cost occurs. Conversely omission of that action commensurately reduces the protection enjoyed by EFT consumers. The financial institution and the consumer play a zero-sum game. What one gains the other must lose. This largely leaves the Congress and the FRB [the Board] in a political cross-fire between adversary parties.[46]

IV. CONCLUSION

An economic impact analysis requirement for regulatory agencies is a salutory feature. It makes the agency cognizant of the adverse effects of its regulations as well as their benefits. If the purpose of the requirement was to make the Federal Reserve Board aware of the regulatory compliance costs, then it has clearly succeeded. The requirement has forced the agency to look for the least costly alternative. Throughout the commentary on the proposed and final notice rules, it was apparent that the Board was engaged in such a search.[47] The economic impact analysis was the determining factor between alternative proposals, or it seemed to be. On several occasions, the Board requested cost estimates for proposed rules from the industry, and sometimes complained when it got no response.[48] The analysis done by the Board's Division of Research and Statistics was probably the Board's only unbiased source of information. Public commentators on proposed rules have been accu-

44. *Id.* at 8,254.

45. *Id.* at 8,248-65.

46. Hsia, *Legislative History and Proposed Regulatory Implementation of the Electronic Funds Transfer Act*, 13 U.S.F.L. REV. 229, 307 (1979).

47. *See* note 45 *supra*.

48. 44 Fed. Reg. 18,475 (1978). Pages 18,474-19 contain the economic impact analysis for the rules regarding the issuance of access devices (plastic, magnetic strip cards).

rately categorized as adversaries.[49]

The analysis to be done under the EFT Act is relatively easy, or at least it is objective, even if difficult to determine.[50] Compare the task of the Board's Research Division with that facing an agency attempting to quantify environmental costs and benefits. In the EFT Act's analysis an agency is required to determine what something costs in dollars and cents, not in aesthetic values. What the Board is asked to do is possible, though often complex. Due to the reasonableness of the Board's decisions and the clarity of its articulated reasons, it is unlikely that anyone would choose to attack one of the regulations in court. If, however, the Board's analysis and decisions had not been sufficient, had left out one of the specifically required considerations, *e.g.*, disparate impact on small institutions, or if the Board had not met the statutory minimum, then one could mount an attack using the standard of review set forth in the APA with the NEPA cases as analogy.

49. Hsia, *supra* note 46, at 307.

50. *See id.* at 307-08. *See also* Glassman, *Economic Impact Analysis of §§ 909 & 911*, 43 Fed. Reg. 60,937 (1978).