IMPROVING FEDERAL CONSUMER PROTECTION IN FINANCIAL SERVICES—CONSUMER AND INDUSTRY PERSPECTIVES

HEARING

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

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IMPROVING FEDERAL CONSUMER PROTECTION IN FINANCIAL SERVICES—CONSUMER AND INDUSTRY PERSPECTIVES

Wednesday, July 25, 2007

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to notice, at 10:03 a.m., in room 2128, Rayburn House Office Building, Hon. Barney Frank [chairman of the committee] presiding.

Present: Representatives Frank, Miller of North Carolina, Scott, Green, Cleaver, Klein, Perlmutter; Gillmor, Neugebauer, McHenry, and Bachmann.

The CHAIRMAN. We will begin the hearing. I thank the witnesses for appearing.

This hearing is one in a series of hearings on the question of what does consumer protection look like in the banking area, in particular after preemption.

As I have said before, there are some of us who wish that the preemption had not happened. I do. I also wish that I did not get more tired at my age than I did 30 years ago and that I could eat more and not gain weight. I have found it unwise to act on the latter two of these, and we are having a hearing today because it would not be wise to act on the first of them either.

The preemption is not going away. If and when there were to be a change in the political climate in which it might be that you could repeal it, we could very well be in a situation, and I am inclined to think we would be, where enough eggs have been scrambled so that unscrambling them would be difficult.

I would tell you that those who want to preserve the preemption should join in our effort to make sure that preemption comes with adequate consumer protection.

In a couple of years, frankly, if the presidency changes hands, and there is still a feeling that the Federal bank regulators having preempted State laws do not themselves have enough in terms of authority and resources and will to do consumer protection, then the preemption will be called into question.

I do not think that is the preferred option. The preferred option is to say okay, here is where we are, let's spend the next year or so working this out. I must say I am convinced from conversations that the current set of tools and resources that the Federal bank regulators have were configured in an era in which the assumption

was that there was a lot of State consumer regulation going on as well. There is now, for national banks, virtually no State consumer regulation, certainly none that is specific to those banks.

It is not a matter of anyone's fault; it is just that there has been a change. We had one set of circumstances, and now we have another.

Part of the issue, and what I am going to ask people to address, is that the Federal Reserve has the authority under the Federal Trade Commission Act to spell out unfair and deceptive practices.

Both the Comptroller of the Currency and the Chairman of the Federal Deposit Insurance Corporation have said—these are not consumer groups but two Federal regulatory agencies—they would like their own authority to deal with unfair and deceptive practices under the Federal Trade Commission Act spelled out.

The Federal Reserve has said no, they do not want to do that. They think it should be done on a case-by-case basis. There are problems when you are doing things case-by-case, but I do not want to be punitive. We certainly are not looking for a regime in which we lock up a lot more people.

The total absence of any negative sanctions almost guarantees that you will not have effective enforcement. It really is not enough for consumer enforcement if the rule is okay, whenever you do something wrong, we will tell you to stop doing it. There needs to be some incentive to stop doing it before you start doing it.

Absent penalties, that cannot be done. If you are in a case-by-case situation under basic precepts of American law, which we all support, that becomes harder to do. You do not penalize someone for doing something when there was some ambiguity about whether he or she had the right to do it.

In the absence of some rules spelled out, you have a harder time enforcing when appropriate. It does seem to me that people ought to know what the rules are.

Again, both the OCC and the FDIC have said they would like to have those rules spelled out. I know the Office of Thrift Supervision, which shares the preemption with the OCC, has in fact spelled out some rules.

Apparently Congress, in some combination of moods, gave the independent power to the OTS, but said that the OCC and the FDIC had to ask the Fed. That is a result for which no rational explanation is even conceivable, much less likely.

I do not know what we collectively were thinking when we did that. Probably nothing. Probably we were busy with something else. That is what happens in large, comprehensive legislation. That is why we have oversight.

My strong view now is that something should be done legislatively to correct that. I do not understand why the OTS should have its own rules spelled out, but the OCC and the FDIC should not.

There are a lot of questions, questions about whether or not the States are involved. The States have a good deal of expertise in regulation here. We have met with State attorneys general and State bank supervisors. There is also the enforcement power at the State consumer level. You have attorney general enforcement

power. It is not clear now who can go to court, and if that is appropriate.

Let me close by saying that this is an issue on which we invite all of you to help us. The goal here is to come up with a rational and fair scheme of consumer protection.

I believe, as many of you know, and I think we have demonstrated, in consumer protection and a good understanding of the importance of financial institutions being able to perform their intermediation role, if those are wholly compatible. Our job is to come up with a better system than we have now, not because anybody individually did something wrong, but because the preemption makes that necessary.

I will just take 10 more seconds in probably a vain effort to try and explain to the press that my repeated criticism over the recent year-and-a-half of the Federal Reserve for not using its authority has not primarily been aimed at their authority under the Home Equity Protection Act. It has been under the Federal Trade Commission Act.

It is as if some in the financial press cannot write about more than one subject at a time, or cannot think about more than one subject at a time.

When we talk about consumer protection, we are not talking only about subprime mortgages. Indeed, we will probably be doing something particular and special for subprime mortgages.

This is about the broader general question of consumer protection involving a whole range of issues. It is that the Federal Reserve has simply told us they are not interested in using that authority, and that we probably, at the end of these hearings, are going to want to put it somewhere else, but that is something we will wait to hear from you on.

I will now call on the ranking member.

Mr. GILLMOR. Thank you, Mr. Chairman. Ranking Member Bachus could not be here and asked me to sit in for him temporarily, and to read a statement from him, but I also want to echo what you said, Mr. Chairman.

There are a number of areas the committee has been looking at, and will be looking at, in the consumer area, not just subprime but credit cards, overdraft fees, and a number of other areas.

A statement from Ranking Member Bachus is as follows:

"Thank you, Chairman Frank, for holding this important hearing on improving consumer protections in financial services. In light of the Supreme Court's recent decision in the *Wachovia* v. *Watters* case, it is important that this committee re-examine the legal framework as it affects consumers of financial products and services.

"U.S. financial systems set the gold standard for economies around the world. Thanks to innovations ranging from credit cards to Internet banking, American consumers have more choices and options available to them than ever before.

"While these innovations have helped fuel a period of unprecedented economic growth, not all consumers have benefitted. For the financially illiterate, more choices can mean greater opportunities to make bad decisions.

"This has underscored the importance of developing strategies that will empower consumers by providing them with the information and the tools they need to protect themselves.

"The agencies have begun making a number of strides in enhancing regulatory cooperation, including the recent Memorandum of Understanding between the OCC and the Conference of State Banking Supervisors, to facilitate prompt referral of consumer complaints to the Federal or State agency with the regulatory authority to obtain redress for the consumer.

"Other constructive initiatives in this regard include the new Web site that the OCC has developed for consumers to lodge complaints and the announcement last week by Federal agencies and State regulators that they will collaborate on an innovative pilot project to conduct targeted consumer protection compliance reviews of selected non-depository lenders with significant subprime mortgage operations.

"Even with these developments, it is my belief that there may be areas where legislative action is necessary. For example, in light of recent problems in the subprime market, it has become clear that we need a national registry and licensing system for mortgage originators so that the bad actors do not move from State to State victimizing consumers with impunity.

"The legislation I introduced 2 weeks ago with Congressmen Gillmor and Price, members of the committee, would establish such a system. Promoting accountability and professionalism among mortgage originators and addressing a gap in the current regulatory framework.

"Mr. Chairman, I look forward to hearing the perspective of our witnesses on this and other consumer protection issues, and I thank you for holding today's hearing."

Mr. GILLMOR. I yield back.

The CHAIRMAN. The gentleman from Texas.

Mr. GREEN. Thank you, Mr. Chairman. I especially thank you, Mr. Chairman, for framing the issues for us. I always try to get here on time because I benefit from your framing of the issues.

I am honored today to be here to hear the perspectives from both the consumers as well as the industry as it relates to these issues: Unfair, deceptive financial practices and the regulators' ability to deal with them; the addressing of complaints and how we can improve the complaint process; and the role of the State regulatory agencies and the enforcement agencies.

If I could, I would just like to say this. One of the things that kind of fascinated me when I had an opportunity to review the materials is the notion that there may be some means of according one-stop-shopping to consumers, so that consumers might have just one number or one place, one agency, that they can initiate their concerns, and from there, can go to many other places, a multiplicity of other places, of course.

I think consumers are so inundated with materials now, so much comes to us through the mail, e-mail, that it would be a great benefit for us to focus on this and see if it is achievable, such that consumers might better benefit from what is available to them.

Many consumers are just not aware of what is available, the methodology, the process. I think this may be a good thing for the average consumer. I look forward to hearing testimony on it.

Having said that, Mr. Chairman, I will have to leave. I have another hearing, so I will be in and out. I do look forward to this. I thank you again, Mr. Chairman, and the ranking member, of course, and I yield back the balance of my time.

The CHAIRMAN. Are there any further opening statements?

If not, we will go to the witnesses. We will begin with Travis Plunkett, who is the legislative director of the Consumer Federation of America.

STATEMENT OF TRAVIS B. PLUNKETT, LEGISLATIVE DIRECTOR, CONSUMER FEDERATION OF AMERICA

Mr. PLUNKETT. Good morning, Chairman Frank, and Representative Gillmor. My name is Travis Plunkett, and I am the legislative director at the Consumer Federation of America. I am speaking today on behalf of six national consumer organizations with tens of millions of members.

I commend the committee for its diligence in examining this important question about how to better protect consumers in the financial services marketplace, especially using Federal regulatory authority.

As Mr. Gillmor mentioned, the elephant in the living room is the Supreme Court's *Watters* decision, which is the culmination of efforts by the Office of the Comptroller of the Currency to cut off the States' abilities to protect consumers of national banks.

These preemptive efforts over a number of years have harmed consumers, because while the States' regulatory efforts have been far from perfect in many respects, and the committee has highlighted some of those imperfections, States traditionally have had the experience, the regulatory infrastructure, the willingness to experiment, and the desire to protect consumers.

Unfortunately, the OCC and some of the other Federal banking regulators are lacking in each of those areas.

Our recommendation is for the committee to continue to examine Representative Gutierrez's legislation that would restore in some modest ways the States' abilities to protect consumers who purchase financial services from the national banks.

In looking at the Federal regulatory scheme, we encourage you to look at the detailed examples I have in our testimony of the failure by Federal agencies to protect consumers beyond the mortgage lending arena.

This committee, rightly so, has spent a lot of time in looking at failures to regulate at the State and the Federal level regarding subprime mortgage lending.

In my testimony, however, I also address failures in regards to credit card regulation, overdraft loans, the availability of deposits to consumers under the Check 21 law, Internet payday lending, unlawful garnishment of Social Security funds, and the manipulation of payment order of checks by national banks.

The Subcommittee on Financial Institutions and Consumer Credit has examined problems with credit card regulation at length.

They have spoken a lot about the Federal Reserve's new disclosure proposal regarding Regulation Z of the Truth In Lending Act.

This proposal is helpful in some respects but it does nothing to stem many of the abusive practices the subcommittee has heard about: Interest rates that are assessed for virtually no reason that climb to over 30 percent; late fees when payments are not late; tricks that credit card issuers use to assess late fees when they are essentially paid on time; and a number of other problems in the credit card marketplace.

Credit cards are Exhibit A as to why some Federal banking agencies have failed in their efforts to protect consumers. They have failed in areas where they have some jurisdiction to act right now.

Regarding consumer assistance efforts, the OCC has trumpeted their consumer assistance group. What they say is they are vigilant in responding to consumer complaints. We could not disagree more.

As Professor Art Wilmarth pointed out in testimony before the subcommittee, compared to other financial regulators, a much higher percentage of complaints filed with the OCC were closed because consumers either withdrew their complaints or commenced litigation. Meanwhile, the percentage of complaints in which the OCC found bank errors declined steadily, a strong indication that many consumers didn't find the OCC helpful.

Just last week, the OCC rolled out with much fanfare a new consumer assistance Web site. We find the Web site to be lacking in several areas. It is very discouraging in many respects regarding complaints consumers may have about banks, for instance, regarding the practice of clearing checks from the smallest amount to the largest check in order to increase bounced check fee income.

In at least one case, this Web site does not provide complete information to consumers about their legal rights regarding disputes if a product is purchased with a credit card.

One of the most difficult problems the committee is going to face when examining these problems is the culture of coziness that exists between some banking agencies—I am exempting the FDIC here—and the regulated institutions.

There are a number of underlying reasons for this, which we address in our testimony. Let me just mention a few.

First, the OCC and the OTS in particular are funded virtually entirely by assessments from regulated banks. A large portion of that funding comes from a fairly small number of banks.

Second, there is an over reliance on the examination process as opposed to enforcement, which means the process is not transparent and accountable.

I will summarize here because my time is up. I would urge you to look at the recommendations that we have for making the regulatory process more independent and for addressing the underlying problems I mentioned. In particular, we encourage the committee to look at giving the Federal Trade Commission the authority to bring enforcement actions against national banks and thrifts for unfair and deceptive practices, and giving it concurrent and independent rule making authority over all matters covered by the FTC Act.

Unlike the banking agencies, the FTC has no responsibility to protect the profitability of the financial institutions that they regulate; its sole job is to focus on consumer protection.

Thank you very much.

[The prepared statement of Mr. Plunkett can be found on page 32 of the appendix.]

Mr. MILLER OF NORTH CAROLINA. [presiding] Thank you.

Mr. Gonzalez, for 5 minutes.

STATEMENT OF RAUL GONZALEZ, LEGISLATIVE DIRECTOR, NATIONAL COUNCIL OF LA RAZA

Mr. GONZALEZ. Thank you very much. Thank you to the committee for holding this hearing and inviting us to participate.

My name is Raul Gonzalez, and I am the legislative director at the National Council of La Raza. What I would like to do today is talk about our Latinos and the credit card market and provide some broad recommendations for expanding access to affordable credit to Latinos and shifting the balance of power back into the hands of consumers.

NCLR has worked to improve the opportunities for Hispanics in the United States since 1968. Part of our mission includes advancing policies that enable Latinos to build and maintain assets and wealth.

With regard to credit cards, we have begun conducting research on obtaining firsthand accounts from our community on their experiences with credit cards and doing other policy analyses.

For example, last summer, we held a roundtable discussion which included individuals who collect complaints regarding credit cards. We heard lots of complaints related to the high cost of fees associated with using credit cards and Latinos also filed numerous complaints about the difficulty in evaluating credit card offers and finding a card with desirable terms.

We also released an issues brief entitled, "Latino Credit Card Use: Debt Trap or Ticket to Prosperity?" In this paper, we described disparities in credit card use and in the application of penalty rates and fees on Latino credit card accounts.

I would like to briefly discuss key issues for Latinos in the credit card market. These include unmanageable debt, credit card scams, and hidden policies that result in revolving debt.

NCLR operates a national home ownership network which has gotten tens of thousands of Hispanics into home ownership. Every year, we interface with folks who are unable to go through the process because they have unmanageable debt.

It is clear the unmanageable debt that they have that precludes them from home ownership also makes them vulnerable to obtaining credit cards with unfair and high APRs, and this makes it difficult for them to climb into the American middle class.

In addition to unmanageable debt, we are hearing from the community that several credit card related scams have been targeted to Latino consumers. These scams include fraudulent credit repair services, affinity credit card scams, and fake credit cards sold to consumers.

With regard to industry policies and practices, we know that many low-income Latino consumers are unaware of harmful poli-

cies such as universal default and double billing for purchases made abroad.

They also do not understand the relationship between the minimum payment requirement on the credit cards and their credit card balance.

For Latinos, access to affordable credit has become increasingly critical as they hope to gain access to the middle class.

As you debate how to address abusive credit card policies and practices, we ask that you consider the experiences of low-income Latino families.

On the one hand, Latinos are becoming more integrated into the financial fabric of the country. They are using credit cards more and more. On the other hand, they are using credit cards to pay for their basic needs, and they are also acquiring debt.

There are several challenges that make it difficult for Latinos to access the credit card system and build credit, including using credit cards to pay for their basics.

According to one survey, 39 percent of Latinos reported basic living expenses and 30 percent reported medical expenses as contributing to household debt. They are using their credit cards to pay for these.

A second challenge is the difficulty that Latinos experience getting into the credit card system; 22 percent of Hispanic borrowers have no credit score and many others have a very thin file. The methods to evaluate creditworthiness make it difficult for these individuals to obtain a credit card with a fair APR.

Latinos are more likely than whites to pay interest rates which exceed 20 percent as a result of this. As a result, Latinos are not just in a vulnerable position with regard to credit cards, but they are also in a vulnerable position with regard to other debt they have, including their homes.

In addressing credit card reforms, policymakers should begin by banning harmful industry policies and practices. This would include universal default, changing term provisions, deceptive monthly minimum payment requirements, double billing on purchases made abroad, mandatory arbitration and the inflation and application of fees.

We also believe that policymakers should improve the system for collecting and reporting on consumer complaints.

There is an enormous opportunity for law makers and industry leaders to integrate Latinos into the mainstream financial system. This committee should move forward to enact legislation that shifts the balance of power back into the hands of consumers, including focusing on financial counseling.

We applaud the committee for holding this hearing and look forward to working with you on this legislation. I would be happy to answer any questions. Thank you.

[The prepared statement of Mr. Gonzalez can be found on page 67 of the appendix.]

Mr. MILLER OF NORTH CAROLINA. Thank you, Mr. Gonzalez.

Mr. Gaberlavage, for 5 minutes.

STATEMENT OF GEORGE GABERLAVAGE, DIRECTOR, POLICY RESEARCH & DEVELOPMENT, CONSUMER AND STATE AFFAIRS, PUBLIC POLICY INSTITUTE, AARP

Mr. GABERLAVAGE. Thank you, Mr. Chairman, Representative Gillmor, and members of the committee, for the opportunity to testify on this important matter.

A major priority for AARP is to assist Americans in accumulating and effectively managing adequate retirement assets. Key to achieving this goal is helping individuals better manage financial decisions and protecting consumers from financial fraud and abuse that can erode retirement savings and financial resources.

The recent meltdown in the subprime mortgage market, rising levels of foreclosures and credit card debt, increasing bank fees and questionable practices, and a steady erosion of State authority to protect consumers have brought us here today.

Consider a few statistics: One out of every five families with a subprime mortgage is expected to lose their home to foreclosure. Last year, Americans paid over $89 billion in credit card fees, interest, and other charges, and consumers paid over $17.5 billion in overdraft fees last year, an increase of 75 percent from 2 years ago.

Add to this list the cost to consumers of fraudulent demand drafts used to access consumer bank accounts, unequal treatment of debits and credits to checking accounts under Check 21 provisions, and unauthorized garnishment of Social Security and other Federal benefits, and it is clear why so many consumers find themselves in financial difficulty.

Over the course of the last several decades, the effectiveness of the regulatory system has eroded as the State role in credit regulation has been preempted and the Federal Government has declined to fill the gap.

In order to turn the tide, there are a number of substantial hurdles in the current Federal system that will first have to be overcome. These include an emphasis on safety and soundness regulation, potentially at the expense of consumer protection; a reliance on examinations in case-by-case actions rather than rule making and enforcement; slow action by regulators in the face of overwhelming evidence of a problem; and dependence on disclosure rather than substantive regulation to protect consumers.

Today, Congress has a very real opportunity to enact meaningful reforms that will minimize abusive practices and institutionalize reform so that progress continues when the current spotlight dims.

Among AARP's legislative recommendations are the following: First, authorize the Federal Trade Commission to bring enforcement actions against national banks and thrifts for unfair or deceptive practices. Given the FTC concurrent and independent authority over national banks for all matters covered by the FTC Act.

Second, allow States to enforce the Federal lending laws and Federal unfair or deceptive practice provisions of the FTC Act against national banks.

Third, as discussed more fully in our written statement, adopt meaningful Federal reforms on a wide range of consumer issues including credit cards, overdraft and other bank fees, and subprime lending.

Fourth, put in place real opportunities for consumer redress in the wake of abusive practices.

Finally, establish an effective centralized complaint reporting and resolution mechanism.

At the same time, we encourage Congress to integrate as fully as possible the States as partners in the effort to restore fairness to consumers in the financial marketplace.

Experience shows that States have been leaders in finding innovative solutions to the types of problems we are discussing today.

In closing, we urge Congress to do all that it can to ensure that Federal and State regulators and enforcement officials are given the tools they need to adequately protect consumers from the abuses we are witnessing today, and those that will emerge in the future.

Thank you.

[The prepared statement of Mr. Gaberlavage can be found on page 74 of the appendix.]

The CHAIRMAN. Thank you. We will hear from Arthur Johnson on behalf of the American Bankers Association, who is here to testify on matters he is discussing with Members of Congress these days.

Mr. Johnson?

STATEMENT OF ARTHUR C. JOHNSON, VICE PRESIDENT, AMERICAN BANKERS ASSOCIATION, AND CHAIRMAN AND CHIEF EXECUTIVE OFFICER, UNITED BANK OF MICHIGAN

Mr. JOHNSON. Thank you. Chairman Frank, Representative Gillmor, and members of the committee, my name is Art Johnson, and I am chairman and CEO of United Bank of Michigan, and I also serve as vice chairman of the American Bankers Association.

I would like to thank you for the opportunity to present ABA's views on how to best protect consumers in light of the recent Supreme Court decision in *Watters* v. *Wachovia.* That decision settled the question of who has jurisdiction over the operational subsidies of national banks and was the latest in a long line of court decisions supporting the dual banking system.

As requested, today we will be focusing on regulatory structures to protect consumers today and not on specific products or practices.

ABA believes that the dual banking system is the best framework to ensure a balanced legal and regulatory environment for the efficient and effective enforcement of consumer protection laws.

We believe that the division of responsibility among State banking agencies, State law enforcement, and Federal regulators is appropriate, with each agency able to focus its resources on institutions within its primary jurisdiction.

While State law enforcement authorities naturally share concern about consumer protection, we believe the bank regulators are in the best position to achieve this objective through a vast array of supervisory and remedial options available to them. Moreover, due to frequent examination and access to a bank's books, regulators have a more complete picture of any bank and are in a better position to stop problems early and choose appropriate corrective measures.

I would note that States face real issues arising from the institutions within their primary jurisdiction that demand their attention and enforcement resources.

As was noted repeatedly at the hearing before this committee just a few weeks ago, many of the problems in the subprime area, for example, have arisen in institutions outside the enforcement jurisdiction of Federal bank regulators.

With a clear division of authority, redundant supervision and enforcement can be avoided. It is, however, appropriate for these entities to coordinate their efforts to protect consumers as they have recently done through information sharing agreements, parallel examinations, and referrals of customer complaints to the appropriate regulator.

In short, after the *Watters* decision, we can stop working at cross purposes and focus instead on cooperating among different agencies with the common purpose of ensuring that customers are treated fairly.

This cooperation is further evidenced in the Federal system by providing extensive and uniform protection for consumers through interagency exam procedures.

In addition, each Federal agency has implemented a consumer complaint process to address any claims of unfair or deceptive practices. However, only the Federal Reserve Board, the OTS, and the NCUA have explicit authority to make rules under Federal unfair and deceptive acts and practices, or the UDAP law; the OCC and the FDIC do not.

To address this anomaly, we support vesting all of the Federal banking agencies with UDAP rule writing authority to be exercised jointly. Only through joint authority can we ensure that the UDAP law is uniformly enforced.

However, in exercising this authority, it is important to target unfair or deceptive practices and not target products that may otherwise benefit consumers.

Before closing, I want to emphasize how seriously bankers take their responsibilities to treat our customers fairly. Take my bank, for example. We have a compliance training program that is required for all of our employees, not just our compliance officer.

In addition, compliance management plays a role in every aspect of our bank that touches our customers. Our directors hold our employees accountable for meeting their obligations. This is especially true for our compliance officer, who in the case of our bank, just happens to be my son.

The important thing to realize is that our bank is typical of thousands of others that invest heavily in a compliance culture, each with dedicated compliance professionals who take great pride in ensuring that consumers in the dual banking system are being treated fairly.

I like to say that compliance is everyone's business, because each time we serve a customer, we have an opportunity to show our respect for them and that we deserve their trust and their business. This is the cornerstone of successful banking.

Thank you for this opportunity. I would be happy to answer any questions that you may have.

[The prepared statement of Mr. Johnson can be found on page 81 of the appendix.]

The CHAIRMAN. Thank you. Next is Jim Sivon, who is a partner at Barnett, Sivon & Natter.

STATEMENT OF JAMES C. SIVON, PARTNER, BARNETT, SIVON & NATTER PC

Mr. SIVON. Chairman Frank, Congressman Gillmor, and members of the committee, my name is Jim Sivon, and I am a partner in the Washington, D.C., law firm of Barnett, Sivon & Natter.

I appreciate the opportunity to appear today to discuss consumer protection issues following the decision in *Watters* v. *Wachovia.*

In order to highlight those issues, I have organized my statement from the beginning of a consumer credit transaction to the end of a transaction.

At the beginning of a credit transaction, the best protected consumer is an educated consumer. Financial literacy has been the focus of a significant amount of attention in recent years, yet more needs to be done.

The solution to this challenge, in my opinion, is to incorporate financial literacy into our public school systems. A few States have done this. The Federal Government and the financial services industry should work together to make this opportunity available nationwide.

The disclosure of key terms and conditions is the next step in the credit process. Disclosure is an important consumer safeguard. However, in order for disclosures to work properly, they must be clear and understandable.

The Federal banking agencies have started to make use of consumer testing in the development of new model disclosure forms. Such testing should continue and disclosures that are unnecessary or counterproductive should be eliminated.

Congress also should resist the temptation to mandate detailed disclosure regimes; detailed statutes can result in overly complex disclosures.

After selecting a particular financial product, a consumer is concerned about the protections that apply. We have a national consumer credit system, but all consumers do not enjoy the same level of protection.

The recent problems in the mortgage market illustrate the limitations of the current system.

The Federal banking agencies have responded to those problems with two separate advisories on mortgage lending practices. Those advisories, however, apply only to Federal lenders, not to State licensed lenders. While efforts are underway within the States to impose similar requirements, nothing guarantees that all States will adopt them.

As a result, consumers that obtain a loan from a federally regulated lender will receive one level of protection and consumers who receive a loan from a State lender receive a different level of protection. This not only deprives consumers of comparable protection but allows institutions to engage in regulatory arbitrage based on consumer protection standards.

Consumers of financial products should receive the same protections regardless of the type of lender that provides the product or the jurisdiction in which the product is delivered. Uniform national consumer protection standards would meet this goal.

Federal preemption is a key part of that approach. However, I would agree with Chairman Frank's opening comments that to work properly, such a system does require robust Federal standards.

Today, national banks and Federal thrifts are subject to a number of consumer protection standards. Yet, we may have reached the point where additional safeguards are appropriate.

Both the Federal Trade Commission Act and the Home Ownership Equity Protection Act authorize the Federal banking agencies to define and prohibit acts or practices that are unfair or deceptive. It now appears that the Federal Reserve Board soon will propose revisions to its HOEPA rule to address unfair and deceptive acts or practices in the mortgage market.

I would recommend that any such rule apply to all lenders. Further, I would recommend that any rule based upon the FTC Act be issued jointly by the Federal banking agencies in consultation with the FTC. Joint rule making would ensure that such a rule is uniform.

After a consumer acquires a financial product, the consumer naturally expects that product to perform as advertised. Yet, consumers do not always appreciate the legal distinctions between different types of lenders and may not be sure where to turn to assistance.

Consistent with Congressman Green's opening comments, I would urge the Federal banking agencies to establish a centralized system for consumer complaints and referrals under the auspices of the Federal Financial Institutions Examination Council.

Enforcement actions are an ultimate form of consumer protection. Policymakers should seek to balance the use of enforcement resources to ensure that consumers are adequately protected.

During the recent problems in the mortgage market, lenders of all types engaged in questionable practices. The institutions that have gone bankrupt because of their practices were State licensed and supervised. This suggests that State supervisory resources were inadequate or not adequately utilized.

In a natural allocation of supervisory resources, Federal regulators should be responsible for federally chartered lenders and State authorities should be responsible for State licensed lenders.

The final step in the consumer credit process is funding. This is not so much an issue for consumers as it is a policy dilemma. Perhaps the best way to address this is to work closely with lenders and investors to develop an approach that balances reasonable accountability with continued liquidity.

Thank you again for the opportunity to appear today. I would be happy to respond to any questions.

[The prepared statement of Mr. Sivon can be found on page 100 of the appendix.]

The CHAIRMAN. I will begin, and I appreciate the responses. Mr. Plunkett, your whole statement will go into the record, so the list

of the organizations on whose behalf you are testifying will be clear.

I was an original sponsor of the effort to overturn the preemption. Without asking anyone to give up that ultimate goal, I do think we need to move forward from where we are.

I want to focus on two questions: Rule making authority and enforcement authority. They are linked. Let me start with rule making authority.

Mr. Johnson and Mr. Sivon, I think you both referenced a joint rule making authority involving all the bank regulators and the FTC. I will tell you what the problem is.

In the Fair and Accurate Credit Transaction Act, we found the problem, namely, if you are a consumer who gets your credit report and you find on that credit report a negative report about something where you were not in fact at fault, report of a transaction where the store had agreed you should not owe them the money, or the product was defective, or you were double billed, or whatever, there is literally now no way for you to contest that. Literally, no way, except to ask the retailer to say, "mea culpa". They are not good at that.

We mandated in the Act, which I think we passed in 2003, that the FTC and the bank regulatory agencies should work together—the bank regulatory agencies plus the National Credit Union Administration should come together and promulgate a set of procedures whereby consumers could challenge these inaccurate reports.

We had a hearing on that. What they said was well, we are still working on it. Frankly, giving all of those regulatory bodies the mandate jointly to come up with rules with nobody having more power than anybody else to impose them is the functional equivalent of recreating today's United States Senate.

You get a very well meaning and elegant institution incapable of action. I must tell you, it is not the fault of any individual. You have seven agencies. They are busy agencies. That one does not work, to me.

In this situation, by the way, I am going to be proposing when we come back that we give the authority to the Federal Trade Commission by itself with a duty to consult with and get comments from the other agencies.

That is on the specific question of the right to contest information in a credit report. Now, I do think we need to spell out more authority, I believe, on unfair and deceptive practices. The current situation is not good either for the consumers or the regulated institutions.

One earlier Comptroller had said to me, well, we can do what we need to do because we have the mandate to protect safety and soundness. I asked for that to be explained. The answer was well, if a bank is being unfair to its customers, that could impugn safety and soundness. It could. It could also, unfortunately, enhance the safety and soundness. Sometimes there is money in not being nice to people.

The notion that any unfair credit practice will cause reputational risk is not, unfortunately, the case. That would be self-enforcing.

I think we need to propose some regulatory authority, some rule making authority beyond what we have. I do agree that we do not want everyone to have his or her own.

We are talking now about rule writing; enforcement is a separate issue. I understand the banking organizations' concerns if we invite the FTC in on enforcement.

For rule writing, we have two agencies now that have enforcement responsibilities but do not yet have rules spelled out because of the Federal Reserve's refusal to write them. They were the ones given the authority—the OCC and the FDIC, both of the major regulators.

What about from the rule writing now, not the enforcement, leave that aside, asking the OCC—not asking—directing the OCC and the FDIC to come together with a set of rules and a codicil to that, directing also maybe that the OTS join in, so that we have one set of rules for the OTS, the FDIC, and the OCC.

We have an OTS set of rules that they have just promulgated. What are your comments on directing the OCC and the FDIC together to come up with a set of rules?

Let me start with Mr. Sivon.

Mr. SIVON. If there is an opportunity for the agencies to work together and come up with a common rule so that it is uniform—

The CHAIRMAN. It is not a question of opportunity. I am talking about what we tell them to do.

Mr. SIVON. Yes, of course.

The CHAIRMAN. A common set of rules spelling out unfair and deceptive practices.

Mr. SIVON. Yes. I think that is what I was endorsing in my comment, that they have a joint rule making authority. I was a little confused in some of your comments about the disadvantages of joint rule making.

The CHAIRMAN. Seven is disadvantageous, too. Six. The OTS, the OCC, the FDIC, the Federal Reserve, the National Credit Union Administration, and the Federal Trade Commission. That appears to go beyond the number of people who will come together and get everything done. That is what we did in the FACT Act; two is very different than six.

Mr. SIVON. I was going to note that there certainly are instances where the Federal banking agencies have worked cooperatively on joint rules in the CRA area, FCRA privacy.

The CHAIRMAN. Yes, that worked well. I agree. Frankly, the Federal Reserve has already demonstrated a reluctance to act in this area. I think if you add the others to the Federal Reserve, which has already said they do not think there is any need for spelling out unfair and deceptive, you just continue to give them the veto.

When they testified, the Comptroller and the Chairman of the Federal Deposit Insurance Commission both said that they would like these rules spelled out. They think it would be better. The Federal Reserve said "no."

I do not think it makes sense to put all three of them in. I think the two other agencies, that would make sense.

Mr. Johnson?

Mr. JOHNSON. Let me try to give you a little perspective from where I come from in Grand Rapids, Michigan. We do business in

an area where we compete with every type of chartered depository institution. We also compete in the lending business with many non-depository lenders.

It is not good for any lender to be able to be in a situation where they can have a competitive advantage over someone else because they have less of a burden to be compliant in the way they do business.

While I am not really from Washington and certainly do not know my way around here, even the part about the deals with my industry—

The CHAIRMAN. We have been speaking English here for quite some time, Mr. Johnson. I think you will find it far less inaccessible than you appear to believe.

Mr. JOHNSON. Thank you. I really believe that given the opportunity for the joint rule making to work, so that there is not a disparity out there on the street between consumer protections is really the right thing.

Just the same way that our regulators always get our attention when we are not being perhaps as proactive as we might be on any element of our business, I would suspect that you have the attention of the regulators.

The CHAIRMAN. That simply is not true. The Federal Reserve has had this authority for I do not know how many years, and they just recently told us, "We are not going to use it." Let's not pretend. In Michigan, do they pretend things? You say you are not used to Washington.

Here in Washington, where people have had the authority for many years and say, "We are not going to use it," I take them at their word. The Federal Reserve has said they are not going to use that authority; they do not think it should be done.

The OCC and the FDIC say it should. I do agree it would be better to do it jointly. That is what I am talking about. Then the question would be, would you have us rescind the authority of the OTS and make them un-do what they did and then join in a joint effort? They just went off on their own. It's statutory. It is not their fault that they had that statutory authority.

Mr. JOHNSON. You are really getting a bit beyond my—

The CHAIRMAN. I appreciate it. I do agree with you that you are at a disadvantage vis-a-vis the unregulated, and that is why, in some areas, the answer is to take sensible regulation that you are under and apply it to them, particularly in subprime. I agree.

If only regulated depository institutions made mortgage loans, we would not now be in the subprime crisis. Regulation has avoided, in a sensible pro-growth way, the abuses that came from the absence of regulation.

Any other comments on the joint OCC/FDIC?

Mr. PLUNKETT. Mr. Chairman, I agree with your notion that the Fed has not acted and we need to look at alternatives and certainly creating a little more regulatory competition to allow those two agencies to write rules, in my opinion, could not hurt.

I am speaking for the Consumer Federation here. I am not sure that some of the organizations that have signed onto this testimony would agree with that notion.

The CHAIRMAN. I want to separate that from FTC enforcement. The question is writing the rules. They could be in the same place. They could be altogether.

Mr. PLUNKETT. I have a "but" though, Mr. Chairman. We urge concurrent authority, rule writing authority, for the FTC as well, simply because the culture at the Agency at least provides for the possibility of more independent enforcement.

At the OCC in particular, I am not sure you have independent enforcement, given the factors that I have outlined.

If they had rule writing authority, given what they have done in other areas, I do not think that they would move aggressively to protect consumers. We need to look at ways to make the rule writing process more independent.

Our idea is to bring the FTC in. I am not sure that shifting the rule writing authority without changing the culture and particularly at the OCC is going to make—

The CHAIRMAN. You get to a certain number of institutions and you are mandating nothing.

Mr. PLUNKETT. Here is an idea. In the Military Lending Act, which deals with payday loans and other loans to Service members, the Department of Defense was made the lead agency in writing the rules. They were required to consult with the banking agencies, but it was made clear that they were the lead.

On specific laws, you make a particular agency the lead, hopefully, and then the fall back is if the other agencies do not collaborate, that agency has the rule writing authority.

The CHAIRMAN. I appreciate it. I am going to end my questioning now. With the FACT Act, we should do that, I believe, with the Federal Trade Commission. In the other case, we gave it to the Federal Reserve. I just have to say that they are very able and distinguished people at the Federal Reserve, but in choosing between making world economic policy and resolving consumer disputes, world economic policy seems to win every time in terms of attention.

The gentleman from Ohio.

Mr. GILLMOR. Thank you, Mr. Chairman. I have a couple of questions. First, for our witness from AARP, you talked about the problems of Federal preemption in a negative way vis-a-vis consumer protection. I want your comments on this.

I think in one area, exactly the opposite is true, and that is in the subprime area. The testimony we have had is that there have been almost no problems in subprime in the federally regulated banks and savings and loans. There have been horrendous problems with mortgage brokers at the State level, lenders regulated by the States, and that is where the problems have come.

I have introduced a bill with Representatives Bachus and Price which would mandate that the States go to a license or registration program for brokers and originators to provide that level of protection and if they do not, then HUD would step in and do it.

That would be an area of Federal preemption. I just want to have your thoughts on that legislation.

Mr. GABERLAVAGE. I think the licensing issue is a very important one, Congressman. We would like to take a look at your legislation. I do not think by any means the situation at the State level is per-

fect. We have worked very hard at the State level, particularly on predatory lending, to improve both the laws and the enforcement at that level.

We definitely would like to take a look at what you are proposing.

Mr. GILLMOR. Okay. Mr. Sivon, you talked about the need for clear and understandable disclosures. I certainly agree with that. You now have some consumer testing and focus groups that are being used to improve disclosures.

Is there an area where the disclosures really are understandable to the consumer? For example, if anybody has taken out a mortgage recently, and you look at all the disclosures you have there, it is so voluminous. I doubt if there is 1 in 10,000 mortgagors who read that disclosure. You have huge disclosure that really is meaningless because it is no disclosure.

There are a lot of people that think we would be a lot better off to go to less disclosure and make the disclosure that took place meaningful.

In that context, let me ask you this from an attorney's point of view, is there a litigation risk to the person making the disclosure by providing a simple disclosure as opposed to all that complexity, because they are going to get sued if they did not have a particular sentence in there?

If you could just comment on that problem, and how to solve it.

Mr. SIVON. Of course. As a general matter, the policy of having disclosures, I think, is a very solid policy and it has worked well. You are absolutely right that in certain instances, it seems we have reached a point where disclosures can become overly complex and confusing. Some rationalization of that and the use of consumer testing that the agencies have undertaken, I think, makes a great deal of sense.

On the litigation side, the thing the committee might want to consider is as disclosures are being designed, and the agencies are given the authority to develop models, that there could be safe harbors for institutions from that type of litigation risk, that if they adhere to the particular model, then that litigation risk would not arise.

Mr. GILLMOR. How would you do that? Would you have the regulator or the legislative body set out and say if you disclose "A," "B," and "C," then you have a safe harbor?

Mr. SIVON. It would probably have to be through legislation.

Mr. GILLMOR. Let me ask Mr. Gonzalez, you talked about Latinos being subject to various credit card schemes. Is it any bigger problem for Latinos compared to anybody else who might fall in the same social/economic category as a Latino, and if so, why would that be?

Mr. GONZALEZ. We have seen that Latinos are more likely to be targeted for credit card scams, in part because they are less likely to be accessing the mainstream financial institutions that give individuals, even low-income individuals, the opportunity to kind of measure whether or not a credit card offer is false.

If you do not have access to banking services, and you are getting credit card offers from what may look like a banking service but is not, then you are more likely to fall for these.

They are also targeted for affinity scams, which for example, could be something related to a particular community that looks like it is an actual credit card but is not a credit card.

Because of lack of exposure to the financial system, and also lack of financial counseling and other issues that could improve financial savvy, they are more likely to be targeted.

Mr. GILLMOR. One more question. Mr. Gonzalez, you talked about while these consumers do not know what they are getting into and the need for education, and I agree with you on that, we had in the subprime area—I had a conference of lenders, regulators and consumer groups from Ohio talk about the subprime problems we had there.

I was surprised that the consensus that came out of the group was that the most single most important thing we could do would be to have greater education—that those who had counseling did not have foreclosures.

If we agree on the concept that consumer education is good, my question to you is, how would you effectively deliver that education to consumers? How do you do it?

Mr. GONZALEZ. Sure. We have a network of about 70 home ownership counseling community based organizations that provide home ownership counseling. In some cases, they counsel people out of moving towards home ownership because they are not ready for it and are more likely to default.

In our network, we have fewer defaults because of that. What we find to be effective, not just for Latinos, our networks are not just Latinos, is one-on-one counseling. Even if you receive the education with relation to what are your rights or what you should be looking for, without counseling, if you are new to the financial services market, including mortgages and credit cards, you still may make the wrong choices based on your situation.

People want to access credit cards because they view it as a way to build a credit score. They may make choices that are not the best for them because of the situation they are in and counseling in the community based organizations that are close to where their community is, where they live and with whom they have built trust, has been the most effective way to keep people from home ownership default.

We view it as a great opportunity to build on that, to make sure that people are not getting into unmanageable debt.

Mr. GREEN. [presiding] Thank you, sir. The gentleman's time has expired. I now recognize myself for 5 minutes.

Mr. GABERLAVAGE. Mr. Chairman, can I make a comment on Mr. Gillmor's issue of disclosures?

Mr. GREEN. Yes.

Mr. GABERLAVAGE. It is important, what the disclosure says and how it is written is very important, but also the context and the timing of when it is given is critical. It is not just what it says. There is a whole slew of behavioral science that has been done on consumer decisionmaking that shows, particularly in these mortgage situations where people are adverse to short term losses, that they will go for these loans that promise them that they will not have to put a lot of money up front, but in the long term, they are bad for them.

We really need to take that into account, as well as the understandability of the disclosure.

Mr. GREEN. Thank you for your comments, sir.

I did not thank the entire panel when I gave my opening statement earlier. I do want to thank you for coming in and testifying. I had the privilege of testifying once before Congress and I remember I prepared for weeks to give about a 5-minute statement. I understand what you do and what you go through. I thank you.

My issue will be the one of one-stop-shopping. I really would like some input from you as to how this can become a reality, if at all possible.

I understand that it will not be a panacea because you have too many institutions that you are working with and there are so many elements in the equation that it may be difficult to get a handle on all of them.

How can we have one point of contact for the consumer? The consumer is the most important part of all this and we all agree. How can we have one point of contact for the consumer so that the consumer can get an issue resolved by the appropriate agency, not necessarily at the point of contact. The point of contact will become the genesis of the process. The revelations will be in the multiplicity of agencies that will have enforcement authority, that we do not plan to eliminate.

How do we get to the point where we can give the consumer good information about the entry point, the alpha of the process, such that the omega can be ultimately achieved?

Who would like to help me with this?

Mr. PLUNKETT. I will give you some thoughts to start with, if you would like.

Mr. GREEN. Yes, sir. Thank you. I will start left to right, and we will hear from everyone, and hopefully my time will not expire.

Mr. PLUNKETT. It is a good idea, and you put your finger on the issue, that the quality of the information that is provided, the advice that is provided, is high. As I just pointed out about the OCC's new Web site, that does not appear to be the case.

An obvious point here is to make sure that the effort is well-financed. Put the agencies under tight timelines to work together because on many occasions, they have shown an incredible ability to take simple tasks and drag them out for years and years.

Not too tight, of course. You want it well done. They need to have specific deadlines they have to meet.

Third, have a process in place to review the information and advice that is provided. The OCC's consumer assistance group has been heavily criticized for not helping consumers resolve complaints. They say they view themselves as a neutral arbiter. In many cases, if you look at the information they provide, they appear to be defending the practices of national banks.

You need a process in place to make sure that the advice that is being provided is actually helping people, and then monitor it closely.

Mr. GREEN. Thank you. Mr. Gonzalez?

Mr. GONZALEZ. Thank you. This is an area where we are just now beginning to look at how the agencies should be brought to-

gether to ensure there is information that consumers can actually use.

We believe that currently getting the answers to your questions or even filing a complaint is a scavenger hunt for consumers, particularly from low-income communities, who can become frustrated with the process.

We are looking into what are the best ways to get there. This is a big issue for our community. We will get back to the committee when we are able to complete that analysis.

Mr. GREEN. Thank you. Mr. Gaberlavage?

Mr. GABERLAVAGE. I would agree with the previous comments. Also, I would add that our surveys show that the public is really not very aware of who to go to, and particularly, Government agencies rank very low, except for State AGs seem to have attention of older consumers.

I think publicizing it has to be a key. Also, possibly working through community organizations and making that known to people, particularly in minority communities.

In a previous job I had at AARP, I ran a campaign to inform people about electronic transfer and direct deposit. It is very important to work through community organizations, and possibly I wonder whether State agencies could be included in this in some way, too.

The proposal on the form that the agencies are working on now is good in the sense that it will provide uniform data that can be analyzed. That is very important.

Mr. GREEN. Thank you. Mr. Johnson?

Mr. JOHNSON. I know we are running out of time here, and I have more than 6 seconds worth to say.

I would like to tell you a little bit about how we handle this sort of thing in our bank because it might give us a key to how we can do it in a broader area.

What we do when there is a complaint or even a question that is posed in person or on the phone by one of our customers to one of our bankers, the key to resolving that question or getting the right answer to that question or resolving that complaint is for that first point of contact to take ownership of this problem.

In many instances, we are able to just physically walk that person over to the other banker who has the answer to their question or who can help them work through their complaint.

I recognize that we cannot physically walk all of the complainants around the country to the right person, but that is something that works for us with the 120-some people we have working for us.

I think the key is for that first point of contact to take ownership and for them to know and to help that customer determine who the next place is that they should be going to with a high degree of accuracy.

One of the most frustrating things any of us can experience is when we are on a help line some place and we have to talk to five or six people before we get to the right one.

If we can have that initial point of contact take ownership of that problem and figuratively walk the complainant to the right place, and that as has been suggested, that is going to take the participation of all the players for that to work, but I think the OCC and

their Web site has been a good start, but it is just that, a good start.

Mr. GREEN. Thank you very much. My time has expired, Mr. Sivon. What I will do is yield. Will you allow me 10 seconds or so for Mr. Sivon?

Mr. MCHENRY. Of course.

Mr. SIVON. Thank you very much. I would like to respond. I think we should acknowledge that the Federal banking agencies have taken some positive steps in this area. They all have consumer complaint procedures and systems in place.

The OCC and OTS also have entered into some agreements with the States on information sharing on complaints.

I do think it should be taken to another level. The mechanism that I would recommend that the committee explore is the Federal Financial Institutions Examination Council.

All the Federal banking agencies sit on that body and last year, Congress amended the FFIEC to include a representative of State banking authorities. There you have an entity in which the Federal banking authorities and the States can sit down and ideally collectively come up with the type of system that you are talking about that could be an one stop shop for consumers.

Mr. GREEN. Thank you. At this time, I recognize Mr. McHenry for 5 minutes.

Mr. MCHENRY. I thank my good friend. This has been a very informative panel. I want to start where I think we have some consensus here across this panel. In some way, shape, or form, each of your written testimony mentions this.

Mr. Plunkett begins actually in what you said before the committee, much less what you have added in your testimony, you said the process is not transparent. When offering credit, consumers are not aware of all the details upon which they are signing this document, this very complex legal document.

I agree with you. I very much agree with you that generally speaking, whether it is A to Z in lending, in particular, mortgage lending right now, the process is not transparent.

Should it be at least part of our focus to ensure that the regulations are written in a clear English style so that perhaps on one page, people can understand the key components of what they are signing rather than a multi-page document written in fine print to actually beyond that, have a supplement to it that says clearly and concisely what the key terms are for the transaction they are undertaking?

If we could just start with Mr. Plunkett, if you could just briefly comment on that.

Mr. PLUNKETT. Sure. I actually agree with you that better disclosure is helpful. When I was talking about the process, I was talking about the regulatory process, the focus on supervision over enforcement.

It is a secretive process. Consumers have a hard time getting a handle on it, what the problems are with the regulatory institutions that are being supervised.

Mr. MCHENRY. You would concur that transparency in the actual lending process and the transaction process for the consumer needs to be clearer?

Mr. PLUNKETT. Necessary. You are right. You cannot provide too much information. It is not sufficient, however, if products that are deceptive or abusive are still available, it really does not help the consumer much if you tell them they are going to be over charged or pay a fee that is not reasonable. You also need to have some protections in place.

Mr. MCHENRY. Beyond protections, try to get an area of consensus.

Mr. PLUNKETT. Better disclosure.

Mr. MCHENRY. Mr. Gonzalez?

Mr. GONZALEZ. Yes. We would agree that there needs to be more transparency, obviously. One focus might be in places where there has been trouble with people, where the lack of transparency has led to ongoing debt, such as the double billing for purchases made abroad, or people not understanding the minimum payments.

It would be very helpful to have plain English descriptions of the terms. They should be clearly headed so people understand them. They should not be scattered throughout the disclosure document. Also, there should be a focus on things that could get consumers in trouble.

Mr. MCHENRY. Thank you.

Mr. GABERLAVAGE. We would agree that the disclosure needs to be much improved. One of our litigators says that they think that the disclosure should be written on bright pink paper. I do not know what color you like. I think one of the problems, I agree with Travis, that it is the practices.

Mr. MCHENRY. Thank you.

Mr. GABERLAVAGE. And the timing. Timing of when they are given.

Mr. MCHENRY. Mr. Johnson?

Mr. JOHNSON. Yes, I think clearly effective disclosure, which is what we are talking about here, and which Mr. Gillmor mentioned as well, is something that we should really all agree on. Getting to there and what exactly that means is perhaps more complex.

We would be more than happy to work with the committee and the regulators to get there.

Mr. MCHENRY. Mr. Sivon?

Mr. SIVON. Same answer. I think disclosure is one of the most important consumer safeguards, so having effective and timely, I agree with the comment on proper timing, that it is important.

Mr. MCHENRY. I want to go beyond this. There is a discussion about the FTC being a better protector of the consumer.

Mr. Johnson, are you a state regulated bank or a federally regulated bank?

Mr. JOHNSON. State regulated.

Mr. MCHENRY. How many separate regulators oversee your bank?

Mr. JOHNSON. We are a State non-member bank, which means we are regulated by the Office of Financial and Insurance Services in the State of Michigan, part of a Department of Commerce, and the FDIC is our Federal bank regulator.

Mr. MCHENRY. For the discussion here about the FTC being the better regulator, what is fascinating to me is you have, through the OCC, roughly 1,800 full time bank examiners out in the institu-

tions monitoring, some on a daily basis, others on a regular basis—basically 1,800 bank examiners that examine 1,850 banks.

What is fascinating to me is that you have an almost one-to-one ratio between examiners and institutions. You have some very large institutions that may have a number of examiners in them.

What many of you are testifying, Mr. Gonzalez, Mr. Plunkett and Mr. Sivon, in particular, is that the FTC would be the better protector of consumers. I think what is important in this discussion is what is the FTC capable of doing?

This committee does not have oversight over the FTC. FTC employs 1,074 people; the OCC employs 1,800 examiners.

It is a very different notion. OCC employs somewhere over 3,000 people in its entirety. The FTC only employs roughly 1,000 people. What you want to do is add all these new institutions in an area in which the FTC does not have any existing knowledge of, and say they are a better protector of the consumer.

I cannot quite understand why you believe the FTC would actually take on minute details within financial institutions when we all know the FTC largely focuses on high profile cases that actually can have a ripple effect across the economy.

Mr. Plunkett, Mr. Gonzalez, Mr. Sivon, I would love to have your response. Mr. Sivon is anxious.

Mr. SIVON. Just because I want to disassociate myself. I did not testify to that effect. I do not agree that they should be active in an enforcement role against nationally chartered banks or federally chartered thrifts. If I gave that impression, it was not my intent.

Mr. MCHENRY. My apologies.

Mr. PLUNKETT. This is our recommendation to deal with the underlying problem I mentioned, which is a pretty clearly established lack of independence, in particular, at the OCC, from the regulated institutions.

You have two issues in bringing the Federal Trade Commission in. One is unfair and deceptive acts and practices' authority, which I think they would have existing staffing to deal with, and clearly, experience to deal with.

It is not true that they do not have anything to do with banking regulation. Right now, they are charged with regulating some aspects of banking laws related to non-banking entities. For instance, credit cards offered by retail establishments and not through banks. Well, actually through banks, but not under the auspices of those banks.

Already you have some split authority between the banking regulators and the FTC, and this is our best recommendation in how to bring a more independent, certainly not perfect, but more independent agency into the process.

They would need additional funding if concurrent rule making authority was granted to bring on additional staff.

Mr. MCHENRY. Do you have any cost estimates?

Mr. PLUNKETT. No.

Mr. MCHENRY. Mr. Gonzalez?

Mr. GONZALEZ. We actually did not include this recommendation in our testimony. We have not actually done the analysis on which would be the better regulating agency.

Mr. MCHENRY. Thank you.

The CHAIRMAN. The gentleman from Missouri.

Mr. CLEAVER. Thank you, Mr. Chairman.

Mr. Johnson and Mr. Sivon, both of you mentioned financial literacy as perhaps a way to deal with the subprime and predatory lending practices. One of you suggested we may want to try to create in schools a financial literacy program.

While I agree partially with that, what would you say to this? The most unproductive schools tend to be in the areas where subprime and predatory lenders are most ravenous. Do you get the point I am making? You are saying let's put it in schools. The schools that do not work seem to be in the same areas.

Mr. SIVON. I would not profess to have any expertise in the area of education. It just struck me in preparing for this testimony and as I thought about financial literacy that the place to achieve it best would be in the school system.

It is a complex issue to drive it down to the school system given the nature of the way schools are governed today in our State based structure.

I do think it makes a great deal of sense and would solve a lot of this problem.

Mr. JOHNSON. Yes, I agree. You make a very good point about—I would stretch the point a little further to say that in most school systems, public or private, the teachers who are there, while they are very well-trained teachers, are not in and of themselves prepared to do the financial literacy education piece today.

That is something that I think the industry and the regulators can help with. I was talking before the hearing started with Congressman Green about a program that our bank participates in as well as many, many ABA member banks, and a program that Mr. Green participated in back in his district.

It is called National Teach Children to Save Day. We go into schools and start the process of here is what you do to save. Here is what the difference between a want and a need is. This is at very low elementary levels all the way up. The methods differ for grade, as you might expect.

Beyond the schools, we have an awful lot of adults out there who are not in the school system any more who also need education.

Mr. CLEAVER. That is what I wanted to deal with now, and maybe Mr. Plunkett and Mr. Gonzalez, although any of you can respond to this, one of my points of intolerance is people speeding through school zones. The signs are always clear. You are supposed to slow down when you go through a school zone because these are vulnerable pedestrians.

Do we all agree?

[Witnesses nodding affirmatively.]

Mr. CLEAVER. When we find that there are specific areas that are targeted, Mr. Gonzalez has already mentioned it for Latinos, but it is also African Americans and to a lesser degree lower income whites. Those are the areas that are targeted by the predatory lenders.

Would you support a slowing down with regard to—these are vulnerable borrowers. That you slow down when you are going through those areas? In other words, when we see that an area is being targeted, what are the negatives in requiring that before a

loan is made in these areas, that you have to do A, B and C, you have to go through some kind of educational process?

I am not talking about 2 or 3 years. I am talking about to make sure they understand what is going on.

If we slow down to protect vulnerable kids, why do we not slow down to protect vulnerable borrowers?

Mr. Gonzalez?

Mr. GONZALEZ. We would agree that we have to approach subprime lending with caution. On the other hand, we need to make sure that people who are in these areas that are ready to enter the market and to build their credit and to enter home ownership have a process to do that.

Through our home ownership counseling network, which puts people through a rigorous robust process, which for some people it means counseling them out of making this choice, we have slowed down the process, but not with the intention of keeping people out of home ownership, but with the intention of keeping them in home ownership and making sure they keep their homes.

Mr. CLEAVER. What if the lending institutions had to do it as well? La Raza does it as one of its many programs, which I am familiar with. I think it is one of the better things going. You cannot touch everyone because everybody is not going to make themselves available.

Mr. GONZALEZ. Right. Details matter with that. I would be concerned that some bigger lenders might decide not to enter that.

Mr. CLEAVER. Are you familiar with the Voting Rights Act?

Mr. GONZALEZ. Yes.

Mr. CLEAVER. What triggers the Federal involvement with regard to the Voting Rights Act is if the voter registration drops beneath a certain level, then Federal registrars are sent into the area. I think this is a problem significant enough that if we see that loans drop beneath a certain level, I think that in itself ought to attract Federal involvement.

Mr. GABERLAVAGE. I think literacy is important but I think this problem is beyond literacy. In many of the low-income and minority communities, you have older persons who try to get a loan because they need some cash flow to pay some bills and things, and not only did they not get the money, but they are losing their home, their primary asset. What happens to them in retirement? Most of these people do not have pensions. What happens to them in their old age?

We need some action on some of the practices that are occurring in these communities and stop, slow down through better regulation and stopping some of these practices that are preying on people, particularly for the older population.

The financial system is very good at marketing. It is sophisticated. It is pinpoint, it is accurate. They can tell you, oh, your CD is expiring or it is maturing, and then there have been cases where banks have marketed specifically to older persons whose CDs were expiring and they marketed variable annuities to them.

Fortunately, one of our regulators in Massachusetts, I think, stopped this practice from occurring. These were inappropriate investments.

It is very good at that, but when the consumer has a problem, particularly in all of these areas, then the response is uneven. The authority of the agencies that are charged with protecting the consumer is uneven. It should be that no matter what door a consumer goes through, whether it is a bank, a credit union, or a thrift, whatever it is, that the protection should be equivalent and it should be effective.

I think that is what we should aim for, and that would really be—it is great to have literacy, but starting in elementary school or something is not going to solve this problem of whole communities losing their equity.

Mr. CLEAVER. Thank you.

Mr. PLUNKETT. Congressman, when looking at particular problems in say, minority communities, some of the legislative proposals that your committee has looked at and that a number of members have co-sponsored, do deal with specific practices that have a particularly negative effect in those communities, such as lending without adequate consideration of the ability to repay, which has been shown in minority neighborhoods in particular to be a serious problem, because many people are getting loans at high interest rates when they could qualify for better terms.

That is one way to approach the problem as well.

Mr. CLEAVER. Thank you.

The CHAIRMAN. I will just add that the problem of people getting old without regard to their ability to pay, I believe, has been greatly enabled by securitization.

Your ability to make a loan without being concerned with someone's ability to pay is enhanced if you are not the person they have to pay. I think that is what securitization has done.

The gentleman from Colorado.

Mr. PERLMUTTER. Mr. Chairman, that was a good lead into what I wanted to say. First, I am sorry that we do not have more members here. We have had a lot of hearings on this subject, and this has been the best panel I think we have had period, just because you are all on the ground. You are worrying about both kind of the individual banker piece of this to the individual consumer.

I just want to thank you all for your testimony today.

The chairman hit on something, and Mr. Johnson, you were sort of talking about this. There is this huge distance now between the borrower and the banker in many cases.

You do not have the personal banker any more and that relationship has sort of evaporated in many instances where you call me up and you say, Mr. Perlmutter, you know, are you sure you really want to borrow this money, or this is happening with your account. You do not have that relationship as much as you used to.

It is not that I want to go back 50 years, but I think that is just something we have to deal with as Members of Congress.

Some of the comments about the over disclosure piece, and Representative Gillmor was asking about this. There are so many products available that if you try to disclose about all these different products, you have a book to read.

We have two policies that I think we have to consider, and we may have gone too far with them. It is not a question of compli-

ance. I think virtually all the banks and the credit card companies and everybody else are complying.

The policy issue is have we pushed the goal of home ownership so far that we allow one percent mortgages to get you into your house and it fails, so it is a policy issue on home ownership, and a policy issue on credit.

Have we extended credit so far with every little product possible and with some Wharton MBA in the background coming up with a new product, but also a new fee attached to that product, that people cannot keep up.

I just think the materials you all provided, your testimony today, was excellent. I am not sure what the answer is. I can tell you the polling we have done and the people that I have talked to, it is Iraq, immigration, health care and credit cards. That is it.

The credit cards, they are mad just because the fees just continue to mount up generally.

I do not mean just to give you a speech here. The issue is that the bank or the lending institution has two things on its side. It has time and education. If you have the education, you usually do not have the time to worry about the fees that you are getting charged. If you have the time, you generally do not have the education.

I have said this in other instances. You all have helped me kind of put my arms around this subject. It is sort of a distance between the banker and the borrower. It is this over disclosure because there is so many products, and the question is do we, as a Congress, want to start limiting the extension of credit, limiting home ownership or not.

If we do not, then we are going to continue to have these kinds of things, and that may be the price you pay.

I do not have any questions. I just wanted to vent.

Thank you very much. Mr. Chairman, I just want to congratulate you on putting this panel together. They are the best I have heard on this subject.

The CHAIRMAN. I appreciate that. I am reminded to include in the record, if there is no objection, a statement entitled, "Improving Federal Consumer Protection" from the National Association of Realtors.

There being no objection, it is so ordered.

I know this encountered some skepticism but sometimes congressional committees have hearings because we want to know things. That is not usually why we have hearings. Sometimes, it is. Today was a good example.

I thank all the witnesses. This was thoughtful testimony from people engaged with the issue. I hope you feel the time was well spent.

When we return from the recess in September, we will be legislating, I believe, in some of these areas. There are three. The narrowest issue, which is the subprime one, where I believe we need some legislation.

There is the broader question of consumer protection after preemption, and there is also the again narrow question of creating a consumer right to contest bad credit information.

This one, it seems to be the consumer groups and the financial institutions are somewhat aligned in their interest because what happens is the typical dispute here is between the consumer and the point of sale, and the financial institution is caught in the middle. The entity that did the sale is telling you they owe us the money and the consumer says, I do not owe you the money, and you are the collectors.

What we want to put in place is a mechanism to cut you out of that loop and let the debate happen where it should happen.

At any rate, I agree with the gentleman from Colorado. This has been a very useful hearing. I thank all the witnesses. We will be in considerable touch.

[Whereupon, at 11:38 a.m., the hearing was adjourned.]

A P P E N D I X

July 25, 2007

TESTIMONY OF TRAVIS B. PLUNKETT
LEGISLATIVE DIRECTOR, CONSUMER FEDERATION
OF AMERICA

BEFORE THE COMMITTEE ON FINANCIAL SERVICES
OF THE U.S. HOUSE OF REPRESENTATIVES

ON BEHALF OF CONSUMER ACTION, CONSUMER FEDERATION
OF AMERICA, CONSUMERS UNION, CENTER FOR RESPONSIBLE
LENDING, NATIONAL CONSUMER LAW CENTER AND THE U.S.
PUBLIC INTEREST RESEARCH GROUP

IMPROVING FEDERAL CONSUMER PROTECTIONS IN
FINANCIAL SERVICES

JULY 25, 2007

Chairman Frank, Ranking Member Bachus and Members of the Financial Services Committee, my name is Travis Plunkett and I am the Legislative Director of the Consumer Federation of America (CFA).[1] I appreciate the invitation to testify today on behalf of a number of national consumer organizations with tens of millions of members, including CFA, Consumer Action,[2] Consumers Union,[3] the publisher of Consumer Reports, the Center for Responsible Lending,[4] National Consumer Law Center[5] and the U.S. Public Interest Research Group.[6]

I commend the Committee for its diligence in examining the extremely important question of how well federal regulators are protecting consumers in the fast changing, increasingly complex financial services marketplace. This is the second hearing that the Committee has held on this topic, while many Committee and Subcommittee hearings this year have touched on regulation of important financial services markets, including mortgage lending, credit cards and other bank loans.

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[1] **Consumer Federation of America** (CFA) is a non-profit association of 300 consumer groups, with a combined membership of more than 50 million people. CFA was founded in 1968 to advance the consumer's interest through advocacy and education.

[2] **Consumer Action** (www.consumer-action.org), founded in 1971, is a San Francisco based nonprofit education and advocacy organization with offices in Los Angeles and Washington, DC. For more than two decades, Consumer Action has conducted a survey of credit card rates and charges to track trends in the industry and assist consumers in comparing cards.

[3] **Consumers Union** is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide consumers with information, education, and counsel about goods, services, health and personal finance; and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers. Consumers Union's income is solely derived form the sale of *Consumer Reports*, its other publications and services, and from noncommercial contributions, grants, and fees. In addition to reports on Consumers Union's own product testing, *Consumer Reports* with approximately 5 million paid circulation, regularly carries articles on health, product safety, marketplace economics, and legislative, judicial, and regulatory actions which affect consumer welfare. Consumers Union's publications and services carry no outside advertising and receive no commercial support.

[4] **The Center for Responsible Lending** is a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is affiliated with Self-Help, one of the nation's largest community development financial institutions.

[5] The **National Consumer Law Center** is a non-profit organization specializing in consumer issues on behalf of low-income people. NCLC works with thousands of legal services, government and private attorneys, as well as community groups and organizations, who represent low-income and elderly individuals on consumer issues.

[6] The **U.S. Public Interest Research Group** is the national lobbying office for state PIRGs, which are non-profit, non-partisan consumer advocacy groups with half a million citizen members around the country.

I. Summary of Concerns and Recommendations

Any discussion about the quality of federal financial services regulation must begin by mentioning the "elephant in the living room." The Supreme Court's recent decision in Watters vs. Wachovia Bank, N.A. represents the culmination of efforts by the Office of the Comptroller of the Currency (OCC) to cut off the long-standing ability of states to protect the consumers of national banks. OCC's preemptive efforts harm consumers because, while not perfect in many respects, states have traditionally had the experience, the regulatory infrastructure, the willingness to experiment and the desire to protect consumers. Unfortunately, the OCC has serious deficits in all of these categories. In fact, over the years, the OCC appears to have demonstrated a lot more interest and expertise in exercising preemptive authority than in protecting consumers. Our recommendation is for Congress to clarify and limit the OCC's preemptive authority, as Representative Gutierrez has proposed, restoring the ability of the states to assist in protecting consumers who purchase financial services from national banks.

We recommend a number of consumer protection standards that the Committee can use to evaluate the effectiveness of financial services regulation, whether state or federal, and to propose changes to improve federal efforts. One of the most difficult problems that the Committee will face in attempting to improve consumer protection efforts is a culture of coziness with the financial institutions they regulate at most of the agencies and an insensitivity to consumer concerns. For example, most of the regulatory failures we highlight today are in areas, like oversight of high-cost "overdraft" loans, where federal regulators have existing authority to act and have chosen not to do so. Simply increasing the authority of the agencies to write or enforce rules, or to offer a unified complaint hotline, will not change the culture in some agencies that has caused them to ignore festering problems in the credit arena or to reject adequate consumer protection measures.

In order to improve federal consumer protection efforts, serious underlying problems with this regulatory culture must be addressed, including a focus on safety and soundness regulation to the exclusion of consumer protection, the huge conflict-of-interest that some agencies have because they receive significant funding from industry sources, the balkanization of regulatory authority between agencies that often results in either very weak or extraordinarily sluggish regulation (or both) and a regulatory process that lacks transparency and accountability.

The key to addressing these root problems is to make the regulatory process more independent of the financial institutions that are regulated. This means allowing the Federal Trade Commission (FTC) to bring enforcement actions against national banks and thrifts for unfair and deceptive practices and to initiate regulation of these entities. It also means granting consumers the right to privately enforce federal laws. Finally, Congress should act to rein in lending abuses where agencies have shown an unwillingness to act vigorously, such as credit card lending, sub-prime mortgage lending and the use of deceptive and high-cost "overdraft" loans by national banks.

II. Achieving Strong Consumer Protection in the Credit Arena, Whether at the State or Federal Level

The Supreme Court's recent ruling in Watters vs. Wachovia Bank, N.A., upheld a regulation by the Department of Treasury's Office of the Comptroller of the Currency (OCC) that permits operating subsidiaries of national banks to violate state laws with impunity. The court ruled that the bank's operating subsidiary is subject to OCC superintendence – even if there effectively is none – and not the licensing, reporting and visitorial regimes of the states in which the subsidiary operates. This split 5-3 court decision all but guarantees ongoing controversy and will likely mean that federal banking regulators will be encouraged to apply federal preemption to new entities associated with national banks.

The practical effect of the exercise of far-reaching federal preemption authority as now permitted by the courts is that it prevents states from using their historical authority to protect consumers and communities in large parts of the financial services arena and leaves a huge consumer protection gap that federal regulators have not shown an inclination or an ability to fill. The OCC has even sought to prevent state attorneys general and regulators from enforcing state laws that it concedes are not preempted. The recent court ruling encourages national banks and their subsidiaries to ignore even the most reasonable of state consumer laws.

Worse still, it promotes further competition to lower consumer protections. States are already getting pressure to reduce protections in order to retain state-chartered banks, and federal regulators have an incentive to keep standards lax, in order to continue to attract the participation of large state-chartered institutions in the federal banking and thrift system.[7] We have already seen that the expanding scope of federal preemption has intensified efforts by state banks and other state regulated financial entities to ask both federal and state regulators to provide them with parallel exemptions.

The truth is that the states have many advantages when protecting consumers in the credit practices arena. States can experiment with different consumer protection approaches more easily. Americans throughout the country have been the beneficiary of this experimentation many times as effective state laws are modeled and adopted in other states and at the federal level.[8] States have the flexibility to respond to variations in problems with credit practices from region-to-region. Given their smaller districts, state legislators are more likely to be responsive to problems in the credit market that surface in certain areas, before they spread nationally. States have an infrastructure in place to license, bond, and otherwise regulate the wide variety lenders, agents, servicers and brokers that offer credit services. State and local enforcement officials are better known to the public than their federal counterparts and more likely to have the

[7] Several large national banks have chosen in recent years to convert their state charter to a national charter. Charter switches by JP Morgan Chase, HSBC and Bank of Montreal (Harris Trust) alone in 2004-05 moved over $1 trillion of banking assets from the state to the national banking system, increasing the share of assets held by national banks to 67 percent from 56 percent, and decreasing the state share to 33 percent from 44 percent. Arthur E. Wilmarth, Jr., "The OCC's Preemption Rules Threaten to Undermine the Dual Banking System, Consumer Protection and the Federal Reserve Board's role in Bank Supervision," Proceedings of the 42nd Annual Conference on Bank Structure and Competition (Fed. Res. Bank of Chicago, 2006) at 102, 105-106.

[8] Among the many examples that could be provided are The Truth in Lending Law and provisions of the Fair and Accurate Credit Transactions (FACT) Act.

personnel, experience and infrastructure to properly resolve consumer complaints about lenders and their agents.

Nonetheless, we certainly do not contend that states always provide effective consumer protection. The states have also been the scene of some notable regulatory breakdowns in recent years, such as the failure of some states to properly regulate mortgage brokers and non-bank lenders operating in the sub-prime lending market, and the inability or unwillingness of many states to rein in lenders that offer extraordinarily high-cost, short term loans and trap consumers in an unsustainable cycle of debt, such as payday lenders and auto title loan companies. Conversely, federal lawmakers have had some notable successes in providing a high level of financial services consumer protections in the last decade, such as the Credit Repair Organizations Act and the recently enacted Military Lending Act.[9]

As the Committee moves forward to examine the implications of the Watters decision on consumers and the effectiveness (or lack thereof) of federal consumer protection efforts, we urge you to use the below consumer protection principles to determine where federal consumer protection laws and regulations must be upgraded, as well as where federal efforts should accede to or partner with state regulation. These are the standards that should apply in evaluating the effectiveness of any consumer protection efforts, whether at the state or federal level.

- **Protection from unfair, deceptive and abusive practices**, including those that unjustifiably increase the cost of the credit product or expose consumers to unexpected fees and costs.
- **Protection from unsustainable debt**, as measured by the borrower's ability to re-pay the loan, caused by such factors as usury, rate gouging, or high fees.
- **Effective redress**, through a private right of action, and timely investigation and resolution of complaints by regulatory bodies, and other appropriate redress mechanisms, such as performance bonds. Access to such redress should not be blocked or unnecessarily delayed through such methods as mandatory arbitration requirements, choice-of-law contract terms, required waivers of legal rights, prohibitions on class action litigation, or unjustifiable restrictions on access to bankruptcy.
- **Strong civil enforcement** by federal and state authorities, including Attorneys General and federal consumer protection authorities, e.g. the Federal Trade Commission (FTC).
- **High standards for comparable products applied to all creditors**, whether a product is offered by a bank, a bank affiliate, a third party contracting with a bank, or a non-bank entity. Conflicting standards should always be harmonized upward to protect consumers.
- **Safety and soundness protections,** such as appropriate licensing, bonding, examination, and supervision requirements.
- **Timely, clear and complete disclosure** of all costs, as well as consumer rights and obligations and contract terms.

[9] Military Lending Act, 10 U.S.C. § 987. Credit Repair Organizations Act, 15 U.S.C. § 1679h (giving state Attorneys General and FTC concurrent enforcement authority).

III. Widespread Federal Regulatory Failures beyond the Mortgage Lending Market Have Harmed Consumers

Since the beginning of the year, a major focus of Congressional oversight of the credit market has been the serious regulatory failures at the federal and state level in the sub-prime mortgage lending market. Given the fact that at least 2.2 million homeowners with sub-prime mortgages face the prospect of losing their homes over the next several years (1 in 5 sub-prime loans issued in 2005 and 2006 are projected to default), this focus is understandable.

However, the focus on sub-prime mortgage lending may have obscured the failures of federal financial services regulators to address a number of other significant lending abuses by banks in recent years. If the Committee is to consider measures to improve consumer protection enforcement by federal financial services regulators, it is necessary to be aware of how and why these abuses have been allowed to continue.

A. The Federal Reserve Board and Office of the Comptroller of the Currency Have Done Very Little Beyond Proposing New Disclosures to Address Abusive Practices and Reckless Lending in the Credit Card Market

The Subcommittee on Financial Institutions and Consumer Credit has conducted two very comprehensive hearings on the impact of current credit card issuer practices on consumers. The Committee heard testimony from academics and consumer representatives regarding abusive lending practices that are widespread in the credit card industry, including:

- The unfair application of penalty and "default" interest rates that can rise above 30 percent;
- Applying these interest rate hikes retroactively on existing credit card debt, which can lead to sharp increases in monthly payments and force consumers on tight budgets into credit counseling and bankruptcy;
- High and increasing "penalty" fees for paying late or exceeding the credit limit. Sometimes issuers use tricks or traps to illegitimately bring in fee income, such as requiring that payments be received in the late morning of the due date or approving purchases above the credit limit;
- Aggressive credit card marketing directed at college students and other young people;
- Requiring consumers to waive their right to pursue legal violations in the court system and forcing them to participate in arbitration proceedings if there is a dispute, often before an arbitrator with a conflict of interest; and
- Sharply raising consumers' interest rates because of a supposed problem a consumer is having paying another creditor. Even though few credit card issuers now admit to the discredited practice of "universal default," eight of the ten largest credit card

issuers continue to permit this practice under sections in cardholder agreements that allow issuers to change contract terms at "any time for any reason."[10]

The Subcommittee also heard about the inaction of banking regulators in responding to these problems in the credit card marketplace:

- The Federal Reserve Board (FRB) has proposed new disclosure regulations under Regulation Z of the Truth in Lending Act (TILA). Although these proposed disclosures are positive and many respects and will make it easier to understand credit card terms and conditions, they will not include all of the information necessary to help consumers make informed choices. Most importantly, the disclosures won't stem the most abusive practices in the market.[11]
- The OCC has taken public enforcement action against a major credit card issuer only twice in recent years. The best-known case involved deceptive marketing practices by Providian. However, this occurred only after the San Francisco District Attorney and California Attorney General initiated action against Providian.[12]
- "In contrast to this absence of public enforcement action by the OCC against major national banks, state officials and other federal agencies have issued numerous enforcement orders against leading national banks or their affiliates, including Bank of America, Bank One, Citigroup, Fleet, JP Morgan Chase, and US Bancorp – for a wide variety of abusive practices over the past decade…"[13]

The OCC and FRB have also been largely silent while credit card issuers expanded efforts to market and extend credit at a much faster speed than the rate at which Americans have taken on credit card debt. This credit expansion has had a disproportionately negative effect on the least sophisticated, highest risk and lowest income households. It has also resulted in both relatively high losses for the industry and record profits. That is because, as mentioned above, the industry has been very aggressive in implementing a number of new – and extremely costly – fees and interest rates.[14] Although the agencies did issue significant guidance in 2003 to require issuers to increase the size of minimum monthly payments that issuers require consumers to pay,[15] neither agency has proposed any actions (or asked for the legal authority to do so) to rein in aggressive lending or unjustifiable fees and interest rates.

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[10] Testimony of Linda Sherry of Consumer Action, House Subcommittee on Financial Institutions and Consumer Credit, April 26, 2007.
[11] Testimony of Kathleen E. Keest, Center for Responsible Lending, U.S. House Committee on Financial Services Subcommittee on Financial Institutions and Consumer Credit, June 7, 2007.
[12] Testimony of Edmund Mierzwinski, U.S. Public Interest Research Group, Subcommittee on Financial Institutions and Consumer Credit of the Financial Services Committee, June 2, 2007.
[13] Testimony of Arthur E. Wilmarth, Jr., Professor of Law, George Washington University Law School, April 26, 2007.
[14] Testimony of Travis B. Plunkett of the Consumer Federation of America, Senate Banking Committee, January 25, 2007.
[15] Joint Press release of Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency and Office of Thrift Supervision, "FFIEC Agencies Issue Guidance on Credit Card Account Management and Loss Allowance Practices," January 8, 2003, see attached "account Management and Loss Allowance Guidance" at 3.

B. The Federal Reserve has Allowed Debit Card Cash Advances ("Overdraft Loans") without Consent, Contract, Cost Disclosure or Fair Repayment Terms

The FRB has refused to require banks to comply with the Truth in Lending Act (TILA) when they loan money to customers who are permitted to overdraw their accounts. While the FRB issued a staff commentary clarifying that TILA applied to payday loans, the Board refused to apply the same rules to banks that make nearly identical loans. As a result, American consumers spent $17.5 billion last year on cash advances from their banks without signing up for the credit, getting cost-of-credit disclosures, or a contract that the bank would in fact pay overdrafts. Consumers are induced to withdraw more cash than they have in their account at ATMs and spend more than they have with debit card purchases at point of sale. In both cases, the bank could simply deny the transaction, saving consumers average fees of $34 each time.

The FRB has permitted banks to avoid TILA requirements because bankers claim that systematically charging unsuspecting consumers very high fees for overdraft loans they did not request is the equivalent to occasionally covering the cost of a paper check that would otherwise bounce. Instead of treating short term bank loans in the same manner as all other loans covered under TILA, as consumer organizations recommended, the FRB issued regulations under the Truth in Savings Act, pretending that finance charges for these loans were bank "service fees." Once again, national consumer organizations provided well-researched comments, urging the Federal Reserve to place consumer protection ahead of bank profits, to no avail.

As a result, consumers unknowingly borrow billions of dollars at astronomical interest rates. A $100 overdraft loan with a $34 fee that is repaid in two weeks costs 910 percent APR. The use of debit cards for small purchases often results in consumers paying more in overdraft fees than the amount of credit extended.

Cash advances on debit cards are not protected by the Truth in Lending Act prohibition on banks using set off rights to pay themselves out of deposits into their customers' accounts. If the purchase involved a credit card, on the other hand, it would violate federal law for a bank to pay the balance owed from a checking account at the same bank. Banks routinely pay back debit card cash advances to themselves by taking payment directly out of consumers' checking accounts, even if those accounts contain entirely exempt funds such as Social Security.

C. Despite Advances in Technology, the Federal Reserve has Refused to Speed up Availability of Deposits to Consumers

Despite rapid technological changes in the movement of money electronically, the adoption of Check 21 to speed check processing, and electronic check conversion at the cash register, the Federal Reserve has failed to shorten the amount of time that banks are allowed to hold deposits before they are cleared. Money flies out of bank accounts at warp speed. Deposits crawl in. Even cash that is deposited over the counter to a bank teller can be held for 24 hours before becoming available to cover a transaction. The second business day rule for local checks means that a low-income worker who deposits a pay check on Friday afternoon will not get access to funds until the following Tuesday. If the paycheck is not local, it can be held for five business days. This long time period applies even when the check is written on the same bank

where it is deposited. Consumers who deposit more than $5,000 in one day face an added wait of about five to six more business days. Banks refuse to cash checks for consumers who do not have equivalent funds already on deposit. The combination of unjustifiably long deposit holds and banks' refusal to cash account holders' checks pushes low income consumers towards check cashing outlets, where they must pay 2 to 4 percent of the value of the check to get immediate access to cash.

Consumer groups have called on the Federal Reserve to speed up deposit availability and to prohibit banks from imposing overdraft or NSF fees on transactions that would not have overdrawn if deposits had been available. The Federal Reserve vigorously supported Check 21 to speed up withdrawals but has refused to shorten deposit hold periods for consumers.

D. The Federal Reserve has Supported the Position of Payday Lenders and Telemarketing Fraud Artists by Permitting Remotely Created Checks (Demand Drafts) to Subvert Consumer Rights Under the Electronic Funds Transfer Act

In 2005, the National Association of Attorneys General, the National Consumer Law Center, Consumer Federation of America, Consumers Union, the National Association of Consumer Advocates, and U. S. Public Interest Research Group filed comments with the Federal Reserve in Docket No. R-1226, regarding proposed changes to Regulation CC with respect to demand drafts. Demand drafts are unsigned checks created by a third party to withdraw money from consumer bank accounts. State officials told the FRB that demand drafts are frequently used to perpetrate fraud on consumers and that the drafts should be eliminated in favor of electronic funds transfers that serve the same purpose and are covered by protections in the Electronic Funds Transfer Act. Fraudulent telemarketers increasingly rely on bank debits to get money from their victims. The Federal Trade Commission has reported that 25 percent of all fraud complaints received by the agency in 2004 involved a bank debit, an increase of 40 percent in just one year. Since automated clearinghouse transactions are easily traced, fraud artists prefer to use demand drafts.

Remotely created checks are also used by telemarketers and others to remove funds from checking accounts that receive the protections of the Electronic Funds Transfer Act. CFA issued a report on Internet payday lending in 2004 and documented that some high-cost lenders converted debts to demand drafts when consumers exercised their EFTA right to revoke authorization to electronically withdraw money from their bank accounts. CFA brought this to the attention of the Federal Reserve in 2005, 2006 and 2007. No action has been taken to safeguard consumers' bank accounts from unauthorized unsigned checks or conversion of an obligation from an electronic funds transfer to a demand draft to thwart EFTA protections.

E. The Federal Reserve Has Taken No Action to Safeguard Bank Accounts from Internet Payday Lenders

In 2006, consumer groups met with Federal Reserve staff to urge them to take regulatory action to protect consumers whose accounts were being electronically accessed by Internet payday lenders. We joined with other groups in a follow up letter in 2007, urging the Federal Reserve to make the following changes to Regulation E:

- Clarify that remotely created checks are covered by the Electronic Funds Transfer Act.
- Ensure that the debiting of consumers' accounts by internet payday lenders is subject to all the restrictions applicable to preauthorized electronic funds transfers.
- Prohibit multiple attempts to "present" an electronic debit.
- Prohibit the practice of charging consumers a fee to revoke authorization for preauthorized electronic funds transfers.
- Amend the Official Staff Interpretations to clarify that consumers need not be required to inform the payee in order to stop payment on preauthorized electronic transfers.

While FRB staff has been willing to discuss these issues, the FRB has taken no action to safeguard consumers when Internet payday lenders and other questionable creditors evade consumer protections or exploit gaps in the Electronic Funds Transfer Act to mount electronic assaults on consumers' bank accounts.

F. The Banking Agencies Have Failed to Stop Banks From Imposing Unlawful Freezes on Accounts Containing Social Security and Other Funds Exempt from Garnishment

Mr. Chairman, we applaud you for urging federal banking regulators to take action regarding recent reports that national banks are not complying with the Social Security Act's prohibition on the garnishment of Social Security and Veteran's benefits. These federal benefits (as well as state equivalents) are taxpayer dollars targeted to relieve poverty and ensure minimum subsistence income to the nation's workers. Despite the purposes of these benefits, banks routinely freeze bank accounts containing these benefits pursuant to garnishment or attachment orders, and assess expensive fees – especially insufficient fund (NSF) fees – against these accounts.

The number of people who are being harmed by these practices has escalated in recent years, largely due to the increase in the number of recipients whose benefits are electronically deposited into bank accounts. This is the result of the strong federal policy to encourage this in the Electronic Funds Transfer Act. And yet, the banking agencies have failed to issue appropriate guidance to ensure that the millions of federal benefit recipients receive the protections they are entitled to under federal law.

G. The Comptroller of the Currency Permits Banks to Manipulate Payment Order to Extract Maximum Bounced Check and Overdraft Fees, Even When Overdrafts are Permitted

The Comptroller of the Currency permits national banks to rig the order in which debits are processed. This practice increases the number of transactions that trigger an overdrawn account, resulting in higher fee income for banks. When banks began to face challenges in court to the practice of clearing debits according to the size of the debit -- from the largest to the smallest --rather than when the debit occurred or from smallest to largest check, the OCC issued guidelines that allow banks to use this dubious practice.

The OCC issued an Interpretive Letter allowing high-to-low check clearing when banks follow the OCC's considerations in adopting this policy. Those considerations include: the cost incurred by the bank in providing the service; the deterrence of misuse by customers of banking

services; the enhancement of the competitive position of the bank in accordance with the bank's business plan and marketing strategy; and the maintenance of the safety and soundness of the institution.[16] None of the OCC's considerations relate to consumer protection.

The Office of Thrift Supervision (OTS) addressed manipulation of transaction-clearing rules in the Final Guidance on Thrift Overdraft Programs issued in 2005. The OTS, by contrast, advised thrifts that transaction-clearing rules (including check-clearing and batch debit processing) should not be administered unfairly or manipulated to inflate fees.[17] The Guidelines issued by the other federal regulatory agencies merely urged banks and credit unions to explain the impact of their transaction clearing policies. The Interagency "Best Practices" state: "Clearly explain to consumers that transactions may not be processed in the order in which they occurred, and that the order in which transactions are received by the institution and processed can affect the total amount of overdraft fees incurred by the consumers."[18]

CFA and other national consumer groups wrote to the Comptroller and other federal bank regulators in 2005 regarding the unfair trade practice of banks ordering withdrawals from high-to-low, while at the same time unilaterally permitting overdrafts for a fee. One of the OCC's "considerations" is that the overdraft policy should "deter misuse of bank services." Since banks deliberately program their computers to process withdrawals high-to-low and to permit customers to overdraw at the ATM and Point of Sale, there is no "misuse" to be deterred.

No federal bank regulator took steps to direct banks to change withdrawal order to benefit low-balance consumers or to stop the unfair practice of deliberately causing more transactions to bounce in order to charge high fees.

IV. The OCC's Consumer Assistance Efforts are Weak

A. The Consumer Assistance Group

The OCC's approach to handling consumer complaints against national banks is unfortunately illustrative of the agency's disappointing overall record in consumer protection. The OCC was established to supervise national banks and its primary focus continues to be on maintaining the safe and sound operation of these banks. However, the OCC also has been assigned important consumer protection responsibilities. Most notably, under the Federal Trade Commission Act, the agency is directed to protect consumers from unfair and deceptive practices by national banks. Further, enforcement of other applicable consumer protection, fair lending and community reinvestment laws and regulations is handled through the bank examination process.

Another consumer responsibility is the processing and disposition of consumer complaints against national banks. This function is largely handled through the OCC's Customer Assistance Group (CAG) which operates a single national call center in Houston, Texas. The

[16] 12 C.F.R. 7.4002(b).
[17] Office of Thrift Supervision, Guidance on Overdraft Protection Programs, February 14, 2005, p. 15.
[18] Dept. of Treasury, Joint Guidance on Overdraft Protection Programs, February 15, 2005, p. 13.

agency's self-described approach to processing consumer complaints is one of a "neutral arbiter." Yet the CAG seems to primarily function as a channel for funneling consumer complaints to national banks. A 2006 U.S. General Accountability Office (GAO) report issued last year found that, as with the other banking regulators, the OCC resolves most of the complaints it receives mostly by providing clarifying information to bank customers.[19] The agency investigates or makes determinations about whether the customer or bank erred less frequently. The GAO report also found that while the OCC receives a greater volume of complaints than other regulators, it lacked a mechanism for gathering consumer feedback on how helpful they were.

CFA and other national consumer groups long have questioned the adequacy of the OCC's complaint system. Our concerns are heightened particularly by the agency's preemption rules that give it exclusive authority for supervising non-bank subsidiaries of national banks. This new authority exponentially increases the number of financial institutions that the OCC's complaint process now has primarily responsibility for handling.

The Houston complaint center historically has been understaffed and, for a time, was only open to the public for limited daily hours four days a week. Criticism from the Chairman and other committee members has prodded the OCC to take some steps aimed at addressing these concerns. For example, several years ago the OCC increased the number of full-time-equivalent CAG staff to fifty, more than doubling its previous staff. However, even this expanded staff still represents less than two percent of the OCC's total workforce of more than 2,800 employees (1,900 of which serve as bank examiners).

The CAG service hours also were increased from 7 to 12 hours a day and we understand that the Houston office now operates a full five-day schedule. (The agency says that the expanded service hours require it to use a third-party vendor to provide initial intake on complaints). Just weeks ago, the OCC finally redesigned the consumer complaint website.

Last year, CFA staff visited the Houston call center. We were impressed with the professionalism of the CAG staff we met that day. Yet we were disappointed to learn that the information collected from consumer complaints are apparently used only at the case-specific level. Agency officials indicated that complaints against specific national banks were sometimes used in developing upcoming compliance exams. However, no concrete examples were provided of instances in which the agency analyzed the overall pattern of complaints against varying institutions and utilized the complaints it received to develop new regulatory guidance or issue new rules for national banks.

In short, the OCC's record is as passive in providing consumer assistance as it is in other areas of consumer enforcement.

B. Consumer Assistance Website

[19] U.S. Accountability Office, "OCC Consumer Assistance: Process is Similar to That of Other Regulators but Could Be Improved by Enhanced Outreach," GAO-06-293 (February 2006).

Just last week, OCC rolled out a new website (http://www.helpwithmybank.gov/) with fanfare, as a tool for consumers with questions or concerns about their bank.[20] Unfortunately, there is less there than meets the eye in both cases. Indeed, a review of the FAQs on the new "Help" site concerning some of the issues that are most problematic for consumers today suggest that it is possible that the site itself may actually discourage consumers from making complaints. For example, on the issue of manipulating payment order of debits to maximize fees, a problem discussed above, here is what the "Help With My Bank" site says:

> **My bank paid my largest check first and then the smaller ones. Doing so created more overdraft fees on my account. Why did the bank pay in this order?**
>
> > You may write your checks in numerical order, but that doesn't mean the bank will post them that way. The same is true with point-of-sale or other electronic transactions: They don't necessarily post in the order in which you made the purchases.
> >
> > When several items come to the bank for clearing, it can choose to debit them from your account in several ways. Many national banks are opting to post the largest dollar items first instead of posting the checks in numerical order. Often the largest check represents payment for rent, mortgage, car payments, or insurance premiums.
> >
> > If your bank adopts this policy throughout its territory, it normally will notify you via your statement.

Another bank practice which increasingly has been attracting attention is the institutions' encouragement of overdrafts to maximize their revenues.[21] Indeed, banks advertise the ability to have overdrafts covered, seducing their customers into taking advantage of that "convenience." Yet here is what the OCC says to the consumer:

> **I wrote a check that was returned because of insufficient funds (NSF) in my account. But the bank never notified me, so other checks bounced and I got hit with several overdraft fees. Shouldn't the bank have sent me a notice?**
>
> > The bank is not required to notify you when a check bounces. You are responsible for keeping a current and accurate check/transaction register. By balancing it with your monthly statement, you will know your account balance and prevent overdrafts.

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[20] "*Comptroller of the Currency Launches Web Site to Help National Bank Customers,*" NR-2007-73 (July 17, 2007), ,http://www.occ.treas.gov/ftp/release/2007-73.htm.

[21] *See, e.g.* Eric Halperin and Peter Smith, *Out of Balance: Consumers Pay $17.5 Billion Per Year in Fees for Abusive Overdraft Loans,*" Center for Responsible Lending (July 11, 2007), http://www.responsiblelending.org/pdfs/out-of-balance-report-7-10-final.pdf.

> State laws generally provide that it is illegal to write a check—knowingly or negligently—without having sufficient funds to cover the check *on the day you write it.*

And for consumers who do try to keep their checkbook balanced and up-to-date, in accordance with the OCC's suggestion? Here's the OCC's advice:

How can my account be overdrawn when I just made a deposit?

> Many transactions are processed overnight. These transactions may not be reflected in an available balance.
>
> Thus it's important to keep a current and accurate check/transaction register and balance it to your monthly statement. A bank's online, telephone, or ATM balances are for information purposes only—they do *not* replace your check/transaction register.
>
> On checking accounts, banks generally post deposits before withdrawals. However, there are no laws requiring national banks to do this. In addition, banks may establish a cutoff time for deposits made at a branch or through an ATM. Deposits made after that time may be treated as having been made on the following business day.
>
> For example, a deposit made after the Friday afternoon cutoff time would be treated as if it were made on the following Monday. So any items with next-day availability would then be available the next day (Tuesday).

But can the bank still charge the overdraft fee in that case?

Can the bank charge an overdraft fee while there is a deposit pending?

> Yes. Many transactions are processed overnight. These transactions may not be reflected in an available balance.
>
> This is why it's important to keep a current and accurate check/transaction register and balance it to your monthly statement. A bank's online, telephone, or ATM balances are for information purposes only—they do *not* replace your check/transaction register.
>
> On checking accounts, banks generally post deposits before withdrawals. However, the law does not require this. In addition, banks may establish a cutoff time for deposits made at a branch or through an ATM. Deposits made after that time may be treated as having been made on the following business day.

> For example, a deposit made after the Friday afternoon cutoff time would be treated as if it were made on the following Monday. So any items with next-day availability would then be available the next day (Tuesday).

A consumer victimized by multiple overdraft fees could be forgiven for taking away this message: "There's no point in complaining, because the bank can do whatever it wants."

Consumers, advocates and state regulators have long noticed that card issuers are either themselves ignorant of, or do not honor, special rights that consumers have when they have a dispute with a merchant over goods or services purchased with a credit card. This right allows consumers to assert the claims and defenses arising out of a credit card purchase of goods or services against the card issuer.[22] The rules for asserting these claims are different than the standard "billing error" rights.[23] We were unable to find any reference at all to this important consumer right in the portion of the "Help With My Bank" section labeled "credit cards dispute."

If, on balance, the overall message of the new website is that there's not much point in filing a complaint, there is also little heart to be taken from the complaint process itself. Apart from the question of whether the resources are adequate, the consumer complaint page on the OCC's website discourages consumers from complaining about situations which, it should be hoped, the OCC would most want to be made aware of: the possibility that a bank was engaging repeatedly in misrepresentations or violations of contractual obligations. Yet the website discourages consumers from do so, instead simply telling them to get a lawyer:[24]

> **When You Need Other Help**
>
> Many complaints stem from factual or contract disputes between the bank and the customer. Only a court of law can resolve those disputes and award damages. If your case involves such a dispute, we will suggest that you consult an attorney for assistance.

Assuming that the consumer does file a complaint, despite all this discouragement, the OCC now explains that it would be illegal for them to tell the consumer if the bank violated the law with respect to the action about which the consumer complained.

> **Can the OCC help me find out if a bank has been cited for a violation of a regulation or law?**
>
> According to Federal law, results of examinations are considered confidential. The OCC cannot release any information relating to any supervisory actions *or regarding whether a violation of law or regulation occurred in connection with your complaint.* [**emphasis added**]

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[22] 15 U.S.C. § 1666i; Reg. Z, § 226.12(c)

[23] 15 U.S.C. § 1666, Reg. Z, § 226.13. For example, there is a 60-day time limit for the consumer to dispute a billing error. There is no flat 60-day time limit for the merchant-related dispute, though there are other restrictions.

[24] http://www.occ.treas.gov/customer.htm#The%20OCC's%20Complaint%20Process.

However, you can look for two kinds of information on our Web site, www.occ.gov:

- whether a bank is in compliance with the Community Reinvestment Act (CRA)
- whether a bank is subject to an enforcement action[25]

It is possible that the OCC's overall discouraging approach to hearing complaints about their banks reflects the poor odds that it would do the consumer any good to make the effort. Results from a GAO study indicate that customer complaints are rarely resolved in the consumer's favor.[26] Overall, the message from the OCC to consumers seems to be, "you're on your own."

V. "Principles-Based" Regulation Leaves Consumers Vulnerable to Lax Enforcement

Some federal regulators have contended that their unwillingness to adopt regulations proscribing specific unfair and deceptive practices that are forbidden in the Federal Trade Commission (FTC) Act and Home Ownership and Equity Protection Act (HOEPA) is actually an advantage for consumers, allowing regulators to nimbly apply broad-based legal requirements on a case-by-case basis. Such case-by-case enforcement based on broad legal principals, they say, makes it more difficult for financial institutions to maintain technical compliance with the letter of the law, while violating its spirit.[27]

In our experience, industry representatives who advocate a principles-based approach to regulation often have weakened consumer protections as their real goal. That certainly appears to be the case in recent calls to adopt a principles-based approach to securities regulation as a way to make our securities markets more competitive internationally. Moreover, in practice, the principles-based approach has been shown to have inherent weaknesses that more than outweigh the purported advantages of streamlined rules and greater regulatory flexibility.

Ideally, under a principles-based approach, regulations clearly define the outcome regulated entities are expected to achieve, and regulators hold them accountable for achieving that outcome. Under such an approach, one could in theory hold a company accountable for filing financial statements that fail to fairly present the company's financial status, or hold a bank accountable for misleading borrowers, for example, without having to prove that any rule was broken. Aggressively implemented, such an approach could in theory provide for effective consumer protection regulation.

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[25] http://www.helpwithmybank.gov/faqs/other_occ_help.html#drop02.

[26] Referring to a 2006 GAO Review of "OCC Consumer Assistance," (GAO-06-293): "What stands out in the 41-page report is that bank regulators rarely stick up for the consumer." Gail Liberman and Alan Lavine, *Regulators RarelyBlame Banks,"* MarketWatch, (April 3, 2006), http://www.marketwatch.com/

[27] "To be effective, rules must have broad enough coverage to encompass a wide variety of circumstances so that they are not easily circumvented. At the same time, rules with broad prohibitions could limit consumers' financing options in legitimate cases that do not meet the required legal standard. That has led the Federal Reserve to focus primarily on addressing potentially unfair or deceptive practices by using its supervisory powers on a case-by-case basis rather than through rulemaking." Statement of Randall S. Kroszner, Member, Board of Governors of the Federal Reserve System before the Committee on Financial Services, U.S. House of Representatives, June 13, 2007.

There are several problems with this approach, however. One is that it relies on regulators to be far more aggressive in holding companies accountable than the banking regulators have shown themselves to be. A second problem is that it moves decisions about what constitutes non-compliant behavior out of the relatively transparent public rulemaking process into backroom negotiations between the regulator and the regulated entity. Observation of the United Kingdom's experiment with principles-based regulation suggests that the likely result of making decisions about the enforcement of regulatory policy behind closed doors will be lax enforcement.

If, on the contrary, regulators were to attempt to adopt a tough approach to enforcement under a principles-based regulatory regime, the lack of clarity in the principles-based approach is likely to result in a large number of disputes between the regulator and regulated entities. In such cases, the task of interpreting regulations may ultimately fall to the courts. That has the disadvantage of being both costly and time-consuming, and of removing decisions about the best approach to regulation from the expert regulators.

The recent forays into principles-based regulation in the securities area suggests another potential problem – the lack of principle in principles-based regulation. Both the recently revised management guidance on Section 404 of the Sarbanes-Oxley Act, and the revised audit standard for internal controls audit, have been touted as adopting a principles-based approach to regulation. However, neither the management guidance nor the proposed audit standard is founded on clearly articulated principles that managers and auditors could be held accountable for achieving. Instead, they spend a great deal of time explaining what managers and auditors will not be held accountable for failing to do. If this is an example of what we can expect of principles-based financial services regulation, our skepticism regarding this approach seems more than justified.

Finally, those who call for principles-based regulation typically ignore both the degree to which our rules-based system is founded on strong underlying principles and the degree to which principles-based systems must rely on "guidance" to provide clarity that the principles alone cannot convey. Ironically, the same parties who have advocated a more principles-based approach to securities regulation have also argued for greater clarity in two areas where a principles-based approach has been adopted – the definitions of materiality and scienter. This further illustrates what we found to be the case – that the support for principles-based regulation tends to be more theoretical than real, and that the last thing most regulated entities want is a regulatory system that defines general consumer protection principles and holds them accountable when they fail to achieve them.

VI. Identifying the Underlying Causes of Federal Regulatory Failures

It would be easy to blame the federal regulatory failures in the credit practices arena solely on the lack of legal or enforcement authority for federal banking agencies, but this would not be true. Although our groups do recommend that Congress enact new consumer protection laws, especially regarding credit card abuses, and that it increase the legal jurisdiction granted to

the FTC in the credit arena, underlying problems that have caused poor federal enforcement will not be solved simply by giving new authority to the same banking agencies.

Most of the regulatory failures cited above are in areas where federal regulators have existing authority to act, and have chosen not to do so. Simply increasing the authority of the agencies to write or enforce rules, or to offer a unified complaint hotline, will not change the culture in some agencies that has caused them to ignore festering problems in the credit arena or to reject adequate consumer protection measures. In fact, by raising expectations of reform and then not following through, such changes could actually be harmful by impeding meaningful reform. In order to fashion effective federal remedies consistent with the above consumer protection standards, the underlying problems with the regulatory culture at the federal banking agencies must also be addressed. These problems include:

1. **An overwhelming focus on safety and soundness regulation, often to the exclusion of consumer protection**. All four of the primary banking regulatory agencies examine and supervise banks.[28] A major focus of this supervision is the financial safety and soundness of the institutions. These agencies are also charged with enforcing consumer protection laws that affect the institutions they supervise, but in many cases do not appear to make consumer protection a significant budget or strategic priority.[29] The obvious problem with vesting both safety and soundness and consumer protection with a single agency is that the agency might well view the two goals as in conflict or place too high a priority on safety and soundness enforcement.[30] As illustrated above regarding the FRB's inaction on bounce loans, an agency focused almost exclusively on what is financially beneficial for banks would likely view a restriction on bank loan income as a threat to the bank's financial stability, even if the practice in question is financially harmful to consumers.

2. **Significant funding from industry sources represents a major conflict-of-interest**. None of the banking agencies receive appropriated funds from Congress. The OCC and OTS receive virtually all of their income from direct assessments on the institutions they supervise. The FDIC is funded by premiums that banks and thrift institutions pay for deposit insurance coverage and from earnings on investments in Treasury securities. The Federal Reserve System receives the greatest portion of its income from interest earned on government securities, but it does receive substantial income from what it calls "priced

[28] The OCC and OTC charter and supervise national banks, and thrifts, respectively. State chartered banks can choose whether to join and be examined and supervised by either the Federal Reserve System or the Federal Deposit Insurance Corporation (FDIC). The FTC is charged with regulating some financial practices in the non-bank sector, such as credit cards offered by department stores and other retailer.

[29] The OTS, for example, cites consumer protection as part of its "mission statement" and "strategic goals and vision." However, in identifying its eight "strategic priorities" for how it will spend its budget in Fiscal Year 2007, only part of one of these priorities appears to be directly related to consumer protection ("data breaches"). On the other hand, OTS identifies both "Regulatory Burden Reduction" and "Promotion of the Thrift Charter" as major strategic budget priorities. Office of Thrift Supervision, "OMB FY2007 Budget and Performance Plan," January 2007.

[30] Safety and soundness concerns at times can lead to consumer protection, as in the eventually successful efforts by federal banking agencies to prohibit "rent-a-charter" payday lending, in which payday loan companies partnered with national or out-of-state banks in an effort to skirt restrictive state laws. However, from a consumer protection point-of-view, this multi-year process took far too long. Moreover, the outcome could have been different if the agencies had concluded that payday lending would be profitable for banks and thus contribute to their soundness.

services to depository institutions," bank examinations, inspections and risk assessments of bank holding companies.[31]

Given that it supervises the largest financial institutions in the country, the OCC's funding situation is the most troublesome. (See Appendix C for more information on the OCC's funding, conflicts-of-interest and regulatory failures.) As highlighted above, the OCC has not initiated a public enforcement order against any of the eight largest national banks for violating consumer credit laws since early 1995. As Professor Arthur Wilmarth said in his testimony before the Financial Institutions and Consumer Credit Subcommittee:

More than 95% of the OCC's budget is financed by assessments paid by national banks, and the twenty biggest national banks account for nearly three-fifths of those assessments. Large, multi-state banks were among the most outspoken supporters of the OCC's preemption regulations and were widely viewed as the primary beneficiaries of those rules. In addition to its preemption regulations, the OCC has frequently filed amicus briefs in federal court cases to support the efforts of national banks to obtain court decisions preempting state laws. The OCC's effort to attract large, multi-state banks to the national system have already paid handsome dividends to the agency....Thus, the OCC has a powerful financial interest in pleasing its largest regulated constituents, and the OCC therefore faces a clear conflict of interest whenever it considers the possibility of taking an enforcement action against a major national bank.[32]

3. **Regulatory balkanization leads to downward pressure on consumer protections, often resulting in "lowest common denominator" regulation. On the other hand, when agencies do collaborate to raise standards, the process can take so long as to make eventual regulatory action far less helpful for consumers.** The present regulatory system for credit practices is institution-centered, rather than consumer-centered. It is structured according to increasingly irrelevant distinctions between the type of institution that is lending money, rather than the type of product being offered to consumers. Agency charter "shopping" is not a viable option in most cases for national banks, but it can be for thrifts and for state chartered banks, which can and do choose between supervision by the Federal Reserve system and the FDIC[33] and, as explained above, between a state and national charter. Regulators often appear to be more concerned that the requirements they place on the institutions they regulate – even if highly justified for consumer protection purposes – might be viewed by these institutions as a "regulatory burden." All of the banking agencies cite "reducing regulatory burden" as a priority and often appear to compete to do so, even if it means that important protections are reduced.

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[31] In 2006, this income was $909 million. "Federal Reserve Release," January 9, 2007. This amount was about one-third of the just under $3 billion in operating costs for the entire Federal Reserve System. Board of Governors of the Federal Reserve System, "Annual Report: Budget Review," April 2007.

[32] Testimony of Arthur E. Wilmarth, Jr., Professor of Law, George Washington University Law School, April 26, 2007.

[33] For example, the First Bank of Delaware dropped its Federal Reserve member bank status and switched to supervision by the FDIC to continue its rent-a-bank payday lending operation.

When agencies do collaborate to apply consumer protections consistently to the institutions they regulate, the process can be staggeringly slow. For example, as credit card debt loads began to increase for Americans in the mid and late 1990s, consumer organizations and credit experts began to issue serious warnings that the lower minimum payment amounts that all credit card issuers were offering their cardholders were contributing to the sharp increase in the number of consumer bankruptcies.34 It wasn't until January 2003 that regulators issued guidance recommending that credit card lenders increase the size of the minimum payment amounts so that consumers would "amortize the current balance over a reasonable period of time," noting that prolonged negative amortization would be subject to bank examiner criticism.35 Issuers were not required to fully phase in the changes until the end of 2006, close to a decade after initial concerns were raised. Another obvious example of a sluggish regulatory process that has harmed consumers is the federal delay in issuing regulations to deal with the serious and well-publicized problems in the sub-prime mortgage lending market.

4. **An undue focus on bank examination instead of enforcement, which lacks transparency and effectiveness.** Bank regulators have said repeatedly to this Committee and others that the process of supervision and examination results in a superior level of consumer protection to taking enforcement action against institutions that violate laws or rules. For example, Comptroller of the Currency John Dugan told this Committee on June 13th that "...ours is not an 'enforcement-only' compliance regime – far better to describe our approach as "'supervision first, enforcement if necessary,' with supervision addressing so many early problems that enforcement is not necessary."[36] Given the widespread consumer abuses in the credit card market documented above and the OCC's ineffectual regulation of national banks like Providian that committed these abuses, this claim is simply not supported by the facts.

   There is another serious problem with relying almost exclusively on the examination process to require national banks to comply with laws and regulations: the process is highly discretionary and not open to public view.

   > Findings made during compliance examinations are strictly confidential and are not made available to the public except at the OCC's discretion. Similarly, the OCC is not required to publish the results of its safety-and-soundness orders....Thus, the OCC's procedures for compliance examinations and safety-and-soundness orders do not appear to provide any public notice or other recourse to consumers who have been injured by violations identified by the OCC.[37]

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[34] Day, Kathleen and Caroline E. Mayer, "Credit Card Penalties, Fees Bury Debtors," *Washington Post*, March 6, 2005.

[35] Joint Press release of Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency and Office of Thrift Supervision, "FFIEC Agencies Issue Guidance on Credit Card Account Management and Loss Allowance Practices," January 8, 2003, see attached "account Management and Loss Allowance Guidance" at 3.

[36] Testimony of John C. Dugan, Comptroller of the Currency, Before the Committee on Financial Services of the U.S. House of Representatives," June 13, 2007.

[37] Testimony of Arthur E. Wilmarth, Jr., Professor of Law, George Washington University Law School, April 26, 2007.

At best, these factors combine to create a culture of coziness with regulated institutions at many of the agencies. At worst, as in the case of the OCC, they appear to have led to regulatory capture.

VII. Recommendations

All of our recommendations are directed at creating a more independent enforcement and regulatory process that is more focused on consumer protection. Unless the underlying causes of federal regulatory failures are addressed to achieve greater independence from regulated institutions and to grant more power to consumers to enforce the law, protections for consumers will not improve. Greater regulatory independence will also mean that some of the meritorious ideas that the Committee has been considering that are not mentioned below, such as a "one stop shopping" process for consumer complaints, will be implemented in an effective manner.

1. **Restore the Ability of the States to Protect Consumers in the Credit Arena.** As it stands now, OCC rules prevent enforcement of many state consumer protections against national banks and their subsidiaries. Banks even maintain that these stronger state laws are preempted when they are based on Congressional statutes that specifically permit states to provide protections beyond those in the federal law. The OCC rules also preempt the performance of essential functions of state officials to protect state citizens and defy over a century of jurisprudence holding that state officers can enforce a broad set of laws against national banks. Historically, these protective actions have covered both the individual bad acts of national banks, as well as bank policies that are deemed to be unfair or deceptive to consumers.

   This is why national consumer organizations favor the approach taken by "The Preservation of Federalism in Banking Act" (H.R. 1996) introduced earlier this year by Representative Luis Gutierrez. We have previously supported legislation along these lines offered by the by the Chairman and Mr. Gutierrez in the last Congress and believe that this bill is particularly necessary and relevant in light of the Watters decision.

   H.R. 1996 establishes much needed standards governing the relationship between state consumer authority and the operation of national banks and their subsidiaries. The bill also covers federal thrifts, as the Office of Thrift Supervision has from time-to-time sought to broaden the scope of federal preemption to new entities, such as independent third party agents of thrifts.

   H.R. 1996 directs federal regulators to distinguish between preempted state laws affecting the business of banking and the powers of national banks and thrifts, as well as permissible state laws of general applicability protecting consumers. The bill also prevents federal preemption from diminishing the ability of states to protect their consumers from fraudulent, deceptive and predatory banking practices. Frequently, no corresponding federal protections exist when the OCC preempts state laws, and thus consumers are deprived of protections currently available to them. Other key provisions in the bill would clarify the visitorial rights of state officials seeking to enforce applicable federal or state laws and reinstate state authority over non-bank operating subsidiaries.

Finally, the bill makes clear that the National Bank Act is not intended to bar a state's ability to enact stronger laws regulating national banks when those laws are based on clear Congressional intent of other federal laws to serve as a floor and not a ceiling for consumer protections.

We urge the committee to hold hearings on this legislation.

2. **Enact legislation to establish high consumer protection standards for credit card, bank overdraft and mortgage loans.** Take legislative action to protect consumers where bank regulators have failed to do so, such as the FRB's unwillingness to apply TILA protections to overdraft loans. We urge Congress to adopt legislation introduced by Representative Maloney (H.R. 946) that would require that consumers who receive overdraft loans benefit from the same protections under TILA as they would for other loans. (See also the attached credit card reform platform in Appendix A and the principles for enacting mortgage lending reforms in Appendix B.)

3. **Authorize the Federal Trade Commission to bring enforcement actions against national banks and thrifts for unfair and deceptive practices. Give the FTC concurrent and independent rulemaking authority over national banks and thrifts for all matters covered by the FTC Act.** Unlike the banking agencies, the FTC has no responsibility to protect the profitability of financial institutions. Its sole job is, or should be, to protect consumers from the unlawful and deceptive practices prohibited by the FTC Act. And yet, the FTC Act deprives the FTC of the essential authority over regulated institutions. The FTC has extensive experience dealing with unfair and deceptive practices by non-bank entities. In light of the failure of the FRB to use its authority under the FTC Act, the FTC should be given concurrent authority both to bring enforcement actions and to engage in rulemaking. This authority would be consistent with the independent authority that state attorneys general have regarding state chartered banks in some states. This is not to say that giving authority to the FTC will be a perfect solution. The FTC's record in recent years with respect to non-bank entities is less than perfect, and Congress may need to make clear to the FTC that it will gain this authority only if it commits to using it in an appropriate fashion. However, the FTC lacks the inherent conflict of interest that paralyzes some of the banking agencies, and it is appropriate for the agency to have full authority under the FTC Act over all entities that engage in unfair and deceptive practices.

4. **Grant states concurrent enforcement authority against national banks and thrifts under federal lending laws and for unfair and deceptive practices under the FTC Act.** This approach will help put state enforcement officials, including banking regulators, back "on the beat." The model for this approach would be the concurrent enforcement authority granted to states under such federal laws as the Telemarketing Sales Act[38] and the Credit Repair Organizations Act.[39] This approach would lead to more vigorous enforcement, and in particular would foster attention to emerging problems that

[38] 15 U.S.C. § 6103 (giving state Attorneys General concurrent authority with FTC to enforce Telemarketing Sales Rule, 12 C.F.R. § 310).
[39] 15 U.S.C. § 1679h (giving state Attorneys General and FTC concurrent enforcement authority).

have not yet become national in scope.

5. **Provide consumers with a private right-of-action under the FTC Act.** At present, the essential protection in the FTC Act against unfair and deceptive practices is not privately enforceable. Yet, individuals are obviously in the best position to invoke the Act in response to individual violations. Even strong federal agency enforcement against widespread abuses would not help consumers who confront individual abuses. Although most states have parallel protections, in many states consumers cannot bring claims under the state deceptive practices statute against banks or other financial institutions. In some states, the deceptive practices statute explicitly excludes these entities. In other states, courts have interpreted the statute to exclude them (often construing an exemption for "regulated practices" to exclude any activity by a regulated financial institution, not just specific practices authorized by banking regulations). Another weakness of state deceptive practices laws is that many prohibit only deceptive practices, not unfair practices, or define the prohibited practices very narrowly.[40] As a result, in many states consumers have very limited remedies for unfair or deceptive practices by financial institutions. Public enforcement does not fill this gap. Even if state Attorneys General and the FTC were granted enforcement authority, their resources are limited and they have to concentrate on cases with broad impact, rather than on obtaining justice for individual consumers.

6. **Reduce conflicts-of-interest between regulators and regulated institutions. Consider requiring federal banking agencies to pool funds collected for supervision, examination and consumer protection.** We would urge the Committee to consider establishing an independent, inter-agency process that receives input from consumer representatives, to distribute the funds to banking agencies based on need.

7. **Require agencies to conduct periodic reviews of the effectiveness of consumer protection rules and enforcement efforts.** Federal agencies must meet statutory requirements regarding the reduction of regulatory burdens and "paperwork" on regulated industries, but no such requirement exists for consumer protection. We urge the Committee to enact legislation that would require banking regulators to regularly investigate key emerging consumer issues and concerns and to make recommendations to Congress regarding changes in supervision, regulation and law that should be made. The agencies should be required to consult consumer representatives, state regulators, Attorneys General as part of this review.

8. **Evaluate industry proposals for "principles-based" regulation with great Skepticism.** All regulations should be founded on strong underlying principles, but we urge you to skeptically view calls by representatives of the financial services industry for principles-based regulation. There is overwhelming evidence that many consumers have been harmed by unfair and deceptive practices in a number of credit markets. As stated above, the OCC and FRB appear to have taken what is essentially a "principles based"

[40] In addition, federally-regulated financial institutions are increasingly claiming that state deceptive practices statutes are preempted by federal law (although many courts have rejected this argument).

approach in protecting consumers for a number of years. It stretches the bounds of credulity to claim this approach has been effective for financial services consumers.

APPENDIX A

ACORN * Center for Consumer Finances * Consumer Action * Consumers Union
Consumer Federation of America * Demos * National Association of Consumer Advocates * National Consumer Law Center • U.S. PIRG

Joint Recommendations of Consumer Groups on the Eve of the Jan. 25, 2007 U.S. Senate Banking Committee Oversight Hearing on Unfair Credit Card Practices

Eliminate reckless and abusive lending by credit card companies

No unsound loans. Make issuers offer credit the old fashioned way, using sound underwriting principles based on the ability of consumers to pay and that ensure the cardholder is not overextending financially by taking on more debt.

Restrict lending to youth without conditions. Young people deserve credit, but only if they qualify. Yet right now, young people are the only group that can obtain a credit card without either a positive credit report, a job, or other evidence of ability to pay, or, barring any of these, a co-signer. No other adult can get a credit card without meeting at least one of these conditions. Young people should have the same safeguards.

No abuse of consumers in bankruptcy. Credit card issuers drive consumers into bankruptcy with abusive terms and collection practices. Stop issuers from collecting on these abusive loans in bankruptcy.

End deceptive and unjust terms, interest rates and fees

Ban retroactive rate increases. Stop issuers from changing the rules in the middle of the game by raising interest rates on past purchases.

No unilateral adverse changes in terms for no reason. Credit card company contracts currently claim the right to change terms for any reason, including no reason. Any change in terms during the course of the contract should require knowing affirmative consumer consent and reasonable notice.

Ban universal default in all its forms. Prohibit punitive "universal default" interest rates based on alleged missteps with another issuer but involving no missed payments to the credit card company itself. It is unfair to impose a penalty rate on a consumer who has not made a late payment to that creditor. Stop card companies from using a change in terms clause to impose penalty rates.

Stop late fees for payments mailed on time. Require credit card companies to follow the Internal Revenue Service (IRS) and accept the postmarked date as proof of on-time payments. This will also eliminate the tawdry practice of assessing late payment fees when payment is received on the due date, because it did not arrive by a specific time (such as 11 a.m.).

Relate fees to cost. Ensure that all fees and other charges closely match the true cost borne by the card issuer.

End roll-over or repeat late and over-limit fees. Ban fees that are charged in consecutive months based on a previous late or over the limit transaction, not on a new or additional transaction offense, even if the consumer remains over the previous limit.

No fees for creditor-approved transactions. Don't let the credit card company charge a fee for a transaction it has approved. Ban over-limit fees when the issuer approves the over-limit transaction.

Empower consumers with more detailed information.

Ban deceptive credit card offers. Solicitations and "invitation to apply" solicitations that do not make a truly firm offer of credit are deceptive because they lead consumers to believe that they are pre-approved for or have a good chance of getting certain interest rates. Most consumers instead receive cards at much less favorable interest rates and terms.

Simplify pricing. Reduce the number and types of fees so consumers can compare cards and understand the real cost of using the card.

Real minimum payment warning. Give each consumer a personalized warning on his or her monthly statement calculating the length of time—in months and years—and the total interest costs that will accrue, if the consumer makes only the requested minimum payment.

Ban unfair teasers. Stop issuers from downplaying permanent interest rates in advertisements and solicitations and from trumpeting temporary rates as "fixed rates."

Enhance 'Schumer Box' disclosures. Include a "Schumer box" disclosure table in all cardholder agreements containing personalized information about the terms of the card granted. The box should include the APR, the credit limit, and the amount of all fees, such as late charges, cash advance fees, over limit fees and any other applicable miscellaneous fees.

Give consumers strong protections to deter illegal acts

Ban pre-dispute binding mandatory arbitration. No consumer should be forced to waive his or her right to a court trial as a condition of using a credit card. Prohibit binding mandatory arbitration for consumers' claims *and* for collection actions against consumers.

Toughen Truth In Lending Act (TILA) penalties. TILA penalties have stagnated since 1968.

Give aggrieved consumers a private right of action to enforce the Federal Trade Commission Act to challenge unfair or deceptive practices by businesses, including banks.

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February 6, 2007

APPENDIX B

The Honorable Barney Frank
Chairman
House Financial Services Committee

The Honorable Spencer Bachus
Ranking Member
House Financial Services Committee

The Honorable Chris Dodd
Chairman
Senate Banking Committee

The Honorable Richard Shelby
Ranking Member
Senate Banking Committee

Dear Chairman Dodd, Chairman Frank, Ranking Member Shelby, and Ranking Member Bachus:

Homeownership is the most accessible tool available to help families achieve a secure economic future, but today market failures and abusive lending practices are stripping the benefits of homeownership from millions of families **throughout the mortgage market.** The epidemic of home losses on subprime mortgages—as many as one in five— is a wake-up call, providing strong evidence that the current system of mortgage regulation is seriously flawed. To preserve homeownership for American families, we need real, systemic change embodied in policies that protect the **sustainability of homeownership**. Below, we outline a policy framework that would drive effective solutions to preserve the traditional benefits of owning a home. Our views represent those of many consumer, civil rights, and community groups, as well as a number of responsible mortgage lenders.

As Congress begins a new session, we respectfully ask that any new anti-predatory lending legislation be based on the following principles:

- **Restore sensible underwriting and eliminate unsustainable loans;**
- **Eliminate incentives for lenders to steer borrowers to abusive loans;**
- **Require accurate and accountable loan servicing;**
- **Ensure effective rights and remedies for families caught in predatory loans;**
- **Preserve essential federal and state consumer safeguards; and**
- **Reduce foreclosures through assistance to distressed borrowers.**

Sustainable loans. Many lenders have abandoned careful lending standards to make loans that borrowers cannot repay without refinancing or selling their home. As a result of this weak underwriting, an increasing number of homeowners are unable to keep up with their mortgage payments. High-risk adjustable rate mortgages (ARMs), which are underwritten to a low teaser payment instead of to the fully indexed rate, are an example of this problem. Studies show that today's subprime mortgages typically include features that increase the chance of foreclosure

regardless of the borrower's credit. This has caused many families to default on unnecessarily risky loans and lose their homes. Other families are forced to refinance and pay associated fees or sell their home. *Responsible lending demands a realistic analysis of the borrower's ability to repay the loan based on all its terms.*

Incentives for fair loans. The subprime market now rewards lenders and brokers who charge borrowers excessive points and fees or channel them toward riskier loan products. Unknown to most borrowers, brokers receive payments known as "yield spread premiums" for selling loans at a higher interest rate than the lender requires. Most subprime mortgages also include prepayment penalties, which can cost families thousands of dollars when they refinance or pay off their loans early. Too often the borrower does not receive a lower interest rate in exchange for the prepayment penalty. In the inefficient subprime market, prepayment penalties are simply another method of stripping home equity or trapping borrowers in costly loans. These fees are only appropriate when they are in exchange for a real benefit to the borrower. A law to sustain homeownership must prohibit brokers and lenders from steering borrowers into mortgages with excessive costs.

Accountable loan servicing. Companies that collect payments on mortgages—loan servicers—have tremendous influence on the success of the loan. Servicer errors and unfair practices in recent years have contributed to the recent surge in foreclosures. Problems typically arise when loan servicers impose costly and unnecessary hazard insurance or delay crediting mortgage payments so that they can charge costly late fees to the homeowner. As it stands now, mortgage servicers have incentives to profit from loan defaults. In a healthy and truly competitive market, loan servicers would charge reasonable fees and support homeowners' efforts to avoid foreclosure.

Basic rights and remedies. Victims of abusive lending practices have very little recourse because industry often uses its market power to limit homeowners' access to justice. To be effective, consumer protection laws must: (1) give families a private right of action, the right to pursue class actions, and defenses against collection and foreclosure, which are often the only effective way to deter bad actors; (2) contain strong remedies and penalties for abusive acts; (3) provide effective assignee liability so that borrowers can pursue legitimate claims even when the originator has sold their loan; and (4) prohibit mandatory arbitration clauses that weaken victims' legal rights and deny them access to seeking justice in a court of law. Without these fundamental procedural protections, other consumer protection rules are unenforceable.

Preserve and advance existing protections. Current laws contain certain essential consumer protections designed to address some of the egregious practices in the mortgage industry, and these protections must be preserved. In particular, the majority of states have passed laws that have been highly effective in curbing abusive lending practices without hampering borrowers' access to credit. Any new law must build on these protections, bearing in mind that real estate markets vary significantly in different locations, and that states are in the strongest position to address new lending abuses that evolve over time. Legislative solutions must also preserve protections for families outside the mainstream real estate market—for example, those who use alternative ownership options such as mobile and manufactured housing and seller-driven

financing; are credit impaired; have limited or no credit histories; have limited English skills; or are located in high-poverty areas.

Reduce skyrocketing foreclosures. Any new law should preserve the benefits of homeownership by assisting homeowners already in distress. Recent research shows that as many as one out of five subprime mortgages made in recent years will end in foreclosure. In addition to strengthening the market to benefit future borrowers, legislation should address the increasing numbers of existing homeowners who risk losing their home. Federal legislation could build on successful state models to provide affordable homeownership preservation loans to borrowers who are in default due to circumstances beyond their control.

* * * * *

We welcome legislation that, based on the principles outlined above, contains effective solutions to current problems and allows rapid responses to emerging abuses. We look forward to working with you on the critical issue of preserving the benefits of homeownership, and we thank you for your time and consideration.

Sincerely,

AARP
AFL-CIO
American Council on Consumer Awareness
Association of Community Organizations for Reform Now (ACORN)
Center For Responsible Lending
Coalition of Community Development Financial Institutions
Consumer Action
Consumer Federation of America
Consumer Union
International Union, United Auto Workers
Leadership Conference on Civil Rights
NAACP (National Association For The Advancement of Colored People)
NAACP Legal Defense & Educational Fund, Inc.
National Association of Consumer Advocates
National Consumer Law Center (on behalf of its low-income clients)
National Council of La Raza
National Fair Housing Alliance
National Lawyers' Committee for Civil Rights Under Law
National People's Action
National Training and Information Center
Rainbow/ PUSH
U.S. Public Interest Research Group
Affordable Housing Education and Development, Inc. (NH)
Alaska Public Interest Research Group
Alexandria Affordable Housing Corporation (LA)

Allen Neighborhood Center (MI)
American Community Partnerships (DC)
American Friends Service Committee NH Program (NH)
Arizona Consumers Council
Arizona PIRG
Birmingham Business Resource Center (AL)
Border Fair Housing & Economic Justice Center (TX)
Cabrillo Economic Development Corp. (CA)
California Reinvestment Coalition
Cambridge Consumers' Council
CATCH Neighborhood Housing (NH)
Ceiba Housing and Economic Development Corp. (Puerto Rico)
Center for Consumer Affairs (WI)
Center for Social Concerns, University of Notre Dame
Champaign County Health Care Consumers (IL)
Cherokee Nation (OK)
Chicago Consumer Coalition
Cincinnati Change (OH)
Civil Justice, Inc
Coastal Enterprises, Inc. (ME)
Codman Square Neighborhood Development Corp. (MA)
Colorado Rural Housing Development Corporation (CA)
Columbia Consumer Education Council (SC)
Community Development Corporation of Long Island, Inc. (NY)
Community Enterprise Investments, Inc. (FL)
Community Frameworks (WA)
Community Housing Development Corporation of North Richmond
Community Housing Partners Corporation (VA)
Community Law Center
Community Law Center, Inc. (MD)
Community Neighborhood Housing Services, Inc. (MN)
Community Reinvestment Association of North Carolina (NC)
Consumer Federation of California
Consumer Federation of Southeast
Corporation for Enterprise Development (DC)
Cuyahoga County Foreclosure Prevention Program
Dayton Community Reinvestment Coalition (OH)
Delaware Community Reinvestment Action Council, Inc. (DE)
Department of Sociology and Anthropology, IU South Bend
Detroit Alliance for Fair Banking (MI)
Durham Community Land Trustees (NC)
East Akron Neighborhood Development Corporation Inc. (OH)
East Side Organizing Project - Cleveland, OH
Empire Justice Center
Enterprise Corporation of the Delta/HOPE (MS)
Ethical Lending Foundation

Fair Housing Council of the San Fernando Valley Housing Research & Advocacy Center (Cleveland)
Fort Berthold Housing Authority (ND)
Foundation Communities (TX)
Frontier Housing, Inc. (KY)
Greater Rochester Community Reinvestment Coalition (NY)
Hamilton County Community Reinvestment Group (OH)
Hawaiian Community Assets (HI)
HEED (MS)
Hipanic Leadership Coalition of St. Joseph County
Home Management Resources
Homeward, Inc. (IA)
Housing Action Illinois
Housing and Credit Counseling, Inc(KS)
Housing Assistance Program of Essex County, Inc. (NY)
Housing Education Program (CA)
Housing Opportunities Made Equal of Virginia, Inc.
Housing Partnership of Northeast Florida, Inc. (FL)
Indiana Association for Community Economic Development (IN)
Inglewood Neighborhood Housing Services, Inc. (CA)
Interfaith Housing Center of the Northern Suburbs - Chicago, IL
Iowa Citizens for Community Improvement
Jacksonville Area Legal Aid, Inc.
Jewish Community Action (MN)
Joseph Corporation of Illinois, Inc. (IL)
Justine Petersen Housing & Reinvestment Corporation (MO)
Kensington-Bailey Neighborhood Housing Services, Inc. (NY)
Knox Housing Partnership, Inc. (TN)
LaCasa of Goshen, Inc. (IN)
Latino Leadership, Inc. (FL)
Lawyers' Committee For Civil Rights Under Law of the Boston Bar Association (MA)
Lighthouse Community Development - Pontiac, MI
Long Island Housing Services, Inc. (NY)
Louisiana CRA Coalition (LA)
Madison Park Development Corporation (MA)
Manna, Inc. (DC)
Mass Consumers' Coalition
MassPIRG
Metropolitan Housing Coalition (KY)
Metropolitan Milwaukee Fair Housing Council (WI)
Metropolitan St. Louis Equal Housing Opportunity Council (MO)
Miami-Dade Neighborhood Housing Services, Inc. (FL)
Michigan Community Reinvestment Coalition (MI)
Micronesia Self-Help Housing Corporation
Mission Economic Development Agency (MEDA)
Monmouth County Fair Housing Board (NJ)

Montgomery Housing Partnership (MD)
Mountain State Justice, Charleston, WV
National Association of Community Economic Development Associations (MD)
National Community Reinvestment Coalition
National NeighborWorks Association (DC)
Native American Health Coalition (TX)
Navajo Housing Authority (AZ)
Nehemiah Community Reinvestment Fund, Inc. (CA)
Neighborhood Housing Partnership of Greater Springfield, Inc. (OH)
Neighborhood Housing Services of Baltimore, Inc. (MD)
Neighborhood Housing Services of Greater Cleveland, Inc. (OH)
Neighborhood Housing Services of Kansas City, Inc. (MO)
Neighborhood Housing Services of New Haven, Inc. (CT)
Neighborhood Housing Services of Oklahoma City, Inc. (OK)
Neighborhood Housing Services of the Black Hills, Inc. (SD)
Neighborhood Housing Services of the Lehigh Valley, Inc. (PA)
Neighborhood Housing Services, Inc. (PA)
Neighborhood Nonprofit Housing Corporation
Neighborhood Renewal Services of Saginaw, Inc. (MI)
NeighborWorks Columbus (GA)
NeighborWorks Rochester (NY)
New Directions Housing Corporation (KY)
New Jersey Citizen Action (NJ)
NHS of Chicago (IL)
Northeast South Dakota Community Action Program
Northeast South Dakota Economic Corporation
Northwest Indiana Community Reinvestment Alliance (IN)
North West Side Housing Center - Chicago, IL
Norwalk (Connecticut) Fair Housing (CT)
Notre Dame Legal Aid
Nuestra Comunidad Development Corp. (MA)
Opportunity Finance Network
Oregon Consumer League
Piedmont Housing Alliance
Pittsburgh Community Reinvestment Group (PA)
PPEP MicroBusiness and Housing Development Corporation
PPEP Microbusiness and Housing Development Corporation, Inc. (AZ)
Project Change Fair Lending Center (NM)
Reservoir Hill Improvement Council
Resurrection Project - Chicago, IL
Rural Opportunities, Inc. (NY)
Salisbury Neighborhood Housing Services, Inc. (MD)
Sargent Shriver National Center on Poverty Law (IL)
Scott County Housing Council (IA)
Scranton Neighborhood Housing Services, Inc. (PA)
Seedco

Self-Help Enterprises (CA)
Shorebank
Shorebank Enterprise Pacific
Siouxland Economic Development Cooperation
SJF Ventures
South Austin Coalition Community Council - Chicago, IL
South Bend Center for the Homeless
Southeast Community Development Corporation
Southern Good Faith Fund (AR)
Southwest Fair Housing Council (AZ)
St. Joseph Valley Project
St. Lawrence County Housing Council, Inc.
Tlingit-Haida Regional Housing Authority (AK)
Tri-County Housing & Community Development Corporation (CO)
Unidos Para La Gente (TX)
United Keetoowah Band of Cherokee Indians (OK)
United Neighborhood Centers of Northeastern Pennsylvania (PA)
United South Broadway Corporation (NM)
Utica Neighborhood Housing Services, Inc. (NY)
Village Capital Corporation
Virginia Citizens Consumer Council
Virginia Poverty Law Center
West Elmwood Housing Development Corp. (RI)
Westchester Residential Opportunities, Inc. (NY)
Western Massachusetts Enterprise Fund
Wisconsin Consumers League
Working Together for Jobs (NJ)

APPENDIX C

THE OCC'S UNAUTHORIZED PREEMPTION THREATENS CONSUMERS AND FEDERALISM

Issue: For approximately a decade, the Office of the Comptroller of the Currency, a division of the Department of the Treasury, has systematically worked to undermine states' efforts to protect their consumers through measures such as state anti-predatory lending laws. This effort culminated in a cluster of rules issued in 2004 that, in effect, allow the OCC to determine what state law applies to national banks and prohibit state attorneys general or state financial regulators from enforcing any remaining applicable state law.[41] The practical effect of these OCC actions has been to deprive banking customers of basic marketplace protections provided by state law and enforcement actions by state agencies.

The OCC states that its purpose in charting this radical new course is uniformity. In the area of consumer protection, however, Congress has consistently stressed the rights of states to enact greater protections for their citizens. A decision to abolish state consumer protections in the name of banking uniformity should not be made by agency mandate. This is particularly true in the OCC's case because of the inherent conflict between its promotion of federal bank charters (and thus increased OCC funding) and the needs of its banking customers.

A challenge to a 2001 OCC rule that permits operating subsidiaries of national banks to "piggy-back" on the preemption rights of their parents is pending before the Supreme Court in *Watters v. Wachovia Bank, N.A.*, No. 05-1342. While the case may provide judicial guidance on the question of whether the OCC has overreached as to this rule, the remaining rules that preempt state law and states' enforcement rights over national banks are also serious threats to federalism and consumer rights.

Scope of Impact: The OCC supervised banks holding 67% of total assets of all U.S. commercial banks in 2005. These banks have approximately 500 operating subsidiaries that deal directly with consumers and that can claim their parents' preemption under the OCC's rules. Further, the scope of the agency's preemption affects far more than just national banks and their operating subsidiaries, because federal law, and some state laws, gives non-national banks "parity" rights with national banks. These result in a considerable spill-over preemption to other entities not regulated by the OCC.

Concerns:

1) **Charter competition:** Depository institutions get to choose the type of charter under which they operate, and thus get to choose their regulator. They may chose between state and federal charters, and among federal charters. This has led to "charter competition." The

[41] This displacement of state enforcement authority is contained in the OCC's claim of broad exclusive "visitorial powers," in 12 C.F.R. 7.4000. The validity of that rule is pending in the Second Circuit. *See OCC v. Spitzer*, 396 F. Supp. 2d 383 (S.D.N.Y. 2005), *appeal docketed*, No. 05-5996cv (2d Cir. 2005).

OCC has marketed its broad preemption of state consumer protections to attract depositories to its charter.

2) **Funding:** The OCC is not funded by Congressional appropriations, but by asset-based assessments on its regulated entities. In 2005, 97% of its operations were funded by revenue from assessments. The agency uses a size-based assessment scale, which makes it especially dependent on a few large banks. In one recent year, for instance, the equivalent of 10% of the OCC's budget ($40M) came from one bank alone.

3) **Imbalance of customer and regulated entity interests:**

- Rule-making and interpretation: The agency's interpretations have been consistently result-oriented to allow banks maximum relief from existing law. For example, "interest" is broadly defined to include many fees for purposes of exporting the laws of business-friendly states and ignoring the laws of the customers' states, 12 C.F.R. § 7.4001(a), but narrowly defined if a broad definition would hurt a bank in its home state, 12 C.F.R. § 7.4001(c).

- Interfering with litigation between banks and their customers or state enforcers: The OCC has expended considerable resources over the last decade filing amicus briefs in litigation on the side of banks against their customers and state enforcement agencies. The amicus activity by the OCC has been substantially higher than other federal financial regulators. In one case, the OCC attempted to stop a state attorney general from pursuing claims of telemarketing fraud by a bank mortgage subsidiary.[42] The company's own employees had described the challenged practice as "unethical," a "fraud," and a "scam."

- Inadequate enforcement to replace the displaced state enforcement: In its recent efforts to displace state enforcement authority even as to non-preempted state law, the agency realized it "could not replace something with nothing."[43] The OCC therefore found authority that it had never used for 25 years to enforce the FTC's unfair and deceptive practices law. However, the OCC has used this authority very sparingly, and, in some instances, only after state law enforcement action has begun.

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[42] *Minnesota ex rel. Hatch v. Fleet Mortgage Corp.*, 158 F. Supp. 2d 962 & 181 F. Supp. 2d 995 (D. Minn. 2001).
[43] A former Treasury official gave that explanation for the OCC's first use of the FTC UDAP authority at a legal conference in San Francisco in May, 2002. (Practising Law Institute, *Consumer Financial Services Litigation)*

NCLR
NATIONAL COUNCIL OF LA RAZA

Latino Credit Card Use: Overcoming Disparities, Structural Challenges, and Harmful Industry Practices

Submitted to:
U.S. House Financial Services Committee
The Honorable Barney Frank, Chairman

Submitted by:
Raul Gonzalez, Legislative Director
National Council of La Raza

National Council of La Raza
Raul Yzaguirre Building
1126 16th Street, NW
Washington, DC 20036

July 25, 2007

INTRODUCTION

The National Council of La Raza (NCLR) – the largest national Hispanic* civil rights and advocacy organization in the United States – works to improve opportunities for Hispanic Americans. Part of this mission includes conducting research, policy analysis, and advocacy on a variety of financial services issues that impact the ability of Latinos to build and maintain assets and wealth. The most recent household wealth survey revealed that the median net worth or wealth of Hispanic households is $7,932, compared to $88,651 for White non-Hispanic households.[1]

All Americans rely on financial products to help them buy homes and otherwise build wealth and financial security. Credit cards are one important way for Americans to gain experience in financial markets or personal finance and build a credit history. Access to safe and affordable credit has become increasingly critical for Latinos – the fastest-growing and largest minority group in the country – as they more fully integrate into the mainstream financial system and work to gain access to the American middle class. Yet, clear disparities in credit card use and in the application of fees exist between racial groups, which only perpetuate the wealth gap. Currently, household debt is on the rise. Many consumers report that they are "maxed out," and low-income families often rely on credit cards as a safety net to make up for limited income. This is a critically important time for Congress to shed light on the credit card industry.

As experts and policy-makers deliberate on how to regulate the credit card market, developing a deeper understanding of the experience of low-income Latino and immigrants with credit cards can help to shape policies that positively impact all consumers. This statement will briefly outline recent data on Latino credit card use, structural barriers in credit markets, and harmful credit card industry policies and practices, and will provide recommendations to improve access to affordable credit and shift the balance of power back into the hands of consumers.

LATINO CREDIT CARD USE

The increase in credit card use among low-income households has been significant, in large part due to heavy marketing by the industry to these consumers.[2] However, while the vast majority of American households use credit cards, a large share of Latino consumers do not. Data from the 2004 Survey of Consumer Finances show that 80% of surveyed respondents said that they use credit cards, compared to only 56% of Hispanic households.[3] Still, more Latinos are using credit cards today than ever before. Between 1992 and 2001, the share of Hispanic families who held credit cards grew from 43% to 53%.[4] Increased credit card use among Latinos is a sign that they are becoming more integrated into the financial fabric of the country. An increase in credit card use, however, has also led to an increase in debt. The average credit card debt among Hispanics increased by nearly 20% between 1992 and 2001, from $3,082 to $3,691.[5]

Although wise credit card use is a good method for building a credit history, an increased reliance on credit cards hampers a family's ability to save for big-ticket items, such as a reliable vehicle, a home, or an education. Recent data show that Latinos are having difficulty managing their credit card debt. Approximately 19.3% of Hispanics in one survey described their situation

* The terms "Hispanic" and "Latino" are used interchangeably by the U.S. Census Bureau and throughout this document to identify persons of Mexican, Puerto Rican, Cuban, Central and South American, Dominican, and Spanish descent; they may be of any race.

as "burdensome and not enough money to pay down [the balance]," and 11.4% of Hispanics reported they were "maxed out and can't use [their cards]." However, 12.7% of all respondents in the same survey characterized their debt situation as "burdensome and not enough money to pay down [the balance], while 7.3% were "maxed out and can't use [their cards]."

STRUCTURAL BARRIERS TO ACCESSING GOOD CREDIT

NCLR recently released a report entitled, *Latino Credit Card Use: Debt Trap or Ticket to Prosperity?*[6] In this report, we found that many structural factors and barriers hamper Latino access to mainstream credit cards with the most desirable contract terms. A forthcoming study by Demos will show that Latino and African American consumers are more likely than White consumers to pay interest rates higher than 20%. More specifically, 13% of Latino, 15% of African American, and 7% of White cardholders pay interest rates greater than 20%.[7] The following factors may explain why such barriers exist:

- **Creditworthiness.** Credit card issuers rely on several factors to determine whether or not to extend credit to consumers, including credit score, the number of credit cards they currently hold, their combined credit card balances and credit limits on their cards, and any record of past delinquencies. Approximately 22% of Hispanic borrowers have no credit score, compared to 4% of Whites and 3% of African Americans.[8] Individuals who lack a repayment history or other observable characteristics will either not be approved for a credit card or receive a card with undesirable terms.

- **Search Costs.** Roughly 5.2 billion credit card solicitations were sent to U.S. households in 2004.[9] Through the collection of consumer financial information, issuers essentially prescreen and select their customers. Individuals with robust credit histories will receive multiple offers from which to choose. Subprime and low-income borrowers who are not operating in the mainstream financial system are less likely to receive multiple offers. These borrowers will have to spend a significant amount of time and resources searching for a credit card that meets their needs.

- **Shopping.** Latino consumers are less likely to shop for a credit card. According to one survey, only 7% of Hispanic consumers who carry a balance report "substantial" shopping for credit, compared to 12% for similar White consumers.[10] Research also shows that Latinos are not shopping and applying for credit cards for fear of rejection. Approximately 25% of Hispanic consumers who use credit cards and were denied a loan did not reapply for fear of rejection.[11]

- **Switch Costs.** For many consumers, relief from a credit card with a high interest rate comes from switching or transferring their balance to a credit card with a lower interest rate. Transferring balances from one card to another is not an option for consumers who carry high interest rates and who are often rejected for credit. Approximately 34% of Hispanic households who carry a balance reported being rejected for a loan, and 23% cited "credit" as a reason for the rejection."[12] These consumers are essentially held captive by their issuer.

CHALLENGES IN POLICY AND PRACTICE

Consumers who use credit cards can be placed into three general categories: 1) consumers who use their card but pay the balance in full each month; 2) consumers who sometimes carry a balance; and 3) consumers who usually or always carry a balance. Consumers in the third category are struggling to make ends meet and using their credit card as a safety net. Consequently, these consumers are also more likely to make a late payment and trigger harmful industry policies and practices that lead to penalty interest rates that exceed 30% and a laundry list of fees. A recent survey showed that borrowers who pay late are more likely to be low income, single, or non-White.[13]

Given the issues listed above, the following industry policies and practices provide notable challenges for Latino consumers:

- **Universal default.** Universal default enables an issuer to increase a consumer's interest rate based on the consumer's credit behavior with *other* creditors. Depending on the credit card issuer, the penalty interest rate that is applied could exceed 30%, even if the consumer has never missed a payment.

- **Change-in-terms provisions.** Change-in-terms provisions enable a credit card issuer to change the terms of a consumer's credit card agreement at any time and for any reason as long as they provide written notice to the consumer 15 days before the change. While recent attention by Congress on credit cards has led one major issuer to cease the application of these provisions, a recent credit card survey revealed that half of the top 20 banks still apply these policies.[14]

- **Double-billing on purchases made outside the U.S.** Firms that process credit card transactions, such as Visa and MasterCard, traditionally charge 1-2% of the cost of *each* purchase made abroad for converting currency, often called the foreign conversion fee. In addition to this fee, however, many credit card issuing banks charge an additional fee for these purchases, even though there is no additional cost to the bank. A recent credit card survey showed that 26 out of 45 issuers charge a foreign conversion fee, in addition to the fee charged by the transaction processing firms, with a total average fee of 3% for *each* transaction. This constitutes double-billing and particularly impacts immigrants who frequently return to their home country.

- **Deceptive monthly minimum balance requirements.** Some consumers are unaware of the consequences of paying only the monthly minimum payment requirement while, for others, the minimum is all they can afford. Consumers who pay only the minimum will ultimately pay more in interest and extend the time that they will be subject to fees.

- **Inflation and application of fees.** Today credit cards come with a laundry list of fees that issuers charge to consumers, such as the annual fee, late payment fee, over-the-credit-limit fee, credit limit increase fee, foreign conversion fee, expedited payment fee, and the replacement card fee, just to name a few. The cost of fees has dramatically

increased over the past ten years, even though the cost to banks to purchase funds has not. A typical late fee in 1980 ranged from $5 to $10, compared to $33 today.

- **Credit card-related scams.** Research conducted by the Federal Trade Commission (FTC) shows that 14.3% of Hispanics are victims of fraud, compared to 6.4% of non-Hispanic Whites.[15] One type of scam is the existence and distribution of affinity and fake credit cards.[16] Affinity credit card scams involve individuals who sell credit cards to Hispanic consumers, claiming that they are custom-tailored to meet their needs. Similar to fake credit card scams, these affinity credit cards are worthless and cannot be used to purchase goods or services.

- **Obscure consumer complaint system.** Currently, the burden is on the consumer to determine which federal agency regulates their credit card issuer and determine how to file a credit card-related complaint. It is highly unlikely that consumers are familiar with the role and responsibilities of the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, or the Office of Thrift Supervision, all of which regulate credit card-issuing banks. The Customer Assistance Group (CAG) of the OCC was created to receive, track, and resolve consumer complaints against national banks. However, CAG's consumer complaint hotline does not appear on credit card statements, and the agency has done little to reach out to Hispanic consumers who have a tendency not to file complaints.

- **Ineffective financial education structure.** A variety of financial education programs has been created to increase financial literacy in the Hispanic community. These programs include workbooks, DVDs, Internet seminars, and brochures. Although financial education is important for raising awareness among consumers, many financial education materials contain generic information or are not custom-tailored to address the unique credit needs of Latinos. Additionally, distribution of materials has been limited, and consumers may have already fallen into debt trouble before gaining access to these resources.

RECOMMENDATIONS

- **Ban universal default and change-in-terms policies.** Policy-makers should enact the "Universal Default Prohibition Act of 2007" (H.R. 2146), which prohibits issuers from increasing interest rates on a consumer's credit card for failing to make payments to another creditor. Additionally, issuers should be prohibited from changing the terms of a consumer's credit card agreement. These policies are fundamentally unfair.

- **Inflation and application of fees.** Policy-makers should require that credit card fees relate back to the cost incurred by the issuer. In regard to the foreign conversion fee, consumers should not be double-billed for purchases made abroad. To this end, banks should cease applying an additional conversion fee to transactions made abroad. Additionally, regulators should require credit card issuers to highlight the foreign conversion fee in non-English-language credit card offers.

- **Enact a mandatory, individualized minimum payment warning.** Policy-makers should enact the "Credit Card Repayment Act of 2007" (H.R. 1510), which requires conspicuous, front-page disclosure of the outstanding balance, a minimum payment warning, and the amount of time that it would take consumers to pay off their balance if they pay only the minimum.

- **Stop credit card-related scams.** Federal agencies, credit card issuers, and local consumer protection agencies should partner with community-based organizations (CBOs) to raise awareness of credit card-related scams that strip wealth from the Latino community. CBOs serve as the "eyes and ears" of the Latino community and understand its needs.

- **Create a community-based financial counseling network.** One-on-one financial counseling has proven to be an effective method for building wealth in the Latino community. Congress should create a community-based financial counseling infrastructure similar to the Housing Counseling Program that the Department of Housing and Urban Development currently oversees. The primary purpose of the program would be to help consumers manage their personal finances, learn how to avoid unmanageable debt, and spot credit card-related and other scams in the community. Resources would be used to hire and train community-based financial counselors and to develop software to track client progress.

- **Improve the consumer complaint system.** Federal regulators should market their consumer complaint centers and highlight any toll-free consumer complaint phone number on all materials sent by credit card issuers to consumers. Furthermore, this information should be provided in languages and formats that consumers understand. Finally, federal regulators should collect consumer complaint information by race and ethnicity to more effectively detect trends within segments of the population, help to shape efforts to eradicate scams, and develop strong cases against predators.

CONCLUSION

It is critical that Congress take the necessary steps to eliminate disparities in credit markets and enact legislation to protect consumers from harmful industry policies and practices. Furthermore, it is vital that the voice of Latino and immigrant communities be part of the debate. The ability of all consumers to save for a home, their retirement, or an education is not a narrow special interest.

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[1] Kochhar, Rakesh, *The Wealth of Hispanic Households: 1996 to 2002.* Washington, DC: Pew Hispanic Center, 2004.

[2] *Improving Credit Card Consumer Protection: Recent Industry and Regulatory Initiatives*, Testimony by Sheila C. Bair, Chairman, Federal Deposit Insurance Corporation, before the U.S. House Financial Services Committee, June 7, 2007.

[3] NCLR calculation based on unpublished tables from the 2004 Survey of Consumer Finances.

[4] Silva, Javier, and Rebecca Epstein, *Costly Credit: African American and Latinos in Debt.* Demos, May 2005.

[5] *Ibid.*

[6] Ibarra, Beatriz and Eric Rodriguez, *Latino Credit Card Use: Debt Trap or Ticket to Prosperity?* National Council of La Raza, 2007. The report is available at www.nclr.org/creditcards.
[7] Wheary, Jennifer and Tamara Draut, *Who Bears the Cost of Credit Card Deregulation*, Demos, work in progress.
[8] Stegman, Michael, et al., "Automated Underwriting: Getting to 'Yes' for More Low-Income Applicants," Presented before the 2001 Conference on Housing Opportunity, Research Institute for Housing America, Center for Community Capitalism, University of North Carolina at Chapel Hill, April 2001.
[9] *Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers*, Government Accountability Office, September 2006.
[10] Unpublished data from the 2004 Survey of Consumer Finances tabulated by the Federal Reserve on behalf of NCLR.
[11] *Ibid.*
[12] *Ibid.*
[13] *Who Bears the Cost of Credit Card Deregulation, op. cit.*
[14] Consumer Action Credit Card Survey, 2007.
[15] "Consumer Fraud in the United States: An FTC Survey," Federal Trade Commission Staff Report, August 2004.
[16] *A Conversation on Latino Credit Card Use*, Transcript from a Roundtable Discussion held at the 2006 NCLR Annual Conference in Los Angeles, California.

Written statement
before the

Committee on Financial Services Committee
United States House of Representatives

on

"Improving Federal Consumer Protection in Financial Services"

July 25, 2007

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Chairman Frank, Ranking Member Bachus, and Members of the Committee:

Thank you for the opportunity to appear here today to discuss the current state of consumer protection in financial services regulation and to make recommendations for action in the wake of tremendous changes in the marketplace and consolidation of significant authority in the hands of federal banking regulators.

Older Americans and Financial Services

The traditional aversion to debt among older consumers has given way in recent years to a much more expansive use of credit among today's retirees and near retirees. As baby boomers approach traditional retirement age, the growing number of older persons with mortgage debt and credit card balances is of real concern. At the same time, AARP is concerned about the affordability of basic banking services for seniors. Our research demonstrates that too many moderate- and lower-income older consumers do not use a financial institution because they are afraid of the fees they will incur.

A major priority for AARP is to assist Americans in accumulating and effectively managing adequate retirement assets. A key to achieving this goal is helping individuals better manage financial decisions and protecting consumers from financial fraud and abuse that can erode retirement savings and financial assets.

The recent meltdown in the subprime mortgage market, rising levels of home foreclosures and credit card debt, increasing bank fees and questionable practices, and a steady erosion of state authority to protect consumers of financial services has brought us here today to discuss two main issues:

- The adequacy of current federal consumer protection rules and recommendations for improvement; and
- The potential future role of state agencies in protecting financial consumers.

Current Federal Consumer Protection Oversight and Enforcement

The sheer number of hearings in this Congress[1] devoted to exploring the shortcomings in the current federal regulatory system is evidence enough that the system is less than adequate when

[1] The House Financial Services Committee and Subcommittees have held at least seven hearings this Congress, including hearings the March 27th hearing on Subprime and Predatory Mortgage Lending; April 17th hearing on Possible Responses to Rising Mortgage Foreclosures; April 26th hearing on Credit Card Practices; June 7th hearing on Improving Credit Card Consumer Protections; June 13th hearing on Improving Federal Consumer Protection in Financial Services; June 19th hearing on Consumers' Ability to Dispute and Change Inaccurate Information; and the July 11th hearing on Overdraft Protection. The Senate Banking Committee has held five hearings, including the January 25th hearing on the Credit Card Industry; February 7th hearing on Predatory Lending and Home Foreclosures; March 22nd hearing on Mortgage Market Turmoil; April 17th hearing on the Subprime Mortgage

it comes to protecting consumers of financial services. As Members of this Committee are well aware, there have been more than a dozen hearings in the House and Senate in the first seven months of this Congress that examined issues related to predatory lending, subprime mortgage lending, credit card practices, bank fees, and credit reporting. The testimony presented at these hearings has documented the very real costs to consumers when financial services regulators fail to act in a timely or effective manner against abusive and unfair practices.

The statistics are sobering:

- Projections are that one in every five families who get a subprime mortgage today will lose their home to foreclosure. That translates to 2.2 million borrowers who stand to lose as much as $164 billion in wealth in the process.[2]

- In 2006, American consumers paid over $89 billion in fees, interest payments, added costs on purchases, and other charges associated with their credit cards.[3]

- Banks and other financial institutions collected over $17.5 billion in overdraft fees in 2006, up 75 percent from 2004.[4]

Add to this list the cost to consumers of demand drafts used by fraudulent payday lenders and telemarketers to access consumer bank accounts; unequal treatment of debits and credits to checking accounts under "Check 21" provisions; and unauthorized garnishment of Social Security and other federal benefits and it is clear why so many consumers find themselves in financial difficulty.

Over the course of the last several decades, the effectiveness of the regulatory system has eroded, as the substantive state role in credit regulation has been preempted and the federal government has declined to fill in the gap. Instead, the federal regulators have been overly reliant on disclosures that have proven to be ineffective. The simple fact is that disclosure documents today often are meaningless, with pages and pages of incomprehensible text that works to obfuscate more than illuminate. Often the timing of the disclosure is delivered too late for the consumer to act. And, we have outdated laws that do not take into account the realities of the new credit products in the financial marketplace.

Market; and the June 25th hearing on Ending Mortgage Abuse. The Senate Permanent Subcommittee on Investigations held a March 7th hearing on Credit Card Practices.

[2] Center for Responsible Lending, "Losing Ground: Foreclosures in the Subprime Market and Their Costs to Homeowners," December 2006. http://www.responsiblelending.org/pdfs/CRL-foreclosure-rprt-1-8.pdf

[3] Elizabeth Warren, "Unsafe At Any Rate," Democracy, Issue #4, Spring 2007. http://www.democracyjournal.org/article.php?ID=6544

[4] Center for Responsible Lending, "Out of Balance," July 11, 2007. http://www.responsiblelending.org/pdfs/out-of-balance-report-7-10-final.pdf

Just as the legal context has changed since the regulatory system was first designed, so too has the economic context. Consumer debt is a more important part of the economy, making it more important than ever to assure a fair marketplace.

The oversight role this Committee and your colleagues in the Senate has performed in terms of casting a spotlight on the regulatory system's ability to adequately protect consumers is critically important to the process of restoring fairness and integrity to the financial marketplace. It is encouraging to see industry participants and regulators alike acknowledge the need for stepped up regulation and enforcement and industry best practices. However, it is equally important that Congress take the steps necessary to institutionalize reform, so that progress continues when the spotlight dims.

The challenge in updating the federal regulatory system is not to be underestimated. Substantial hurdles will have to be overcome to effect meaningful and sustained reform, including:

- **Heavy emphasis on safety and soundness regulation, potentially at the expense of consumer protection.** The primary focus of the federal banking regulators is the financial safety and soundness of the institutions they are charged with overseeing. The Office of the Comptroller of the Currency's (OCC) preemption rules, for example, emphasize the goal of giving national banks wide latitude to conduct their business activities in accordance with "uniform [federal] standards of operation and supervision that" that will reduce compliance costs and maximize profits and stability.[5] While safety soundness and consumer protection functions sometimes coincide, these goals may be in conflict. Practices that may improve a financial institution's bottom line may not be in the consumer's best interest.

- **Reliance on examinations and case-by-case actions rather than rulemaking and enforcement.** Federal banking regulators generally work to enforce compliance through the supervision and examination process. This process is highly discretionary and lacks transparency. Findings generally are confidential and not available for public review. While this process may assist in resolving safety and soundness concerns at the financial institution level, it is not necessarily effective in correcting abusive practices against individual consumers. The most effective way to ensure fair dealings in the marketplace is to establish clear, firm rules and enforce those rules with clear, firm consequences.

- **Slowness to act in the face of overwhelming evidence of a problem.** It took nearly four years for regulators to act after the first warning signals of problems in the subprime marketplace. In fact, at the same time that the regulators were seeing signs of trouble, they were continuing to encourage the development and use of adjustable rate mortgages that are now defaulting in record rates.[6] Similarly, just a few months ago, the Federal

[5] 69 Fed. Reg. 1904, 1907-08 (2004) (preamble to OCC's activities preemption regulation).

[6] See the opening statement of Senate Banking Committee Chairman Christopher Dodd, "Mortgage Market Turmoil: Causes and Consequences," hearing, March 22, 2007: "Regulators tell us that they first noticed credit standards deteriorating late in 2003. By then, Fitch Ratings had already placed one major subprime lender on

Reserve Board proposed its first major revision of the credit card disclosure rules in nearly 40 years, despite the enormous changes that have taken place in the industry during that time.

- **Dependence on disclosure rather than substantive regulation to protect consumers.** Certainly, effective disclosure should be an important component of any consumer protection regulatory regime. At the same time, disclosure should not be considered a substitute for substantive regulation, but rather a complement to it. While the federal emphasis on disclosure makes sense in a context where states can undertake the substantive regulation necessary for effective consumer protection, it makes far less sense in an environment where the federal government occupies so much of the financial services regulatory field.

Enhancing Consumer Protection in Financial Services

This Committee has played a key role in spotlighting the abuses that have caused such turmoil in the subprime mortgage market and have plagued consumers of financial services in the credit markets. Congress now has a very real opportunity to put in place meaningful reforms that will minimize abusive practices. While we welcome the recent actions by federal banking regulators recognizing the need to put in place additional consumer protections, there is more that must be done if the hurdles to effective consumer protection are to be overcome.

Among AARP's recommendations for action are the following:

- **Authorize the Federal Trade Commission (FTC) to bring enforcement actions against national banks and thrifts for unfair or deceptive practices. Give the FTC concurrent and independent authority over national banks for all matters covered by the FTC Act.** Currently, the FTC is prohibited from enforcing this statute with respect to national banks. Congress may also want to consider granting similar authority to all federal banking regulators; at a minimum, this authority needs to be granted to the FTC which is the only agency charged with consumer protection.

- **Allow states to enforce the federal lending laws and federal unfair or deceptive practices provisions of the FTC Act against national banks.** This will help restore the "cop on the beat" consumer protection function traditionally carried out by the states. .

- **Adopt meaningful credit card reforms at the federal level**, including strict prohibitions on two-cycle billing, universal default, and other abusive practices, and required advance notice of material changes in the terms of the credit card agreement.

'credit watch,' citing concerns over their subprime business. Despite those warning signals, in February 2004 the leadership of the Federal Reserve Board seemed to encourage the development and use of adjustable rate mortgages ..."

- **Adopt meaningful rules to ensure that overdraft and other fees** imposed by financial institutions are reasonable and that customers are immediately notified that such charges are being assessed. Consumers should be given a reasonable opportunity to rectify their accounts before any additional charges or similar adverse actions are assessed.

- **Adopt meaningful reform in subprime lending**, including requirements for sensible underwriting policies that examine a borrower's ability to repay the mortgage over the life of the loan.

- **Adopt meaningful opportunities for consumer redress** by eliminating mandatory arbitration clauses in credit card and mortgage agreements and by allowing individuals to bring private rights of action under the FTC Act.

- **Establish an effective centralized complaint reporting and resolution mechanism.** Consumers cannot be expected to know which of the federal banking regulators has jurisdiction over the financial institution with which they have a dispute or complaint. As such, the concept of a one-stop complaint center makes sense, but only if it does more than simply send the customer back to the bank or discourage the customer from filing a complaint.

The State Role in Consumer Protection

The recent Supreme Court ruling in Watters vs. Wachovia Bank, N.A.,[7] which upheld the federal preemption by the Office of the Comptroller of the Currency of state laws applied to the operating subsidiaries of national banks, is the latest in a string of unfortunate federal regulatory and court actions severely limiting the role of the states in protecting consumers of financial services. AARP is a strong supporter of a robust and energetic state role in consumer protection. We have a longstanding policy in favor of a federal regulatory system that serves as a "floor," while allowing states and local governments to add their own, stronger protections.[8]

In evaluating the appropriateness of preemption, AARP urges policymakers to consider:

- the extent to which the federal or state authorities have identified and focused on the specified problem and addressed the problem satisfactorily;
- potential benefits resulting from additional federal, state or local laws;
- the possibility of intolerably high compliance burdens resulting from both federal and state regulations;
- unique state or local needs that would be adversely affected;
- the capacity of the states to respond effectively to emerging issues, unusual circumstances or unanticipated consequences; and

[7] *Watters v. Wachovia Bank, N.A.*, No. 05-1342 (U.S., April 17, 2007).
[8] AARP, The Policy Book, 2007, Financial Services and Consumer Protection, Federal and State Roles, p. 11-4.

- preserving the role of the states as laboratories for policy innovation with our federal system.

It may be cliché now, but the states often are effective consumer protectors because they are the local "cop on the beat." Consumers generally know who their state and local enforcement officials are and are more likely to complain to them rather than to someone in Washington, D.C. or some other distant place. State officials also are more likely than their federal counterparts to witness first-hand the devastation to communities that can accompany abusive financial services practices, such as predatory lending. As such, the states often can detect problems at the "emergent" stage and before they become a full blown crisis. This "early warning" role can be critical to stopping abusive or unfair practices early.

As the Committee considers the implications of the Watters decision on consumers, we urge you to integrate a state role as fully as is possible under the law. At a minimum, states should be empowered to enforce federal laws against unfair and deceptive practices if national banks engage in such activity.

Conclusion

Mr. Chairman, I want to thank you and the Committee for the opportunity to appear before you today. The issue of adequate consumer protection in the financial services arena is one that is only going to grow in importance over time. We urge Congress to do all that it can to ensure that federal and state regulators and enforcement officials are given all the tools they need to adequately protect consumers from the abuses we are witnessing today ...and those that will emerge in the future.

Testimony of

Arthur C. Johnson

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Committee on Financial Services

United States House of Representatives

July 25, 2007

Testimony of Arthur C. Johnson
on behalf of the
American **Bankers** Association
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July 25, 2007

Mr. Chairman and members of the Committee, my name is Arthur C. Johnson. I am Chairman and Chief Executive Officer of United Bank of Michigan, headquartered in Grand Rapids, Michigan. I also serve as Vice Chairman of the American Bankers Association (ABA), and am testifying today as a representative of the ABA. The ABA, on behalf of the more than two million men and women who work in the nation's banks, brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks – makes ABA the largest banking trade association in the country, representing both state and federal charters in our dual banking system.

The ABA appreciates the opportunity to present its views regarding how best to protect consumers in light of the recent United States Supreme Court decision in *Watters* v. *Wachovia*.[1] That decision, by settling the question of who has jurisdiction over operational subsidiaries of national banks, enables the banking industry to move beyond the question of ***who*** supervises to the question of ***how best*** to supervise.

[1] *Watters* v. *Wachovia*, __ U.S. __, 127 S.Ct. 1559, 167 L.Ed.2d 389, 75 USLW 4176 (2007) (available at http://www.supremecourtus.gov/opinions/06pdf/05-1342.pdf).

The *Watters* decision was the latest in a long line of decisions, including Supreme Court decisions, that upheld the preemption authority of the OCC under the National Bank Act. *Watters*, by clarifying the law applicable to bank operating subsidiaries, helps to assure a fair and predictable legal and regulatory environment. It also helps to maintain the flexibility that state and federal regulators need in order to adapt to the constant changes that are inevitable in a dynamic and growing banking industry responding to changing customer demands and needs. Both domestically and internationally, a balanced and effective legal and regulatory environment is critical to assure the competitive banking system necessary to finance a vibrant economy. In the aftermath of the *Watters* decision, the resources of state and federal regulators now may be devoted fully and more efficiently to assuring a safe and sound industry that preserves and enhances public trust. This is a very positive development for all concerned.

Maintaining our customers' trust is core to the business of banking. No bank will be successful over the long term if it does not treat its customers well. It is therefore imperative that banks take steps to protect their customers' deposits and financial information, provide accurate settlement of financial transactions, respect consumer legal rights, and provide excellent customer service. Thus, consumer protection is a high priority for banks. Banks spend a considerable amount of time and resources to assure compliance with the law, and we are examined carefully by our primary regulator to assure that this is so.

The ABA believes enhanced cooperation between state and federal regulators to facilitate appropriate oversight of consumer protection efforts can benefit customers and financial institutions alike, drawing upon the strengths of each regulator's separate authorities.

In my testimony I would like to make the following points:

I. The dual banking system – with each state and federal governmental agency responsible for the institutions within its primary jurisdiction – is the best framework to ensure a balanced legal and regulatory environment for the efficient and effective enforcement of consumer protection laws.

II. Universality and uniformity of consumer compliance oversight is an agency priority that ABA supports, including vesting joint rulemaking authority in all the Federal banking agencies to implement Section 5 of the Federal Trade Commission Act (FTCA), governing unfair and deceptive acts or practices.

III. Consumers are best protected when banks make compliance everyone's business.

I. The Dual Banking System Provides a Balanced Legal and Regulatory Framework

The dual banking system has been enormously successful in creating an environment that encourages innovation, fosters safe and sound banking, and serves consumers well. It is a foundation upon which our banking industry is built and has served the nation well for over 140 years, creating an unsurpassed financial engine to power history's greatest economy serving the world's most prosperous citizens.

While many have observed that no one would start out to create such a banking regulatory system, it is hard to argue with its success in promoting safety and soundness and consumer confidence. The system works best when it works as intended. State and federal regulators are each responsible for oversight of distinct and well-defined groups of financial institutions, but banking agencies in both domains share the mission of regulating comprehensively to promote the vitality of the system, central to which is promoting the interests and confidence of bank customers. This division of responsibility—but unity of mission—that has been created by Congress and sanctioned by the courts enables the

regulators to use their limited resources efficiently and effectively. It also enables different governmental actors to respond to different concerns in the manner deemed most appropriate for the people and institutions within their field of responsibility.

The *Watters* case is the most recent in a long line of cases that have affirmed the dual banking system and confirmed the roles anew. We now can stop working at cross purposes and shift the focus to how the state and federal regulators can build off each other's strengths. The way has been opened for strengthening cooperation among agencies with separate jurisdictions but ***common purpose*** -- to ensure that financial customers are treated fairly.

Many recent initiatives have been undertaken to assure just that. Examples of these initiatives include the following:

- In 2006 the State Liaison Committee – comprised of the Conference of State Bank Supervisors (CSBS), the American Council of State Savings Supervisors, and the National Association of State Credit Union Supervisors – was added to the Federal Financial Institutions Examination Council (FFIEC) as a voting member. This provides the states with a direct voice in all matters coming before the FFIEC.
- The Office of the Comptroller of the Currency (OCC) has an initiative underway, as discussed by Comptroller Dugan in his testimony before the Committee on Financial Services on June 13, 2007, to conduct parallel exams with state regulators of national banks and independent mortgage brokers, respectively. This approach is likely to provide the regulators with a better understanding of the roles of the various actors in the mortgage origination process and to position the regulators better to address weaknesses wherever found, including those that occur outside of the banking industry.

- The Federal Reserve Board and the Office of Thrift Supervision (OTS) announced on July 17, 2007, a joint initiative with the Federal Trade Commission, the CSBS, and the American Association of Residential Mortgage Regulators to improve the supervision of subprime mortgage lenders.[2] Pursuant to that initiative, the federal and state regulators will conduct targeted consumer protection compliance reviews of non-depository lenders with significant subprime mortgage operations.
- The OCC and the OTS, working with the National Association of Insurance Commissioners, have entered into cooperation and information sharing agreements with 49 state insurance regulators and the District of Columbia. These agreements require the parties to send to the appropriate regulator copies of any complaint received that relates to insurance sales. The state insurance departments will handle matters regarding insurance activities, while the OCC or OTS (as appropriate) will handle matters regarding banking or savings association activities. The parties to the agreements communicate with each other to the fullest extent possible on matters of common interest and keep each other apprised of the resolution of any complaint that is referred.
- The OCC and OTS also have entered into a model Memorandum of Understanding (MOU) with the CSBS and are now negotiating with the states to enter into MOUs directly with the state regulators.[3] Pursuant to those agreements, a regulator that receives a consumer complaint about an institution outside of its jurisdiction will refer

[2] *See* http://www.federalreserve.gov/boarddocs/press/bcreg/2007/20070717/default.htm.

[3] The OCC has entered into 20 agreements with states and the Commonwealth of Puerto Rico since signing its agreement with the CSBS. The OTS agreement with CSBS was executed after the OCC agreement, and thus the OTS is earlier in the process of negotiating final agreements with the individual states.

the complaint to the appropriate agency, and the referring agency will be informed of the resolution of the complaint.

- The OCC recently supplemented the referral system with a website, at http://www.helpwithmybank.gov, designed to help customers figure out whether they are dealing with a national bank and then to provide assistance to those who are. The Comptroller has proposed to the other members of the FFIEC that this site be developed further into a one-stop approach to assisting all consumers regardless of the type of financial institution they use.[4]

Initiatives of this nature are important steps to ensure that consumers' complaints will be heard – and acted upon – by the agency with the authority and resources to address the problem.

Each governmental entity within the dual banking system has specific responsibilities with regard to enforcement. State and local governments can regulate a national bank with respect to zoning rules or tax obligations, for instance. They may not, however, regulate a federally-chartered bank or savings association or its subsidiary with respect to a law governing the business of banking. This limit on state authority clearly applies to consumer protection laws, as underscored, for example, by the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, in which Congress stated that the OCC was to enforce applicable laws regarding community reinvestment, consumer protection, fair lending, and the establishment of intrastate branches. This division of supervisory responsibility works both ways, of course. For instance, the OCC is precluded from taking action against a state bank for a violation of applicable federal law.

The ABA believes that these distinctions are appropriate. The strength of a national system of banking is that it operates under a program of uniform laws, uniformly applied. These laws can only be developed, and are best enforced, at the federal level. This ensures a consistent protection for customers of federally-chartered firms regardless of their location and avoids federal policy being made—or frustrated—in a piecemeal fashion through litigation at the state level.

Bank regulators, unlike law enforcement agencies, have many tools that enable them to exercise due regard for safety and soundness and systemic risk considerations together with enforcement responsibilities. These range from the behind-the-scenes citation of an issue in an exam report as a matter requiring attention to the public actions of issuing a cease-and-desist or civil money penalty order or even closing a bank and imposing lifetime bans from participating in banking activities. Simply put bank regulators are just as concerned about consumer protection as are law enforcement authorities, but the bank regulators are better able to achieve their objectives through an enormous array of enforcement options that allow them to meet their broader mandate for law enforcement as well as financial stability.

Moreover, the bank regulators have a complete picture of any given bank. This picture is obtained through the frequent (and in some cases continuous) examinations of banks and the regulators' complete access to all of a bank's books and records. Thus, they are in a better position than any other actor to spot and address problems early, to calibrate an enforcement response to the situation, and to place the action within the context of the overall safety and soundness of the institution and the stability of the financial system.

[4] *See* OCC News Release 2007-73, July 17, 2007.

State Attorneys General and other law enforcement bodies do not have a safety and soundness mandate or systemic risk concerns. They are focused on questions of law and have only law-enforcement tools, such as the ability to sue, in order to achieve their objectives. As the old saying goes, when all you have is a hammer, the whole world looks like a nail. Law enforcement agencies hold, in essence, only a hammer. Yet our national financial policies require a very high regard for safety and soundness and systemic risk concerns as well.

States that identify local concerns that warrant a unique response are free to regulate in a manner they deem appropriate for the state-chartered institutions within their jurisdiction. However, it is appropriate that the federal component of the dual banking system remain subject to policies that are developed and enforced at the federal level. The consumer is then free to choose the institution that offers the products and services that best meet the consumer's needs.

It must be noted that states have very real issues arising from the institutions within their primary jurisdiction that demand their attention and enforcement resources. The most recent example of this involves the issue of subprime lending. As repeatedly noted in testimony recently provided to the House Financial Services Committee in a hearing on Improving Federal Consumer Protection in Financial Services,[5] many of the problems in the subprime area have arisen in institutions outside the enforcement jurisdiction of the federal bank regulators.

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[5] *See* Testimony of John C. Dugan, Comptroller of the Currency, Before the Committee on Financial Services of the U.S. House of Representatives, June 13, 2007, at 28 ("The abuses in the subprime lending business – loan flipping, equity stripping, and making subprime loans that borrowers have no realistic prospect of repaying – simply have not seeped into the national banking system."); and Testimony of Sheila C. Bair, Chairman of the Federal Deposit Insurance Corporation, Before the Committee on Financial Services of the U.S. House of Representatives, June 13, 2007, at 4 ("Another significant change in the financial system has been the increased participation by providers other than banks and thrift institutions. For example, one estimate shows that some

Before the current subprime issues there were problems with predatory lending by non-bank lenders. In commenting on an OTS proposal concerning preemption of state lending standards, a coalition of 46 state attorneys general stated:

> Based on consumer complaints received, as well as investigations and enforcement actions undertaken by the Attorneys General, predatory lending abuses are largely confined to the subprime mortgage lending market and to non-depository institutions. Almost all of the leading subprime lenders are mortgage companies and finance companies, not banks or direct bank subsidiaries.[6]

The point is not to suggest that federal regulators have fewer issues to deal with than do state regulators, or vice versa. Rather, the point is that all regulators have demands on their resources, and the current division of labor is appropriate in light of this fact. The current system is the best approach for applying supervisory resources in the most efficient and effective manner.

Many new actors in the businesses of mortgage lending and consumer finance (for example) have thus far been able to operate subject to comparatively little supervision in many instances. Concentrating enforcement resources on the banking industry adds potentially significant burden in return for little gain while diverting resources away from industries whose customers would benefit from closer attention.

The dual banking system functions most effectively and efficiently when there is a respect for the division of regulatory authority. A misallocation of resources that creates

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52 percent of subprime mortgage originations in 2005 were carried out by companies that were not subject to examinations by a federal supervisor.").

[6] Brief for Amicus Curiae State Attorneys General, *Nat'l Home Equity Mortgage Ass'n* v. *OTS*, Civil Action No. 02-2506 (GK) (D.D.C.) at 10-11.

redundant supervisory and enforcement authority over entities that already are heavily regulated while allowing other financial institutions to escape largely unregulated is unlikely to provide the best protection for customers. Stated another way, a system of checkers checking checkers, while leaving demonstrably troubling activity inadequately supervised, is unnecessary for an industry that depends on uniform laws uniformly applied and counterproductive from the perspective of consumer protection.

II. Uniformity and Vigilance of Consumer Compliance Oversight is a Federal Banking Agency Priority—and one that ABA Supports

The application of consistent consumer protection policy has been achieved through two primary vehicles: First, the development of common standards and examination procedures in fulfillment of the mandate of Congress in establishing the Federal Financial Institutions Examination Council (FFIEC); and second, the implementation of a direct consumer complaint process to address unfair or deceptive practices in fulfillment of the mandate of Congress in Section 18 of the FTCA.[7] These two vehicles work in tandem to create a process of focused consumer compliance oversight and a strong supervisory expectation that banks adopt a self-correcting culture of compliance—an expectation that I and my colleagues strive in earnest to meet.

Coordinated Supervision through the FFIEC

The FFIEC is charged with prescribing "uniform principles and standards for the federal examination of financial institutions…and mak[ing] recommendations to promote uniformity in the supervision of these financial institutions. The Council's actions shall be designed to promote consistency in such examination and to insure progressive and vigilant

[7] 15 U.S.C. 57a.

supervision."[8] Through its Task Force on Consumer Compliance, the FFIEC fulfills its statutory purpose in the area of consumer protection by developing and issuing interagency examination procedures covering over a dozen federal consumer protection statutes—including the Truth-in-Lending Act (which, in turn, includes the Home Ownership and Equity Protection Act, frequently referred to as HOEPA), the Fair Debt Collection Practices Act, and the FTCA's Section 5 prohibition on unfair or deceptive acts and practices as implemented by the Credit Practices Rule, to name just a few.

In addition, the FFIEC agencies have set forth common standards for arriving at a bank's, or savings association's, rating for consumer compliance performance. This rating stands as an identifiable grade separate and apart from the CAMELS rating so that boards of directors can hold their managements directly accountable for the quality of their institution's compliance management programs and performance.

The banking agencies within the FFIEC have gone a step further and coordinated their examination and interpretation of the Community Reinvestment Act (CRA) regulations, taking time to make specific provision for how illegal credit practices and discriminatory conduct will adversely affect the bank's CRA rating. Moreover, the FFIEC's Task Force members have endorsed top-down compliance oversight so that banks and savings associations are all expected to implement consumer compliance programs that contain system controls, monitoring of performance, self-evaluation, accountability to senior management and the board, self-correcting processes, and staff training.

In execution of these uniform standards the FFIEC agencies and state banking agencies are able to invoke the enormous array of options discussed earlier. Perhaps the most

[8] 12 U.S.C. 3301.

important of these is the regularity of on-site examination. On a periodic basis, FDIC examiners visit my bank and spend 3-6 weeks examining our compliance management program, as well as our track record for meeting our consumer protection obligations. In the case of some of my colleagues at much larger banks, examiners are there every business day of every business week, year-in and year-out.

Agency Obligations and Authority under the FTCA

The second vehicle that works to assure strong compliance oversight is the dedicated consumer complaint processes that each of the federal banking agencies has implemented in furtherance of the mandate of the FTCA's Section 18. At the June 13 hearing, each agency testified to its respective complaint processing program. These programs treat each consumer complaint as its own case receiving individualized attention. The sum and substance of these complaints and their trends are used by the agencies to focus their examination programs on potential deficiencies. In fact, in the rare case where a complaint suggests a serious breach, the agency may intervene by special examination.

The federal banking agencies' discharge of FTCA Section 18 duties does not end with complaint processing. Under that section, each agency is tasked with addressing any unfair or deceptive practices that arise. In fulfillment of this obligation, the agencies actively work to help banks and thrifts avoid practices that would be considered unfair or deceptive under section 5 of the FTCA (the "UDAP law").[9] In regulations,[10] guidance,[11] enforcement

[9] 15 U.S.C. 45(a).

[10] *See, e.g.*, 12 C.F.R. § 7.4008(c) (OCC rule incorporating Federal Trade Commission UDAP law into law governing national bank lending); 12 C.F.R. Part 227 (Federal Reserve Board rule on Unfair or Deceptive Acts or Practices); 12 C.F.R. Part 535 (OTS rule on Prohibited Consumer Credit Practices); and 12 C.F.R. § 563.27 (OTS rule on Advertising).

[11] *See, e.g.*, Interagency Guidance on Nontraditional Mortgage Product Risk, 72 Fed. Reg. 37569 (July 10, 2007); Joint Guidance on Overdraft Protection Programs, 70 Fed. Reg. 9127 (Feb. 24, 2005); Joint Federal Reserve

actions,[12] speeches,[13] and other documents,[14] the agencies have repeatedly punctuated their communications to banks and savings associations with references to the UDAP law. What is as important as the breadth of transactions that the regulators have addressed is the fact that not a single one of the federal banking agencies has shied away from asserting its authority to examine for compliance with, or enforce, the UDAP law under the common authority of Federal Deposit Insurance Act Section 8(i)[15] and other enabling legislation.

Nevertheless, there is an historical anomaly in the grant of regulatory authority for UDAP enforcement. Although each agency is directly required to implement a consumer complaint process and to address any resulting claims of unfair or deceptive practices, only the Federal Reserve Board, OTS, and National Credit Union Administration (NCUA) have explicit rulemaking authority to implement the UDAP law.[16] The OCC and FDIC do not. While each agency has asserted the authority to enforce the UDAP statute, arguably not every agency has the authority to define in advance through a rulemaking what practices are unfair or deceptive.

Board and Federal Deposit Insurance Corporation Guidance on Unfair or Deceptive Acts or Practices by State-Chartered Banks (March 11, 2004); FDIC Guidance on Unfair or Deceptive Acts or Practices, FIL-57-2002 (May 30, 2002); OCC Advisory Letter 2002-3 (March 22, 2002) (informing national banks and their operating subsidiaries about the risks of engaging in unfair or deceptive acts or practices); Federal Reserve Board Staff Guidelines on Credit Practices Rule (effective Jan. 1, 1986)

[12] *See, e.g.*, Dugan Testimony, at Appendix B (listing 10 public enforcement actions brought by the OCC under the FTC Act).

[13] *See, e.g.*, Remarks by Julie L. Williams Before the Annual Meeting of the Cleveland Neighborhood Housing Services (June 15, 2004); Remarks by Julie L. Williams Before the Mid-Atlantic Bank Compliance Conference, Annapolis, MD (March 22, 2002)

[14] *See, e.g.*, Letter from Alan Greenspan, Chairman of the Federal Reserve Board, to The Honorable John J. LaFalce, May 30, 2002; FDIC Compliance Handbook, Section VII: Abusive Practices; Federal Trade Commission Act, Section 5 Unfair or Deceptive Acts or Practices; OTS Examination Handbook, Section 1355 "Consumer Affairs Laws and Regulations: Unfair or Deceptive Act," (Dec. 1999).

[15] 12 U.S.C. 1818(i).

[16] 15 U.S.C. 57a(f)(1).

To address this anomaly, we support vesting all of the federal banking agencies with UDAP rule-writing authority to be exercised ***jointly***. Only by a grant of ***joint*** authority can we maintain uniformity in any formal regulatory action to impose specific UDAP standards on the different components of the banking system.

Just as it is anomalous to vest rulemaking authority in some but not all of the banking agencies, it would be anomalous – and harmful – for the five federal agencies that are members of the FFIEC to adopt different standards of what is an unfair or deceptive act or practice. An act becomes no more or less unfair or deceptive by virtue of the actor's type of charter. Thus, there is no reason to vest the banking regulators with authority to initiate individual rulemakings under the UDAP law.

Indeed, there is a good reason ***not*** to vest the agencies with ***independent*** rulemaking authority under the UDAP law. Consumers should receive the same level of fair treatment at all financial institutions. Weaker consumer protection standards at only some financial institutions can taint the entire industry, while overly prescriptive standards imposed on only some institutions result in unnecessary burdens on the affected entities. Neither outcome is desirable. We can be certain that both will be avoided only by the joint exercise of rulemaking authority.

To avoid inconsistent treatment of consumers in financial institutions outside the jurisdiction of the FFIEC agencies, states should fund a corresponding supervisory program for state-chartered, non-bank financial firms by a system of fees comparable to the fees that both state and federally-chartered banks pay for supervision. Identifying unfair or deceptive acts or practices for all financial institutions can benefit not only consumers but also the institutions that serve them by providing clear standards of conduct. This also would

safeguard the banking industry from being tainted by practices that occur outside the industry. Moreover, to the extent that the rules are effectively applied to all lenders, then we would avoid the perverse result of a strong bank supervisory program driving business to lower-cost/lightly supervised firms operating outside of that program.

The problems in the subprime market are a prime example of the dangers of business moving to the unregulated market. Bankers across the country have seen numerous examples of bank customers, or potential customers, being steered to unsafe mortgages by real estate agents and mortgage brokers. In many cases bankers told their customers that the banks could not match the initial monthly payments on these mortgages but that the mortgages were going to reset, only to have the customers ignore the danger. And yet, bankers are concerned that solutions that are being proposed will not apply, or not apply effectively, to non-banks. This is the inherent weakness in the recent guidance from the regulators, which we otherwise support.

There are considerable challenges in trying to identify a practice that is inherently unfair or deceptive. Frequently, the determination of whether a practice is objectionable can be made reliably only after considering the context of a particular transaction. Certain loan features may impose additional obligations on a consumer in exchange for a lower interest rate. Other features, while perhaps less attractive than those offered by another lender, may be perfectly legitimate as long as they are adequately disclosed. It must be remembered that the abuse is found in the practice rather than the product. Any traditional product can become a vehicle for abuse, and many innovative products have been proven to be powerful means of serving the special needs of customers and promoting economic inclusion.

Thus, the determination of what is unfair or deceptive needs to be made carefully so as to restrain abusive practices and not to curtail products that can be beneficial under a variety of circumstances.

III. Consumers are best protected when banks make compliance everyone's business.

Before closing, I want to emphasize how seriously the ABA members and the industry that I represent take our responsibilities to deliver compliant services and products and to treat our customers fairly in the process. Take my bank as an example. Upper management and our board expect all our employees to treat all our customers not only in accordance with the law but also in accordance with our business ethics. To that end, we have a compliance training program that is required for all of our employees – not just our compliance officer. In addition, compliance management plays a role in every operational aspect of our bank that comes into contact with customers—from the marketing of products, through account opening and credit administration, to handling personal information and monitoring for financial crime. Further, we hold our employees accountable for meeting their obligations. This is especially true for our compliance officer—who in my case happens to be my son.

But the important thing to realize is that our bank is typical of the thousands of others that invest heavily in a compliance culture—each with dedicated compliance professionals who take great pride and apply tremendous effort to assure that consumers in the dual banking system are getting treated fairly. It is rare to find the employees in any organization who are satisfied that they are getting the resources they need. Yet when ABA recently conducted its survey of compliance officers in banks of all sizes and asked them whether their boards consistently provided them the support they required, fully 93 percent of the over 400 respondents replied, "Yes."

As former Comptroller Eugene Ludwig said at the recent annual ABA Regulatory Compliance Conference attended by more than 1,100 industry professionals, the principles of a first-class compliance program are all aimed at "getting it right the first time." This is ultimately the aspiration of our entire industry, and our compliance programs are designed to correct our course when we stray—even before the examiner shows up or a consumer complaint is received. This is what we mean by self-identifying and self-correcting compliance management. No one is perfect. But no industry tries harder to get it right.

Some bankers say compliance is everyone's job, and it is. But I like to say that compliance is everyone's business—because each time we have a chance to serve a customer we have an opportunity to show them just how much we respect them and deserve their trust and their business. This is the cornerstone of successful banking and responsible customer service, and it is what will enable us to continue meeting our customer's needs over the long-term.

Conclusion

Our dual banking system has served the country well. The state and federal regulators have been instrumental in preserving the public trust that is so vital to a healthy banking system. Current efforts at cooperation between the state and federal regulators are just the most recent example of how the dual banking system can work to protect consumers. Through information sharing agreements, joint examinations, and referrals of customers to the appropriate regulator, everyone – including the states, the federal government, and consumers – can be assured that a consumer complaint will be heard by the appropriate agency and that the agency will be accountable for its actions. We have, in short, an

appropriate division of labor inherent in our dual banking system. Our recommendations are designed to build upon and reinforce the strengths of that system.

We also have a federal system that has provided extensive – and uniform – protection for consumers. The fair treatment of consumers does not vary by charter, nor should it. The federal bank regulators have acted in a consistent manner to protect individuals, and the same consistency should be applied to the implementation of the UDAP law.

Statement of

James C. Sivon

Partner
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Before the
Committee on Financial Services

Of the
U.S. House of Representatives

July 25, 2007

Chairman Frank, Ranking Member Bachus, and members of the Committee, my name is Jim Sivon, and I am a partner in the Washington, D.C. law firm of Barnett Sivon & Natter, PC. Our firm specializes in financial services law and regulation. I appreciate the opportunity to appear today to discuss consumer protection in the financial services industry following the U.S. Supreme Court's decision in *Watters v. Wachovia Bank.*

The decision in the *Watters v. Wachovia Bank* case is the latest in a long line of decisions by the U.S. Supreme Court interpreting the National Bank Act. As a whole, those decisions have insulated national banks from state interference with the conduct of their banking business. This has permitted the development of our national banking system as envisioned by its authors, President Lincoln and his Treasury Secretary, Salmon P. Chase. President Lincoln and Secretary Chase foresaw how a system of national banks could contribute to the growth and development of our nation. Today, almost 145 years since the passage of the National Bank Act, we have a system of healthy and financially strong national banks that serve as an important source of credit and opportunity for consumers and businesses.

At the same time, it is important that federally chartered banks and thrifts are responsive to consumers and treat them fairly. In order to highlight some of the consumer protection issues facing national banks and federal thrifts following the decision in *Watters v. Wachovia*, I have organized my statement chronologically from the beginning of a consumer credit transaction to the end of the transaction.

Financial Literacy

At the beginning of a credit transaction, the best protected consumer is an educated consumer; that is, a consumer who is financially literate. Financial literacy has been the focus of a significant amount of attention in recent years. Many financial services firms and financial

regulators have made a commitment to financial literacy. Citigroup, for example, has committed over $200 million over a 10 year period to support financial education programs and organizations around the world. The FDIC also has an excellent financial literacy program called Money Smart that has reached over 600,000 consumers.

Yet, financial literacy surveys by the Jump$tart Coalition for Personal Financial Literacy indicate that much more needs to be done. The Coalition has tested the financial literacy of high school students annually since 1997. Throughout that period, test scores have hovered in the low- to mid- 50 percent range. These surveys also show a gap in financial literacy between minority and non-minority students. In the most recent survey, white students scored an average of 55 percent on the test, while African-American students scored 44.7 percent, and Hispanics scored 46.8 percent.

In my opinion, the solution to this challenge is to incorporate financial literacy into the curriculum of our public school systems. This would ensure that young men and women receive financial literacy training before they become active consumers of financial products and services. A few states have modified their curriculum to require financial literacy to be taught in their public school systems. The Federal Government and the financial services industry should work with the states to make this opportunity available in all states.

Disclosure

The disclosure of the key terms and conditions of a financial product or service is the next step in the credit process, and is an important consumer safeguard. Generally, Congress and financial regulators have relied upon disclosure requirements to protect consumers rather than restrictions on price and product terms and conditions. The Truth in Lending Act, for example, requires creditors who make consumer loans to disclose all financial charges in dollar and annual

percentage terms, but does not dictate rates or conditions. I believe that this is an appropriate policy. It stimulates competition and innovation to the benefit of consumers.

However, in order for disclosures to work properly, they must be clear and understandable. As financial products and services have become more complex, disclosure requirements may have reached a point where consumers are more overwhelmed than informed. The volume of paper in a typical residential real estate closing, for example, is daunting. Some disclosures also may be counterproductive. Just last week, the American Bankruptcy Institute and the Ford Foundation released a study that found that credit card disclosures designed to prevent overspending may have the opposite effect on some consumers.

Ensuring that disclosures are informative, and not overwhelming, is a challenge. The federal banking agencies have started to make use of consumer testing and focus groups in the development of new model disclosure forms. Such testing should continue, and disclosures that are unnecessary or counterproductive should be eliminated. Congress also should resist the temptation to mandate disclosure terms, type size or other details. Detailed statutes typically result in lengthy detailed regulations. More general statutory guidance gives regulators the flexibility to craft and revise disclosures to address new products and meet the changing needs of consumers.

Uniform National Protections

After selecting a particular financial product or service, a consumer is concerned about the protections that apply to that product or service. We have a national consumer credit system, but all consumers do not enjoy the same level of protection.

The recent problems in the mortgage market illustrate the limitations of the current system. The federal banking agencies have responded to the problems in the mortgage market

with two separate interagency advisories on appropriate lending practices and policies. These advisories, however, apply only to lenders that are subject to federal supervision and regulation, not to state licensed lenders. While efforts are underway within the states to impose similar requirements on state licensed lenders, nothing guarantees that all states will adopt the same or even similar requirements. As a result, consumers that obtain a loan from a federally regulated lender receive one level of protection, and consumers who receive a loan from a state lender receive a different level of protection or no protection at all. This not only deprives consumers of comparable protections, but allows institutions to engage in regulatory arbitrage based upon different consumer protection requirements.

Consumers of a financial product or service should receive the same protection, regardless of the type of lender that provides the product or service or the jurisdiction in which the product or service is delivered. Uniform, national consumer protection requirements would meet this goal.

I recognize that individual states may wish to impose additional requirements on the lenders for local reasons. However, history has shown that some laws enacted in the name of consumer protection unintentionally have caused financial losses to insured institutions, and thereby reduced the availability of credit.[1] Federal preemption of such laws protect the fiscal integrity of national banks and federal thrifts, and the supply of credit.

On the other hand, preemption should not create a void in consumer protection. The protections afforded consumers who obtain products and services from national banks and

[1] The nation's experience with due on sale clauses is an example of state consumer protection laws that have unintended consequences. After a number of states prohibited lenders from enforcing such clauses in the wake of record high interest rates of the late 1970s and early 1980s, the economic condition of mortgage lenders worsened, and the number of insolvencies increased. Eventually, the Federal Home Loan Bank Board published a regulation preempting state laws that prohibited the enforcement of due on sale clauses, and the U.S. Supreme Court upheld the preemptive effect of the regulation in the case of *Fidelity Federal Savings & Loan Association v. de la Cuesta*, 102 S.Ct. 3014 (1982).

federal thrifts should be robust. Today, national banks and federal thrifts are subject to a number of federal consumer protection statues that protect consumers, including the Truth in Lending Act, the Equal Credit Opportunity Act, and the Fair Housing Act. Yet, we may have reached a point where additional safeguards are appropriate. Both the Federal Trade Commission Act ("FTC Act") and the Home Ownership Equity Protection Act ("HOEPA") provide the federal banking agencies with the authority to define and prohibit acts or practices by depository institutions that are unfair or abusive, whether in the mortgage area (HOEPA) or with respect to any service (FTC Act).

HOEPA

HOEPA was enacted in 1994 in response to Congressional concerns over "reverse redlining." HOEPA establishes a class of residential mortgage loans that are subject to special disclosures and other requirements. A HOEPA loan is defined as a closed-end, non-purchase mortgage loan, secured by a consumer's principal residence, that has an annual percentage rate in excess of 10 percent above Treasury securities with a comparable maturity, or that has total fees and points that exceed the greater of $400 or 8 percent of the total loan amount. The Federal Reserve Board has the authority to adjust these triggers, within certain parameters. The current triggers are 8 percent above Treasuries for a first loan, and 10 percent above Treasuries for a second loan, and the fee trigger has been raised to the greatest of 8 percent of the loan or $547 to reflect inflation.[2]

HOEPA loans are subject to extra disclosure requirements, which must be made at least 3 days prior to the loan closing. The Act also imposes substantive restrictions on these loans,

[2] 12 C.F.R. § 226.32 and Supplement I.

including prohibitions on prepayment penalties (unless certain conditions are met),[3] penalty interest rates in the event of a default, balloon payments for short-term loans, and negative amortization features. Further, a lender may not engage in a "pattern or practice" of extending credit through HOEPA loans without regard to the consumers' repayment ability, including current and expected income, obligations, and employment.

While HOEPA is primarily concerned with HOEPA loans, it also provides the Federal Reserve Board with the authority to proscribe certain practices with regard to all mortgage loans.[4] This legislation gives the Federal Reserve Board the power to regulate any act or practice that the Board determines is "unfair, deceptive, or designed to evade the provisions of [HOEPA]." With respect to re-financing transactions, the Board's authority also includes the ability to prohibit any act or practice that it determines is "abusive" or that is "otherwise not in the interest of the borrower."

The Board initially issued regulations implementing HOEPA in 1995.[5] In 2001, the Board amended these regulations to broaden the coverage of the Act and to prohibit certain practices that the Board determined were unfair, deceptive, or designed to evade HOEPA.[6] For example, the regulations state that a creditor may not restructure a HOEPA loan as an open-end line of credit loan in order to avoid coverage under the Act, and that a lender who does not verify and document repayment ability will be presumed to engage in a pattern or practice of such conduct.[7]

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[3] The loan may include a prepayment penalty if certain conditions are met and if the penalty does not apply 5 years after the date of the loan origination.

[4] 15 U.S.C. § 1639(*l*) (2).

[5] 60 Fed. Reg. 15463 (1995); 12 C.F.R. §§ 226.32 and 226.34.

[6] 66 Fed. Reg. 665617 (2001).

[7] 12 C.F.R. § 226.34.

Based upon Chairman Bernanke's recent testimony to this Committee, it appears that the Federal Reserve Board soon will propose revisions to its HOEPA rule to address unfair or deceptive acts or practices. Consistent with my earlier remarks, I would recommend that the Board use its authority under HOEPA to apply such requirements to all lenders.

FTC Act

The Federal Trade Commission Act states, at Section 5, that "unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce" are unlawful.[8] With respect to banks and savings associations, the FTC empowers the Federal Reserve Board, the Office of Thrift Supervision, and the National Credit Union Administration Board to issue implementing regulations to carry out the purpose of the Act, which must define "with specificity such unfair or deceptive acts or practices," and include requirements "prescribed for the purpose of preventing such acts or practices."[9] Enforcement authority is given to each of the appropriate federal banking agencies to enforce the Act and regulations. The FTC Act also directs each of the banking agencies to establish a separate division of consumer affairs to receive consumer complaints and take appropriate action.

To date, the FTC has not relied on regulations in this area. Instead, it has developed a body of principles through enforcement actions and policy statements. The Federal Reserve Board has promulgated one regulation to date under its FTC authority, the "Credit Practices Rule."[10] This rule declares that it is an unfair or deceptive practice for a bank to include a loan

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[8] 15 U.S.C. § 45.

[9] 15 U.S.C. § 57a(f). In addition, the statute requires that within 60 days after an FTC rule on unfair or deceptive acts or practices takes effect, the Federal Reserve, OTS and NCUA Board shall promulgate substantially similar rules, unless the agency finds that the practice is not unfair or deceptive or would interfere with monetary policy or the payments system.

[10] 12 C.F.R. § 227.11 et. seq. This rule was based upon a credit practices rule issued by the FTC, see 16 C.F.R. 444.

term in which the debtor waives certain procedural rights, agrees to an irrevocable assignment of wages, or takes a security interest in personal household goods. Additionally, the federal banking agencies have issued advisories on unfair or deceptive acts or practices based upon the FTC's policy statements, and the OCC has exercised its existing enforcement authority under Section 5 of the FTC Act on several occasions.

Ideally, any new rule based upon Section 5 of the FTC Act should be issued jointly by the federal banking agencies, in consultation with the FTC. Joint rulemaking would ensure that the rule is uniform for all federally supervised institutions. Consultation with the FTC would ensure that the federal rule is comparable to the standards the FTC applies to non-federally supervised lenders.

Crafting such a rule will not be easy. As former Federal Reserve Board Chairman Greenspan noted in a letter to former Congressman John LaFalce "it is difficult to craft a generalized rule sufficiently narrow to target specific acts or practices determined to be unfair or deceptive, but not to allow for easy circumvention or have the unintended consequent of stopping acceptable behavior."[11]

Consumer Complaints

After a consumer acquires a financial product or service, a consumer naturally expects that product or service to perform as advertised. When it does not, consumers should have appropriate recourse to lenders and regulators. All four banking agencies have established programs to receive and address consumer complaints, and each of these programs has been effective. The OCC reports, for example, that its Customer Assistance Center has helped consumers receive more than $30 million in relief over the past five years. Additionally, the

[11] Letter from Chairman Greenspan to Congressman John LaFalce dated May 30, 2002.

federal banking agencies have undertaken a number of initiatives to improve coordination with state regulators.[12]

Yet, consumers do not always appreciate the legal distinctions between different types of lending institutions, and may not be sure where to turn for assistance. Therefore, it would seem appropriate for the federal banking regulators to establish a centralized system for consumer complaints and referrals under the auspices of the Federal Financial Institutions Examination Council, which now includes a representative of state banking authorities.

Enforcement

Enforcement actions are an ultimate form of consumer protection. Cease and desist penalties, including restitution payments to consumers, and civil money penalties not only punish violators, but deter future violations. Consumers, however, do not care who enforces an applicable requirement, as long as someone does. Thus, policymakers should seek to balance the use of enforcement resources to ensure that consumers are adequately protected.

During the recent problems in the mortgage market, lenders of all types engaged in questionable practices. However, the institutions that have gone bankrupt because of their practices were state licensed and supervised. This suggests that state supervisory resources were inadequate or not adequately utilized.

In a natural allocation of supervisory resources, federal regulators should be responsible for federally chartered lenders, and state authorities should be responsible for state chartered or licensed lenders. Such an allocation is appropriate on both practical and policy grounds.

Collectively, the states supervise over 100,000 different financial institutions. Asking State Attorneys General to be responsible for national banks and federal thrifts, in addition to

[12] For example, last week, the Federal Reserve Board and OTS announced a joint initiative with the FTC, the CSBS, and the American Association of Residential Mortgage Regulators to improve the supervision of subprime mortgage lenders.

state lenders, seems an inappropriate allocation of resources. Further, as a policy matter, the system of prudential supervision exercised by the OCC and OTS can be much more efficient and effective than litigation initiated by a State Attorney General. Under federal law, national banks and federal thrifts are subject to regular examinations, and many of the nation's largest banks and thrifts have full-time, on-site examiners. This regular examination process permits federal authorities to identify potential and real violations of consumer protection statutes and regulations on a timely basis, and require corrective actions, with an impressive array of enforcement options and resources behind that requirement.

Funding

The final step in the consumer credit process is funding. This is not so much an issue for consumers, as it is a policy dilemma. Funding for consumer finance is provided by a combination of regulated and unregulated sources. In the mortgage market, for example, funding is provided by the GSEs, which are regulated, and private investors in mortgage-backed securities, who are not. These private investors have the ability to invest their funds in any instruments. Therefore, subjecting investors to liability for violations of consumer protection requirements will simply encourage them to make alternative investments, and reduce the funds available for mortgages. Perhaps the best way to address this is to work closely with lenders and investors to develop an approach that balances reasonable accountability with continued liquidity. Placing liability on investors for activities that are beyond their ability to know, let alone police, will not work.

Thank you again for the opportunity to appear today, and I would be pleased to respond to any questions.

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HEARING BEFORE THE HOUSE FINANCIAL SERVICES COMMITTEE

ENTITLED

IMPROVING FEDERAL CONSUMER PROTECTION IN FINANCIAL SERVICES – CONSUMER AND INDUSTRY PERSPECTIVES

STATEMENT OF THE

NATIONAL ASSOCIATION OF REALTORS®
JULY 25, 2007

REALTOR® is a registered collective membership mark which may be used only by real estate professionals who are members of the NATIONAL ASSOCIATION OF REALTORS® and subscribe to its strict Code of Ethics.

EQUAL HOUSING OPPORTUNITY

The National Association of REALTORS® (NAR) is pleased to submit our views to the House Financial Services Committee for the hearing entitled, "Improving Federal Consumer Protection in Financial Services – Consumer and Industry Perspectives." We commend Chairman Frank, Representative Bachus and members of the Committee for holding this hearing on the important issue of consumer protection in the financial services sector. NAR's statement focuses on federal public policy recommendations to protect our nation's homebuyers from mortgage abuse which puts borrowers in situations of greater risk of foreclosure and other financial harm.

The National Association of REALTORS®, "The Voice for Real Estate," is America's largest trade association representing more than 1.3 million members and five commercial real estate institutes and its societies and councils. REALTORS® are involved in all aspects of the residential and commercial real estate industries and belong to one or more of some 1,400 local associations or boards, and 54 state and territory associations of REALTORS®.

REALTORS® Want to Prevent Irresponsible and Abusive Lending

Irresponsible and abusive lending practices are a major problem for our nation's communities. While responsible subprime lenders have played an important role in helping millions of consumers achieve homeownership, abusive lending occurs much too often in subprime markets. Unfortunately, some lenders have abused their role and taken advantage of vulnerable borrowers by charging extremely high interest rates and loan fees unrelated to risk, using aggressive sales tactics to steer consumers into unnecessarily expensive or inappropriate loan products, advertising "teaser" interest rates (like the 2/28 or 3/27 adjustable rate mortgage) that steeply increase after the first few years of the loan and basing their lending on artificially high appraisals. The consequence of abuses in the subprime market is higher rates of foreclosures leading to the loss of families' homes and savings and increased vacancy rates which, in turn, can cause all homes in a neighborhood to lose value.

Real estate professionals have a strong stake in preventing abusive lending because:

- Abusive lending erodes confidence in the Nation's housing system.
- Legislative and regulatory responses to lending abuses that go too far can inadvertently limit the availability of reasonable credit for prime as well as subprime borrowers in a credit-driven economy. When responses to abusive lending constrain the ability of the secondary mortgage market to provide liquidity for home finance, consumers will find it more difficult and expensive to buy a home.
- Citizens of communities, including real estate professionals, are harmed whenever abusive lending strips equity from homeowners. This is especially the case when irresponsible lenders concentrate their activities in certain neighborhoods and create a downward cycle of economic deterioration.

NAR Supports Key Responsible Lending Principles

NAR supports (a) keeping fair and affordable mortgage products available for borrowers with imperfect credit; and (b) eliminating abusive and problematic mortgages made without sufficient regard to whether the borrower can afford the loan and avoid foreclosure. Specifically, NAR supports a detailed list of improvements to the Home Ownership and Equity Protection Act of 1994(HOEPA) which were included in our statement submitted for the March 27, 2007 House Financial Services Subcommittee on Financial Institutions and Consumer Credit for the hearing entitled, "The New Regulatory Guidance on Subprime Hybrid Mortgages: Regulators and Response."

However, with 2.2 million American households projected to lose their homes and as much as $164 billion due to foreclosures in the subprime mortgage market,[1] the public policy debate has grown far beyond how to fix HOEPA. Instead, the focus is now on how to keep people in their homes and how to prevent this subprime "mess" from happening again.

NAR supports the general principle that all mortgage originators should act in "good faith and with fair dealings" in a transaction and treat all parties honestly. NAR's Code of Ethics already imposes a similar obligation on REALTORS®, who are required to treat everyone in the transaction honestly. NAR encourages legislators to use such a standard of care as a guiding principle when drafting anti-predatory lending legislation rather than using the phrase to create a new federal duty that would be too general and, therefore, too difficult to enforce.

1. Affordability. NAR supports strong underwriting standards that require all mortgage originators to verify the borrower's ability to repay the loan based on all its terms, including taxes and insurance, without having to refinance or sell the home.[2] Lenders should consider all relevant facts, including the borrower's income, credit history, future income potential, and other life circumstances. Lenders should not makes loans to borrowers that make loss of the home through sale or foreclosure likely if the borrower is unable to refinance the mortgage or sell.

- Underwriting Subprime Loans with "Teaser Rates." Some subprime loans are structured with a significant jump in monthly payments often resulting in "payment shock" for the borrower. While these mortgages may be a reasonable choice for subprime borrowers who can afford them, a majority of subprime borrowers do not have the resources to deal with, or an understanding of the unique terms and conditions of these risky mortgage products that can result in, a significant "payment shock." Therefore, lenders (including mortgage brokers) should exercise more caution when underwriting such loans to subprime borrowers to make sure the borrower is able to afford the mortgage. Examples

[1] Losing Ground: Foreclosures in the Subprime Market and Their Cost to Homeowners, Center for Responsible Lending (December 2006).
[2] The limited exceptions to this general principle would include prime borrowers with sufficient verifiable assets to handle a balloon mortgage or a significant jump in mortgage payment.

of these risky mortgage products include loans with a short-term interest "teaser" rate for the first two or three years (known as 2/28s and 3/27s), loans with an initial interest-only period, and mortgages that negatively amortize.[3]

NAR will carefully monitor the debate on underwriting standards for subprime loans. We will continue to support policies consistent with the goal of assuring that, taking into account all relevant circumstances, borrowers, who have demonstrated the financial capacity to meet their mortgage obligations, continue to have access to mortgage loans made by responsible lenders.

- Reasonable Debt-to-Income Ratio. NAR supports requiring lenders to make subprime loans that have a reasonable debt-to-income ratio. Borrowers should have enough residual income after making their monthly mortgage payment, including property taxes and insurance, to meet their needs for food, utilities, clothing, transportation, work-related expenses, and other essentials. Requiring underwriting at a fully amortizing, fully indexed rate is meaningless if the lender uses such high debt-to-income ratios that the family doesn't have enough money left each month to pay for other necessities.

- Escrow/Reserve for Payment of Taxes and Insurance. Lenders that make subprime mortgage loans should generally require that the monthly payment include an amount to be held by the mortgage servicer in an escrow/reserve/impound account for the payment of the borrower's periodic payments, such as taxes and insurance. Similar to the escrow requirement exceptions for prime loans that exist in some jurisdictions, borrowers who make at least a 20 percent downpayment should have the option to budget for these payments independently.

2. Limit Stated Income/Stated Assets Underwriting. Since mortgages underwritten based on "stated income" and/or "stated assets" (also known as "no income verification" or "no doc" loans) typically have higher rates, lenders making subprime loans should, as a general rule, underwrite loans based on verified income and assets. The main exception should be for borrowers whose incomes derive from hard-to-verify sources (such as self-employed borrowers).

3. Flexibility for Life Circumstances. NAR believes that a standard for determining a borrower's ability to repay must be flexible to accommodate borrowers with unique circumstances, such as:

- ✓ Borrowers who have demonstrated the ability to make monthly payments, over a long term, that are higher than underwriting standards would otherwise allow. Lenders should consider, for example, the borrower's history of making rent and student loan payments.

[3] Negative amortization ordinarily results if the mortgage permits a borrower to pay less than the interest on the mortgage for a limited time, in which case the difference is added to the total amount of the loan the borrower must repay.

- ✓ Borrowers with large assets but low income who, for cash management or other financial planning reasons, elect a mortgage with a monthly payment that their current income is not sufficient to cover.
- ✓ Borrowers who anticipate a jump in income or assets due to life events such as graduation, completion of professional training, paying off a student or car loans, another member of the household entering the work force, or an inheritance.

4. Anti-Mortgage Flipping Policy. NAR supports an anti-mortgage-flipping rule requiring mortgage originators making or arranging a refinance loan to verify that the new loan provides a significant benefit to the borrower.[4] The lender should consider the circumstances of the borrower, as discussed above, as well as all terms of the new loan including taxes, insurance, fees and other costs of refinancing, prepayment penalties, and the new interest rate, compared to those of the refinanced loan.

5. Bar Prepayment Penalties. NAR opposes prepayment penalties for all mortgages. Prepayment penalties often trap borrowers in loans they cannot afford by making it too expensive to refinance. If complete prohibition of prepayment penalties is not feasible, NAR supports permitting prepayment penalties for the shortest time and the lowest amount possible. For example, a borrower in a 2/28 mortgage should be able to refinance by the end of the initial two-year "teaser" rate period without having to pay a prepayment penalty.

6. Improvements for Assessing Creditworthiness. Borrowers with little or no credit history, as traditionally measured, usually have lower credit scores and must pay more every month for their mortgage than those with higher scores. NAR supports ongoing efforts to take into account consumer payment history not typically considered, such as rent, utility, telephone, and other regular payments. We urge HUD, the regulators, the GSEs, and lenders to work to strengthen these efforts. Use of alternative credit histories will be especially beneficial for low- and moderate-income first-time homebuyers and borrowers with problematic loans that need to refinance their mortgage to avoid foreclosure.

Another public policy issue associated with credit histories is the failure of furnishers to report good payment histories to the consumer reporting agencies. NAR has heard reports that many problematic subprime lenders purposefully withhold information on timely mortgage payments from the credit bureaus in order to keep their customer defined as a subprime borrower. The result is obvious – the borrowers with no positive payment histories for their subprime loan keep treading the waters of high-interest rates and expensive credit products. NAR supports requiring all institutional mortgage lenders to report payment history of borrowers on a monthly basis.

7. Mortgage Choice for Borrowers. NAR supports requiring mortgage originators to offer borrowers one or more mortgages with interest rates and other fees that appropriately reflect the borrower's credit risk. It remains the responsibility of borrowers

[4] One test often proposed is the loan must provide a "reasonable net tangible benefit" to the borrower.

to decide upon the best mortgage for their needs and circumstances, but they can only do so if they understand all the facts so they can make an informed decision. The following are suggested principles for consideration of Congress and the regulators:

- For originators who offer nontraditional mortgage products, the originator should:
  - offer all borrowers a choice of several significantly different mortgage options;
  - include at least one traditional loan product as an option for the borrower to consider, if the borrower qualifies for such a product offered by the originator; and
  - before application acceptance, disclose the maximum potential payment over the life of the loan and the date the initial payment will increase to a fully amortizing, fully indexed payment amount.

- Originators that offer FHA-insured mortgages or VA home loan guaranty mortgages should consider whether these types of mortgages should be offered as an appropriate option for a subprime borrower.

- If the originator does not offer mortgages with rates and fees appropriate for the borrower's credit risk, the originator should inform the borrower a lower interest rate may be available from another originator or that the borrower may wish to seek housing counseling. Doing so will allow the borrower an opportunity to shop elsewhere or receive counseling before proceeding. For example, a prime borrower that applies for a loan to a lender that only makes subprime loans should be advised that other, more affordable options may be available.

- For loans originated by a mortgage broker, the broker should offer mortgage options that are among the lowest-cost products appropriate for the borrower.

8. Enforcement/Remedies. NAR supports enactment of strong remedies and penalties for abusive acts by mortgage originators. Among the options for consideration are:

- Criminal penalties similar to those under RESPA.

- Civil penalties similar to those under RESPA.

- Assignee liability that balances the need to protect innocent borrowers with problematic loans against the risk that increasing the liability of innocent holders of mortgages in the secondary market could reduce the availability of mortgage credit.

- Prohibition of mandatory arbitration clauses that bar victims' access to court.

Strengthen the Independence of Appraisers

NAR believes that the independence of appraisers should be strengthened to ensure that appraisals are based on sound, fair and accurate appraisal principles and reflect a property's true value. An overwhelming number of appraisers, upwards of 90%, have experienced pressure to meet targeted values.[5] The pressure is often subtle with an appraiser being asked whether or not they can provide an appraisal to match a general price. Over 75% of appraisers report concerns that if they do not meet such requests, they will lose both the appraisal job and future business.[6] In addition, many appraisers fear that they may be black listed and/or erroneously reported to their state licensing and regulatory agency.

NAR supports the following measures to strengthen the appraisal process in federally related transactions:

1. Consumer Disclosure: NAR recommends that lenders be required to inform a borrower of the methods used to value a property to determine the amount of the mortgage loan, and borrowers have the right to receive a copy of each value estimate or value opinion. Furthermore, lenders should be required to obtain a detailed site visit appraisal for properties financed with nontraditional mortgage products.

2. Penalties for Improper Appraisal Influence: Congress should consider civil penalties against those who would coerce, intimidate or otherwise influence the appraisal process to meet a targeted value. Parties with an interest in the outcome of an appraisal should be limited to requests that the appraiser (1) consider additional, appropriate property information; (2) provide further detail, substantiation, or explanation for the value conclusion; and (3) correct errors in the appraisal report.

3. Assist States to Improve Regulation of the Appraisal Industry: While the appraisal industry is regulated at the state level, the Appraisal Subcommittee Federal Financial Institutions Examination Council sets appraisal qualifications and standards for federally related transactions. Thus, state regulatory agencies both license appraisers and certify appraisers for federally related transactions. NAR opposes expanding the authority of the Appraisal Subcommittee to issue binding regulations on states. However, NAR would support providing greater assistance to states for the purpose of strengthening regulatory and enforcement activities. For example, developing a grant program funded by an increase in the Appraisal Subcommittee roster fee would be a valuable resource for states.

4. Support Enhanced Education and Qualifications for Appraisers: The Appraisal Subcommittee, through its standards and qualifications authority, should recognize appraisers who have obtained special designations or training from professional appraisal organizations that are sponsors or affiliate sponsors of the Appraisal Foundation.[7]

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[5] National Appraisal Survey, October Research (2007).

[6] *Id.*

[7] The Appraisal Foundation, a non-profit educational organization dedicated to the advancement of professional valuation, was established in 1987 by the appraisal profession in the United States. In 1989

NAR believes that these four principles will help strengthen the appraisal process and ensure appraisal independence. These measures will provide the consumer added certitude that the appraised value of their purchase truly is a fair and accurate valuation.

Foreclosure Avoidance and Mitigation

NAR supports legislative, regulatory, and private-sector foreclosure avoidance and mitigation efforts. We urge lenders, especially lenders that have made loans without considering the ability of the borrower to make payments under the loan, to act promptly to help borrowers resolve the problem. Possible steps could include recasting the mortgage, forbearance, favorable refinancing, waiving of prepayment penalties, and other appropriate tools. Prompt action will almost always be in the best interests of the lender, as well.

NAR also supports increased funding for programs that provide financial assistance, counseling, and consumer education to borrowers to help them avoid foreclosure or minimize its impact. We also believe that Congress and the regulators should examine alleged abuses by mortgage servicers, some of whom are engaging in predatory servicing by imposing unjustified high fees on borrowers. These abusive practices can contribute to, or even cause, delinquencies and foreclosures.

Conclusion

Irresponsible and abusive lending can be a disaster not only for the borrower and his or her family, but for the community as well. Problematic loans are often made in concentrated areas and are more likely to result in foreclosures. High foreclosures of single-family homes are a serious threat to neighborhood stability and community well-being. Foreclosures can lead to high vacancy rates which, in turn, can devastate the strength and stability of communities.

REALTORS® help families achieve the dream of homeownership. The National Association of REALTORS® supports responsible lending, based on sound independent appraisals, with increased consumer protections to ensure that the "dream" our members help fulfill does not turn into a family's worst nightmare. NAR stands ready to work with Congress on the important issue of risky mortgage products and we are happy to make available to your constituents our "How to Avoid Predatory Lending" consumer education brochure and our "Learn How to Avoid Foreclosure and Keep Your Home" brochure.[8] Thank you.

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the U.S. Congress gave the organization specific authority relating to real property appraiser qualifications and appraisal standards.

[8] NAR's consumer education brochures are available for downloading at: www.REALTOR.org/subprime

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