CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

June 5, 2003

H.R. 2120
Financial Contracts Bankruptcy Reform Act of 2003

As ordered reported by the House Committee on Financial Services
on May 21, 2003

H. R. 2120 would address the treatment of certain financial transactions when a party to such transactions can no longer meet its financial obligations. CBO estimates that implementing H.R. 2120 would have no significant impact on the federal budget. By potentially increasing the costs of the Federal Deposit Insurance Corporation (FDIC) and the Federal Reserve, the bill could affect direct spending and revenues, but CBO estimates that any such impact would be negligible.

Financial institutions often use various types of complex financial transactions, such as swaps and derivative contracts, to obtain and provide liquidity to the marketplace. Such transactions entail risk, while others can be used to hedge against such risk. Because of the interconnected nature of the financial markets, a default by one party could adversely affect another party and cause disruptions within financial markets.

Under U.S. law, several statutes govern the insolvencies of participants in financial markets, but as financial transactions have become more complex and sophisticated, many statutory inconsistencies between these laws have emerged. Enacting H.R. 2120 would make technical changes to the U.S. Bankruptcy Code, the Federal Deposit Insurance Act, the Federal Deposit Insurance Corporation Improvement Act of 1991, and the Securities Investor Protection Act of 1970 to improve consistency between these statutes. Such amendments include clarifying and expanding the definitions of various types of financial transactions, such as "repurchase agreement" and "swap agreement." Other changes would address issues such as how to calculate damages when certain financial obligations are not met.

Certain provisions of H.R. 2120, specifically in sections 2 and 7, would explicitly preempt state laws that may relate to these types of financial transactions. Such preemptions are intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA), but CBO estimates any costs to states would be insignificant and would not exceed the threshold established in UMRA ($59 million in 2003 adjusted annually for inflation). The bill contains no new private-sector mandates as defined in UMRA.

According to the FDIC this bill would essentially ratify current practices involving the settlement of complex financial transactions during insolvencies or bankruptcy proceedings. Thus, CBO estimates that enacting H.R. 2120 would not result in any significant cost to the federal government. In addition, CBO estimates that any cost associated with the FDIC's requirement to develop regulations for recordkeeping by insured depository institutions, as well as the Federal Reserve, under section 9 of this legislation would be negligible.

The CBO staff contact for this estimate is Susanne S. Mehlman. This estimate was approved by Peter H. Fontaine, Deputy Assistant Director for Budget Analysis.