The Costs and Benefits of Disclosure

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Bank supervisors monitor banks for “safety and soundness.” If investigations detect problems, supervisors can act to reduce a bank’s risk, which protects taxpayer liability. The supervisors collect, on- and off-site, a wide body of information, such as details on problem loans. They use this information to rate banks, and results remain private and confidential as required by regulatory policy.

Why not let banks voluntarily disclose or require supervisors to share useful information that, incidentally, costs about $3 billion (in 2005) to collect? So if banks could disclose their risk ratings, would better information lead to more efficient market prices of bank securities and avoid costly, duplicate collection efforts?

Richmond Fed economist Ned Prescott built a model to investigate whether there was a good reason to require disclosure. He found that public disclosure of bank ratings by supervisors can create an incentive for banks to withhold information so they can get better ratings and gain market favor. So, mandatory disclosure may hurt the ability of the supervisor to collect that information in the first place. (In the model, allowing banks to make exam results public is the same as requiring a supervisor to share the information.) Prescott also shows that allowing a bank to voluntarily disclose its exam report is no better. If a bank did not disclose its report voluntarily, the markets would assume it withheld the information because it had a bad rating since, if it had a good rating, it would have disclosed the information. As a result, voluntary disclosure can impair supervisors’ ability to gather information in the same way that mandatory disclosure can — by creating incentives for banks to withhold it. His findings demonstrate that there are good reasons for supervisors not to share some of this information.


First introduced in 1975, the Earned Income Tax Credit (EITC) is one of the largest federal government assistance programs targeted to lower-income households. Designed to encourage work force participation, the program distributed $40 billion to 22 million families in 2004.

In a new study, Chicago Fed economist Leslie McGranahan and former associate economist, Andrew Goodman-Bacon, investigate the spending patterns of EITC-eligible households during February and March, the period in which EITC benefits are disbursed. The authors found that these households increase relative average monthly spending on vehicles by 35 percent relative to non-EITC families. The EITC families also spent more on other transportation costs. “Given the crucial role of access to transportation in promoting work, this leads to the conclusion that recipient spending patterns support the program’s prowork goals,” the authors conclude.