PERSPECTIVES ON THE CONSUMER FINANCIAL PROTECTION AGENCY

HEARING

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

FIRST SESSION

SEPTEMBER 30, 2009

Printed for the use of the Committee on Financial Services

Serial No. 111–81

U.S. GOVERNMENT PRINTING OFFICE

54–872 PDF WASHINGTON : 2010

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

HOUSE COMMITTEE ON FINANCIAL SERVICES

BARNEY FRANK, Massachusetts, *Chairman*

PAUL E. KANJORSKI, Pennsylvania
MAXINE WATERS, California
CAROLYN B. MALONEY, New York
LUIS V. GUTIERREZ, Illinois
NYDIA M. VELÁZQUEZ, New York
MELVIN L. WATT, North Carolina
GARY L. ACKERMAN, New York
BRAD SHERMAN, California
GREGORY W. MEEKS, New York
DENNIS MOORE, Kansas
MICHAEL E. CAPUANO, Massachusetts
RUBÉN HINOJOSA, Texas
WM. LACY CLAY, Missouri
CAROLYN MCCARTHY, New York
JOE BACA, California
STEPHEN F. LYNCH, Massachusetts
BRAD MILLER, North Carolina
DAVID SCOTT, Georgia
AL GREEN, Texas
EMANUEL CLEAVER, Missouri
MELISSA L. BEAN, Illinois
GWEN MOORE, Wisconsin
PAUL W. HODES, New Hampshire
KEITH ELLISON, Minnesota
RON KLEIN, Florida
CHARLES A. WILSON, Ohio
ED PERLMUTTER, Colorado
JOE DONNELLY, Indiana
BILL FOSTER, Illinois
ANDRÉ CARSON, Indiana
JACKIE SPEIER, California
TRAVIS CHILDERS, Mississippi
WALT MINNICK, Idaho
JOHN ADLER, New Jersey
MARY JO KILROY, Ohio
STEVE DRIEHAUS, Ohio
SUZANNE KOSMAS, Florida
ALAN GRAYSON, Florida
JIM HIMES, Connecticut
GARY PETERS, Michigan
DAN MAFFEI, New York

SPENCER BACHUS, Alabama
MICHAEL N. CASTLE, Delaware
PETER T. KING, New York
EDWARD R. ROYCE, California
FRANK D. LUCAS, Oklahoma
RON PAUL, Texas
DONALD A. MANZULLO, Illinois
WALTER B. JONES, JR., North Carolina
JUDY BIGGERT, Illinois
GARY G. MILLER, California
SHELLEY MOORE CAPITO, West Virginia
JEB HENSARLING, Texas
SCOTT GARRETT, New Jersey
J. GRESHAM BARRETT, South Carolina
JIM GERLACH, Pennsylvania
RANDY NEUGEBAUER, Texas
TOM PRICE, Georgia
PATRICK T. MCHENRY, North Carolina
JOHN CAMPBELL, California
ADAM PUTNAM, Florida
MICHELE BACHMANN, Minnesota
KENNY MARCHANT, Texas
THADDEUS G. McCOTTER, Michigan
KEVIN McCARTHY, California
BILL POSEY, Florida
LYNN JENKINS, Kansas
CHRISTOPHER LEE, New York
ERIK PAULSEN, Minnesota
LEONARD LANCE, New Jersey

JEANNE M. ROSLANOWICK, *Staff Director and Chief Counsel*

CONTENTS

PERSPECTIVES ON THE CONSUMER FINANCIAL PROTECTION AGENCY

Wednesday, September 30, 2009

U.S. House of Representatives,
Committee on Financial Services,
Washington, D.C.

The committee met, pursuant to notice, at 10:07 a.m., in room 2128, Rayburn House Office Building, Hon. Barney Frank [chairman of the committee] presiding.

Members present: Representatives Frank, Waters, Gutierrez, Watt, Moore of Kansas, Hinojosa, Clay, Baca, Miller of North Carolina, Scott, Green, Cleaver, Bean, Ellison, Wilson, Perlmutter, Donnelly, Carson, Speier, Minnick, Adler, Driehaus, Kosmas, Himes, Maffei; Bachus, Castle, Royce, Lucas, Manzullo, Biggert, Capito, Hensarling, Garrett, McHenry, Campbell, Marchant, McCarthy of California, Posey, Jenkins, Lee, Paulsen, and Lance.

The Chairman. The hearing will come to order. I want first to welcome some visiting Parliamentarians. We have members of the Parliament we are particularly glad to welcome from Kosovo and Mongolia, two nations that were not allowed to have elected free Parliaments for some time. We are delighted that this progress of self-governance has reached them, and we welcome them as our guests. Our colleague, the gentleman from North Carolina, Mr. Price, Representative David Price, who works on behalf of the House Democracy Partnership, has sponsored them.

Our hearing today is open. We are dealing with the Consumer Financial Protection Agency and we will have a couple of panels. This is a hearing on a particular legislative draft. It is, we will just say preliminarily, the third iteration. The Administration had a proposal. I, as a courtesy to them, introduced their proposal with some changes, but not a lot. Since that time, we have had the benefit of a lot of conversation.

Today's legislation reflects further conversation, but it is the starting point, not the endpoint of a markup that will occur the week after next. We will be having a hearing, is it tomorrow, on derivatives? Is that the hearing? Yes. We will have hearings this week on particular pieces of legislation.

The history was the Administration made some proposals. We on our side modified them after a lot of conversation, in the case of derivatives, conversation with the Agriculture Committee, which shares jurisdiction with us.

In the week after next, after these two hearings, we will be proceeding to markups. We did mark-up and the House passed the compensation piece of our approach here.

So for those who were wondering what was happening, two very significant pieces of this will begin the markup process on the second week. As to Floor time, the leadership of the House is still deciding the form in which these will go to the Floor on the timing, but we will begin when we get the next markup schedule and we will proceed. And we will have finished marking-up, I believe, certainly by early November, probably late October, because we are seriously into the markup phase.

Now, we will begin the hearing today on the Consumer Financial Protection Agency. This was a proposal that the Administration made that I greatly welcome. Consumer protection has been in the hands of the Federal bank regulators, and I think it is fair to say that no calluses will be found on the hands of those in the Federal bank regulatory agencies who had consumer responsibilities, because there is no evidence of any particular hard work. The single biggest chunk of that authority is with the Federal Reserve.

I am somewhat interested to see that many members on both sides, especially on the Republican side, recently have become very critical of the Federal Reserve. There is a consensus that we have to restrict the Federal Reserve's power under section 13(3). There is a consensus that we will increase auditing over the Federal Reserve. But there appears to be an exception on the part of some of my colleagues.

The Federal Reserve's lackadaisical record in consumer protection does not appear to have engaged the same degree of skepticism. Thus, we hear a lot of calls for removing power from the Federal Reserve. But when it comes to consumer protection, I think they have demonstrably been at their weakest. I think they have done a good job in some other areas. Somehow that gets left out.

If this bill passes, and I hope it will, it will take power from the Federal Reserve and take funding from the Federal Reserve, because we do not think the banks, which have to contribute in assessments to various agencies, should be charged extra for this. And, in fact, a substantial part of the funding for this agency will come from the Federal Reserve. The Federal Reserve will be ceding a lot of power that is not used very much, and funding will come with it.

So, again, I would urge people who want to be appropriately careful in the evaluation of the Federal Reserve not to leave out an area where the Federal Reserve seems to have become lazy. Let me just say that it is true that recently the Federal Reserve has done some consumer activity. In every case—and I mean this quite literally—where the Federal Reserve has in recent years done anything for consumer protection, it has done so after this committee in particular initiated action.

There was a long period when the Federal Reserve did virtually nothing. In 1994, Congress gave the Federal Reserve, under the Home Ownership and Equity Protection Act, the authority to regulate mortgages of all kinds, whether they were in the banking system or not. Mr. Greenspan consciously and deliberately refused to use that. The Federal Reserve had the power to promulgate a code of unfair and deceptive practices for banks. In fact, in 2004, when the control of the currency—although it was in the Bush Administration, it was a Clinton Administration holdover appointee, Mr.

Hawk, promulgated a very sweeping preemption that knocked State enforcement entities out, and it was criticized largely at the time by, for example, Sue Kelly, who was then the Republican Chair of the Oversight Committee. One of the problems was that the Federal regulators had nothing to put in place of the State consumer protections they had abolished.

And I asked the new Comptroller of the Currency, Mr. Dugan, what he was going to do about it. He said, I have this problem; the Federal Reserve has the power to promulgate the unfair and deceptive practices code, and they haven't done it and won't do it. In fact, a Governor, Ned Gramlich, one of the few consumer-oriented officials at the Fed over the years, tried very hard to get Mr. Greenspan to use that power, to use the power under the Home ownership and Equity Protection Act, to use that power under the statutes giving him those powers.

Now, the Federal Reserve has since acted only after this committee, particularly after 2007—frankly, when the Majority changed hands—that we took action. The Federal Reserve took action on mortgages after this committee acted. The Federal Reserve took action on credit cards after this committee acted.

Under the leadership—and let me say at this point, I want to express the great sorrow and condolences for a member of this committee, to one of our most active members, the gentlewoman from New York, Mrs. Maloney, who suffered the tragic loss of her husband. And to Carolyn Maloney, as she grieves, we should just note that it was her initiative on credit cards and on overdrafts in both of those cases that led to Federal action. So I think the record is very clear and I don't say this—this is not a personality defect in the regulators, although in Mr. Greenspan's case, I think it was, as he has acknowledged, excessive by the ideological rigidity. It is the case that if your primary responsibility is the safety and soundness of the banking system in administering banks and providing the assurance that they live up to the fundamental economic statutes, then consumer protection suffers very, very deeply. And this bill would remedy that.

The gentleman from Alabama is now recognized for 3 minutes.

Mr. BACHUS. I thank the chairman. And let me start by expressing our heartfelt condolences of all of the Republican members to Mrs. Maloney on the passing of her husband, Clifton. Our thoughts and our prayers are with her and her family during this difficult time.

And I would also like to join the chairman in expressing our greetings to our colleagues from Mongolia and Kosovo. I am glad that they are here. Welcome.

The CHAIRMAN. If the gentleman would yield briefly. Stop the clock, please. And we will start it over for the gentleman so that he has his full 3 minutes. I would just say that I apologize to our colleagues from Kosovo and Mongolia. I assume that their English is much better than our Serbo-Croatian and Mongolian. But I do have to say it is unfair for them to hear as their first two spokespeople of the American Congress, myself and the gentleman from Alabama. Let me just assure you, your ability to understand will go up from here, I say on behalf of myself and my colleague.

The gentleman is now recognized again for 3 minutes.

Mr. BACHUS. Yes, we do have some English speakers who will be speaking later on.

I thank you for having today's hearing, Mr. Chairman, and I look forward to hearing the perspectives from our witnesses on the merits or possible demerits of creating the Consumer Financial Protection Agency. And I think we can do a better job of protecting the consumer. I think we all agree on that and we should.

However, the Administration's proposal, I think, is conceptually flawed. Since the Treasury Department submitted the legislative language to Congress 3 months ago, we have heard from a host of community bankers, credit unions, accountants, small business owners, and Federal financial regulators that this, what could prove to be a massive new regulatory bureaucracy, will create more confusion for our consumers, more government spending, but, more importantly, less innovation and less creation of credit and less consumer protection.

I know some of our witnesses today have said some of that credit has been a bad thing, but I think ultimately that choice should be left to the individual as long as it is under acceptable terms.

In deference to this widespread public and official opposition, I do commend Chairman Frank for releasing, last Friday, a new working draft that attempts to narrow the scope of an overly broad proposal by the Obama Administration. However, I think that what his proposal does is basically tinkering around the margins of a fundamentally flawed proposal, and it is not a solution. What is needed is an entirely different approach.

The CHAIRMAN. That is 3 minutes. If the gentleman wants more time, we will—

Mr. BACHUS. No, that is fine.

The CHAIRMAN. It was only 2 minutes? I am sorry. It should have been 3 minutes. I apologize. I ask that we start again for the gentleman with 3 minutes. I apologize. The gentleman has an additional minute.

Mr. BACHUS. Thank you. Fortunately, there are a number of alternatives that would achieve the goals of empowering consumers and combating abusive practices without limiting credit, without imposing excessive compliance and litigation costs on small businesses, without creating a new government bureaucracy, and without undermining safety and soundness regulation.

For example, the House Republicans have introduced, I think, a strong proposal on consumer protection through regulatory consolidation, and we would like the witnesses to comment on our proposal if they have read it.

I think this is absolutely the wrong time to create a new government agency empowered not only to ration credit, but, most importantly—and I don't know that anyone has paid a lot of attention to this, other than some of our colleagues and some of the regulators—it gives this agency the power to design financial products offered to consumers, and that is a striking expansion of government's role.

Every day we hear about struggling families, families with good credit histories who are denied credit so that they can own a home. And I think this only makes things worse.

Thank you, Mr. Chairman.

The CHAIRMAN. The gentleman from North Carolina, Mr. Watt, for 1 minute.

Mr. WATT. Thank you, Mr. Chairman. I just—I doubt that anybody will get to the end of this process and say that we have not had enough discussions or hearings about any aspect of this—these proposals that the Administration has sent over.

There are two parts to this. The regulated entities, the ones that say they have had consumer regulation in the past, whom we haven't seen much of, are concerned that their existing regulators ought to continue to have that authority. But there is a whole other set of unregulated entities out there that we need to make sure that the Consumer Financial Protection Agency is set up to write rules for, examine, enforce rules, in addition to figuring out what the relationship should be between this new CFPA and the existing regulators.

So I don't want to lose sight of that and hope we can bring some clarity to that as we go forward.

The CHAIRMAN. The gentleman from Delaware, for 1 minute.

Mr. CASTLE. Thank you, Mr. Chairman.

I believe consumers should be protected from deceptive practices with regard to financial products. Not only should institutions provide adequate disclosures, but consumers should also have the basic financial literacy to understand the contracts into which they enter.

For these reasons, I believe consumer protection reform must be enacted. However, I do have reservations about the Consumer Financial Protection Agency, as proposed.

First, a majority of the subprime mortgages that contributed to the financial crisis originated outside the traditional banking sector and were virtually unregulated. As currently written, does CFPA focus its resources and scope enough on this problem area?

Second, should we provide existing regulators with checks and balances over the CFPA director in the rulemaking process if safety and soundness concerns are raised?

Finally, if part of the goal of this bill is to streamline consumer protection laws, why are we eliminating Federal preemption, thereby allowing States to go beyond Federal law to create a patchwork or further gaps in consumer protection rules.

I hope today's hearing will provide further insight on these issues. And I yield back the balance of my time.

The CHAIRMAN. The gentleman from North Carolina, Mr. Miller, for 2 minutes. I am sorry, there was a mistake. The gentleman from Texas, Mr. Green, for 1 minute.

Mr. GREEN. Thank you, Mr. Chairman.

Mr. Chairman, I am in support of a Consumer Financial Protection Agency. I think that this is the right time to do it. In fact, my suspicion is that if we don't do it now, we may not find a right time to do it. I think that there are many issues that have to be delved into, and I look forward to it.

I think the chairman has already demonstrated that he is sensitive to a good number of issues. We are no longer having the plain vanilla requirement. There are entities that have been exempted, and I think that by working through the process, we can get to safety and soundness, as well as consumer protection. And they are not inconsistent with each other.

I thank you for the time, Mr. Chairman, and I yield back.

The CHAIRMAN. The gentleman from California, Mr. Royce.

Mr. ROYCE. Thank you, Mr. Chairman.

Regulators have discussed at length the problems with separating safety and soundness from consumer protection regulation. They have talked about the problems that are going to arise from this model, even saying it will weaken protection for consumers.

We also know this proposed consumer agency will increase costs. Last week, the regulators acknowledged that the ultimate cost for funding this agency will fall on consumers. They will see the cost of credit go up and the availability of credit go down. But the failure of this proposal to adequately preempt State laws is equally disconcerting.

Our architects of this Republic added the commerce clause to the Constitution precisely to prevent a fragmented economy. They envisioned one national market, not a market where local and State governments with conflicting State laws could strangle free trade among the States. We have seen the ill effects of this type of patchwork regulatory system in our insurance market. I think it would be a grave mistake to move forward with that failed model for the rest of the financial services sector. I yield back, Mr. Chairman.

The CHAIRMAN. The gentleman from Texas for 2 minutes, Mr. Hensarling.

Mr. HENSARLING. Thank you, Mr. Chairman.

As I read the bill summary of the new CFPA law, it reminds me of a title of one of my favorite Led Zeppelin works, "The Song Remains the Same."

If in doubt, read the bill. Section 131(b)(1), 136(a)(1) shows that we still have an agency that can outlaw products and practices that are determined to be "unfair," "abusive," or do not substitute "fair dealing" totally in their subjective opinion.

Are subprime loans inherently abusive? Tell that to the millions of Americans who have homeownership only because of a subprime loan. Are payday loans inherently unfair? Tell that to the millions of Americans who use them to avoid an eviction notice or prevent the utilities from being shut off.

What is different? Now a single unelected bureaucrat, as opposed to five unelected bureaucrats, will have the power to decide whether the Rodriguez family in Mesquite, Texas, can obtain a mortgage; whether the King family of Athens, Texas, can get a car loan; or whether the Shane family of Kaufman, Texas, can even get a credit card to buy their groceries.

For those who persist in wanting to, by government fiat, restrict credit opportunities in the midst of a national credit crunch, when that particularly impacts low- and middle-income families, the bill is well-designed to achieve those goals.

What else remains the same? Product approval can still trump safety and soundness. Clearly, taxpayers are left out of the equation. Preemption remains—multiple standards that add cost and uncertainty. Taxing the agency—it still retains the power to essentially tax the industry, taxes that are passed on to consumers in the form of higher fees and less credit. Plain vanilla goes from mandatory to highly, highly suggested.

The bill supposedly is about consumer protection. The best way that we can protect consumers is with competitive markets that encourage product innovations, give customers choices, and prevent fraud and deception. Thank you, Mr. Chairman.

The CHAIRMAN. The gentleman from Kansas, Mr. Moore, for 2 minutes.

Mr. MOORE OF KANSAS. Thank you, Mr. Chairman.

Last year's financial crisis exposed an out-of-date regulatory structure in need of a complete overhaul. The proposed Consumer Financial Protection Agency is a key component of the proposal to create stronger oversight of our financial system. I commend the chairman for the improvements he made that revised the draft bill released last week.

In today's hearing, I hope we will explore some of the more difficult questions on CFPA: one, transferring consumer protection enforcement away from bank regulators; and two, the proper role of States' enforcement of policymaking power in relation to the new Federal agency.

I welcome the chairman's ideas on coordinated exams and a dispute resolution mechanism. I hope these and other ideas generate a discussion of not if, but how best to implement the CFPA to fully protect consumers.

And I yield back my time. Thank you, sir.

The CHAIRMAN. The gentleman from New Jersey, Mr. Garrett, for 2 minutes.

Mr. GARRETT. Thank you, Mr. Chairman, and the ranking member, for holding this important hearing today. Last week, the chairman circulated a new discussion draft of legislation to create a whole new Federal agency to oversee all individuals in their financial decisions.

Now, there are some new provisions in this draft that seek to clarify what products and what agencies and entities are covered. Most changes really are pretty much cosmetic and little more than attempts to make it a little bit more politically palatable for some of the concerned Members of the other party to pass it.

This legislation still separates consumer protection from safety and soundness regulation, much like Fannie Mae and Freddie Mac did. And we all know how that turned out. This legislation still creates an uber regulator with essentially no bounds or limits on authority. This legislation still limits consumer choices and reduces consumer credit. And this legislation still does absolutely nothing to address the problems that caused our financial collapse. So this legislation really hasn't changed that much, and my opinion of it really hasn't changed that much either.

It is simply another example of something taxpayers can't afford, simply another example of government overreach, simply another example of increasing the power of the Federal bureaucrats at the expense of the individuals. It is also really another example of the Federal Reserve being held out as a personal piggybank, if you will, of the current powers that be in Washington, D.C.

So maybe to some, the idea of creating a whole new entity in the Federal bureaucracy, with dubious benefits to society, sounds like a political winner, but it is clear that the more people concentrate on the consequences of that idea, the less likely it will be.

We really must not push through a bad idea that will limit consumer choice and credit availability and encourage and increase costly and unnecessary litigation and potentially decrease the safety and soundness of our very basic banking system in this country.

Thank you, Mr. Chairman. With that, I yield back.

The CHAIRMAN. The gentleman from Minnesota, Mr. Ellison.

Mr. ELLISON. Thank you, Mr. Chairman.

One of the most important causes of the financial crisis was the complete and utter failure of our system of consumer financial protection. The most abusive and predatory lenders were not federally regulated, while regulation was overly lax for banks and other institutions that were covered.

To address this problem, we need a new agency dedicated to consumer financial protection, a Consumer Financial Protection Agency. Of course there are some who would like to keep the same regulators on the job and thereby duct-tape together the shards of a broken system.

Anyone who wants to take this bankrupt approach should read the Washington Post article from this last Sunday, which I will submit for the record, that discussed the Fed's failures to act on consumer protection.

Those failures were so great that even former Fed Chairman Alan Greenspan has backtracked and said the Administration's proposal is probably the "right decision" regarding a Consumer Financial Protection Agency. Of course, that initial proposal was not perfect, but we will continue to work on it over the weeks ahead. I yield back. Thank you.

The CHAIRMAN. The gentleman from Alabama is recognized for the final minute.

Mr. BACHUS. I thank the chairman.

Every day we hear about struggling families, families with good credit histories who are denied credit, so they can own a home, buy a car, start a business, or send their children to college.

We can protect those consumers and we can do that without limiting their options for borrowing, investing, and saving, as this proposal would do. We can also do that without putting the government in the job of designing financial products, something that was never intended. We can better protect consumers without imposing new taxes and fees on their financial transactions, something the Administration has proposed without increasing the cost of borrowing or creating a new bureaucracy.

And finally, Republicans and Democrats can work together to find practical solutions that will allow our markets and our financial institutions to function effectively, and, at the same time, protect consumers.

Thank you, Mr. Chairman.

The CHAIRMAN. We will now begin with the hearing. All witnesses and members will be, if there is no objection, given the right to insert into the record any additional materials. So no one needs to ask for any special permission. The record will be open.

And in particular, since we are under the 5-minute rule, I would advise openness, as you may be given questions which the members will ask you to answer in writing. I would ask you to give priority to answering those in writing so that we can incorporate any such answers into the hearing record.

We will begin with Hilary Shelton, who is the director of the National Association for the Advancement of Colored People, the NAACP.

STATEMENT OF HILARY O. SHELTON, DIRECTOR, WASHINGTON BUREAU, NATIONAL ASSOCIATION FOR THE ADVANCEMENT OF COLORED PEOPLE (NAACP)

Mr. SHELTON. Thank you, and good morning. Thank you, Mr. Chairman, Ranking Member Bachus, and members of the Committee on Financial Services for inviting us here today. I appreciate the opportunity to share with you the views of the NAACP on the creation of a Consumer Financial Protection Agency, or CFPA.

I would also like to begin by thanking you, Chairman Frank, for all you have done, and continue to do, to help all Americans obtain access to capital and financial security. In fact, NAACP members from across the Nation who were fortunate enough to hear your presentation at our Centennial Convention in New York this summer are still talking about the need for this new agency and its promise to our communities.

The NAACP is very supportive of the creation of a strong and effective CFPA with the protection of civil rights and a directive that it seek to eliminate discrimination as a core part of its mandate. For too long, racial and ethnic minorities, the elderly, and others have been targeted by unscrupulous lenders and underserved by traditional financial institutions.

The result of this lack of standard rule and the strict enforcement of the rules that we do have has been the financial stagnation, and, in too many cases, the economic ruin of people's lives, families, and entire communities. When they have been engaged, too many regulators have spent too much time in recent years asking what is the effect on the financial industry, without asking what is the effect on the consumer?

One result of these misplaced priorities, as we have seen, has been an almost complete collapse of not only our Nation's economy, but the near ruination of the global financial system as well. Examples of financial abuses, targeting racial and ethnic minorities abound, especially in the mortgage arena, where predatory lenders consistently target certain groups and communities, and by abusive credit card companies and exploitive payday lenders.

In my written testimony, I provided the committee with numerous examples of studies that conclusively show not only a targeting of certain groups by financial services, but also the disparate impact this unscrupulous, wealth-stripping behavior has had on individuals, families, and, indeed, whole communities.

In the interest of time, I will not go into detail here. Suffice it to say that the evidence that racial and ethnic minorities have been targeted by abusive financial services is strong and conclusive, and their eradication is a top civil rights issue of our day.

As envisioned, the CFPA would provide the government with the tools necessary to help all consumers investigate and be treated fairly by what is often a confusing and potentially ruinous environment. It would support, if not require, regulators to become more protective of consumers, and it would make civil rights protections more a key element in the regulation and oversight of financial services.

It is also because of the systemic discriminatory and abusive lending practices that we were pleased to see a strong support of our provisions in the latest draft of CPA's legislation that creates an Office of Fair Lending and Equal Opportunity and makes the fight against discrimination part of the mandate of the new agency.

These provisions will go a long way towards putting some teeth into the laws that are already on the books and to protecting consumers, all consumers, as they attempt to navigate our Nation's financial services.

One area where the NAACP would like to see the current CFPA proposal strengthened is that we would like to see regulation of the Community Reinvestment Act, the CRA, fall under the CFPA's jurisdiction. We need to renew, reinvigorate, modernize, and expand CRA, and I appreciate the comments of the chairman last week when he said that he too is serious about updating this important law.

I would suggest that perhaps in the course of reauthorizing CRA, this committee consider putting authority of this important law under the newly created and robust CFPA.

In order to fully address the needs of local communities, many of which are represented by the NAACP, the CFPA should be able to review and enforce lending laws at that level.

Mr. Chairman, it is our belief that a strong CFPA will go a long way towards addressing the very real needs of enforcement and regulation in the financial services arena.

However, let me make it clear that we have no illusions that this new agency will fully address all of the needs and shortcomings that continue to plague our communities and, indeed, our Nation. We still need strong laws to address many of the problems that allow unscrupulous lenders to continue to operate.

Specifically, the NAACP will continue to fight for aggressive antipredatory lending laws, as well as curbs on abusive payday loans, and real assistance for homeowners facing foreclosure.

In that vein, I look forward to continuing to work with you, Mr. Chairman, as well as all the other members of this committee, to enact strong legislation to help all Americans gain the American dream of economic security.

Thank you very much. And I look forward to your questions.

[The prepared statement of Mr. Shelton can be found on page 147 of the appendix.]

The CHAIRMAN. Next, Michael Calhoun, president and chief operating officer of the Center for Responsible Lending.

STATEMENT OF MICHAEL CALHOUN, PRESIDENT AND CHIEF OPERATING OFFICER, CENTER FOR RESPONSIBLE LENDING

Mr. CALHOUN. Chairman Frank, Ranking Member Bachus, and members of the committee, thank you for your work over the last year as you have dealt with one of the largest financial crises our country has ever faced. Most of the witnesses today, from both panels, acknowledge that poor oversight and weak consumer protection were major causes of our present crisis.

The question is how to improve them. And an appropriate test is what would have happened over the last 10 years if proposed reforms had been in place. The CFPA bill that is before this committee would have prevented the worst of what we are experiencing now. However, some of the proposals to weaken it would have exacerbated the last crisis and would make it likely that we will repeat these mistakes in the future. In other words, done wrong, we can make things even worse for consumers and the whole economy.

There are four critical things we have to get right. First, we need to create an independent agency. As we have learned, if financial products are not sound, the markets built on them cannot be sound.

Second, we need to cover products, not labels. We need to make sure to prevent the gaps and unlevel rules that contributed so much to the current crisis.

Third, we need to be careful not to insulate abusive practices with preemption. This was done over recent years with mortgages, credit cards, and debit cards, all with disastrous results.

And fourth, we need to provide effective enforcement. There has been case after case in recent years where, when standards were enacted but without enforcement, they created an illusion of protection that was worse and more dangerous than none at all.

I was struck, Mr. Chairman, by your comments about the impact of Mr. Greenspan's approach at the Fed to not enact consumer protections. That takes me to what is the core issue I want to ask you to focus on, and that is the preemption that has been raised. Imagine what would have been the case if Mr. Greenspan would have had not only the authority to not act, but also the authority to wipe out all State protections and to bar all States from stepping in to protect the abuses that we saw.

We should remember, it was the States who led the way in addressing the ability to repay, finding loans that were being made repeatedly to customers who had no ability to stay in those homes. It was the States who addressed broker kickbacks where the brokers received payments to steer people to higher-priced loans, even though in 2001, HUD took action to actually protect those kickbacks. So I think it is also important to know the details of the preemption in this bill.

The sweeping scope of present financial preemption is a recent and isolated phenomenon, as the chairman mentioned. In 2004, the Federal banking agencies took preemption to a whole new level as they competed with each other to be attractive to the institutions they regulated, who they referred to in official documents as their customers.

The bill makes a return to preemption as it was 5 years ago and it relies on you, the Congress, not agencies, to prescribe preemption. States still cannot set usury limits for mortgage loans, credit cards, or other credit under this bill as it currently reads. There are, however, proposals to greatly increase preemption beyond current levels and make all rules of the CFPA preemptive. This would wipe out State consumer protection laws and a wide array of transactions, and weaken overall consumer protection.

If that had been in place over the last year, we would have faced an even greater disaster. We would have seen, again, no opportunity for States to detect problems and test solutions, and no enforcements of State civil rights laws.

Finally, we need to make sure there is effective enforcement for this bill. Looking at the overdraft area, the Fed acknowledged, in 2001 and 2004, major problems with overdraft loans. It issued best practices that said you should not be applying these to debit cards. You should protect people from outrageous fees or from repeated fees.

One bank submitted a request for approval of their overdraft program. The OCC refused to give that approval and the bank asked, "Are you going to enforce these guidelines against us?" And the OCC said, "We will only enforce those things that are law. These are not law. Do what you will."

Fast forward, 8 years later, $80 billion of overdraft fees later. For the American public, we now have proposals that the Fed may act.

We look forward to working with the committee to establish an effective CFPA that is enforceable and efficient. Thank you, Mr. Chairman.

[The prepared statement of Mr. Calhoun can be found on page 76 of the appendix.]

The CHAIRMAN. Next, Mr. David John, who is the senior research fellow at the Thomas A. Roe Institute for Economic Policy Studies at the Heritage Foundation.

STATEMENT OF DAVID C. JOHN, SENIOR RESEARCH FELLOW, THE HERITAGE FOUNDATION

Mr. JOHN. Thank you for having me. And it is a delight to be a part of this panel. I think we all agree on the problem. The area that I am going to disagree is the solution. I thoroughly agree that consumer regulation has been faulty and has been a cause of some, if not all, of the disruptions that we faced in the last year. I also agree that the various financial regulators have not given the consumer regulation the emphasis it needs.

However, I believe that a far better approach would be to coordinate the consumer activities of existing State and Federal and financial regulators by creating a coordinating council designed to promote equal standards of consumer protection, using agencies' existing powers and perhaps additional powers passed by the States.

Critics of the current regulatory system justified the need for a CFPA by citing instances where different agencies apply different regulatory standards to similar products, or fail to apply any standards at all. And they point to unregulated entities or products that took advantage of consumers.

But these are problems that can just as easily be solved by a coordinating committee as they can by anything else. The council, which would be actually similar to your Consumer Financial Protection Oversight Board, in your most recent draft, would consist of one representative from each Federal agency, regulatory agency, and elected representatives from the councils of the various types of the State regulators.

In addition, it would have a fully participating chairman appointed by the President, a board of outside experts who would monitor consumer regulatory activities and issue reports on that. Staffing would come from within the agencies, except for a very small support staff for the chairman and advisors.

The inclusion of State regulators the council would make coverage even more universal than it would be under the proposed CFPA. Standards agreed to by the council would also apply to insurance companies, which are exempted from the CFPA approach, and as States move to license in the unregulated mortgage brokers and others who are often responsible for abuses in mortgage lending. Instead of a one-size-fits-all policy dictated by Washington, States would continue to have some flexibility in implementing regulations, subject to the oversight of the council and its expert advisors who would issue public statements and studies to make sure that consumers and legislators were aware of States with poor coverage or enforcement. Likewise, poor Federal agencies.

The failure to act could make loans from State-regulated entities in those States that failed to work properly ineligible for securitization or sale to investors in other States. This approach would preserve State regulation of those entities that are currently State-regulated, rather than attempting to federalize all aspects of consumer financial relationships.

The council would also include both the SEC and the CFTC, thus closing gaps in the CFPA, as proposed, including the regulation of retirement savings accounts, which are also becoming ever more complex and difficult for consumers to understand.

The council would be responsible for developing broad standards for consumer regulation, while leaving the writing and enforcement of specific regulations to those agencies with responsibilities in that area. This ensures that the regulations would take into consideration the operational realities of regulated institutions as well as any special characteristics of regional markets.

Another key advantage to the council is that by using existing regulators in their current authority, the regulators' individual efforts can be better monitored than the results of a proposed vast new bureaucracy with vague and almost unlimited powers.

Through proper congressional oversight and reports from the new council's expert advisors, Congress and State legislators could better pinpoint successes and failures than it could by attempting to keep track of the efforts of one massive agency.

I have proposed—there is a footnote on page 6 that a mechanism similar to the Uniform Commercial Code be used to recommend policies and specific regulatory and legal language to the individual States to ensure that the proper standards are kept and met. I believe that this approach would have a much better opportunity to solve some of the problems that have been raised here, and will be raised here later, than a proposed new agency. Thank you.

[The prepared statement of Mr. John can be found on page 123 of the appendix.]

The CHAIRMAN. Next, we will hear from Janice Bowdler, who is the senior policy analyst at the National Council of La Raza.

STATEMENT OF JANIS BOWDLER, DEPUTY DIRECTOR, WEALTH-BUILDING POLICY PROJECT, NATIONAL COUNCIL OF LA RAZA (NCLR)

Ms. BOWDLER. Good morning. Thank you. I would like to thank Chairman Frank and Ranking Member Bachus for inviting NCLR to share perspective on this issue. Latino families have been particularly hard hit by the implosion of our credit markets. Lax oversight allowed deceptive practices to run rampant, driving Latino families into risky products and ultimately cyclical debt. In fact, Federal regulators routinely missed opportunities to correct the worst practices.

Congress must plug holes in a broken financial system that allowed household wealth to evaporate and debt to skyrocket.

Today, I will describe the chief ways our current regulatory system falls short, and I will follow with a few comments on the CFPA. Most Americans share a fundamental goal of achieving economic security they can share with their children. To do so, they rely on financial products—mortgages, credit cards, car loans, insurance, and retirement accounts. Unfortunately, market forces have created real barriers to accessing the most favorable products, even when families are well-qualified.

Subprime creditors frequently targeted minority communities as fertile ground for expansion. Subprime lending often served as a replacement of prime credit, rather than a complement. With much of the damage coming at the hands of underregulated entities, gaming of the system became widespread. Despite the evidence, Federal regulators failed to act.

This inaction hurt the Latino community in three distinct ways. Access to prime products was restricted, even when borrowers had good credit and high incomes. This most often occurred because short-term profits were prioritized over long-term gains. Lenders actually steered borrowers into costly and risky loans, because that is what earned the highest profits. Disparate impact trends were not acted upon.

Numerous reports have documented this trend. In fact, a study conducted by HUD in 2000 found that high-income African Americans, living in predominantly black neighborhoods, were 3 times more likely to receive subprime home loans than low-income white borrowers. Regulators failed to act, even when Federal reports made the case.

And shopping for credit is nearly impossible. Financial products have become increasingly complex, and many consumers lack reliable information. Many chose to pay a broker to help them shop. Meanwhile, those brokers have little or no legal or ethical obligation to actually work on behalf of the borrower. Regulators dragged their feet on reforms that could have improved shopping opportunities.

If our goal is to truly avoid the bad outcomes in the future, the high rates of foreclosure and household debt, little or no savings and the erosion of wealth, we have to change the Federal oversight system. Lawmakers must ensure that borrowers have the opportunity to bank and borrow at fair and affordable terms.

We need greater accountability and the ability to spot damaging trends before they escalate. Some have argued that it is the borrower's responsibility to look out for deception. However, it is unreasonable to expect the average family to regulate the market and in effect to do what the Federal Reserve did not.

The proposed CFPA is a strong vehicle that could plug the gaps in our regulatory scheme. In particular, we commend the committee for including enforcement of fair lending laws in the mission of the agency. This, along with the creation of the Office of Fair Lending and Equal Opportunity, will ensure that the agency also investigates harmful trends in minority communities. This is a critical addition that will help Latino families.

We also applaud the committee for granting the CFPA strong rule-writing authority. This capability is fundamental to achieving its mission.

Also, we were pleased to see that stronger laws are not preempted. This will ensure that no one loses protection as a result of CFPA action. As the committee moves forward, these provisions should not be weakened.

And I will close just by offering a few recommendations of where we think it could be strengthened. A major goal of CFPA should be to improve access to simple prime products. Obtaining the most favorable credit terms for which you qualify is important to building wealth. This includes fostering product innovation to meet the needs of underserved communities.

We need to eliminate loopholes for those that broker financing, and for credit bureaus. Real estate agents, brokers, auto dealers, and credit bureaus should not escape greater accountability. And we need to reinstate a community-level assessment. Without it, good products may be developed but will remain unavailable in entire neighborhoods. Including CRA in the CFPA will give the agency the authority necessary to make such an assessment.

Thank you. And I would be happy to answer any questions.

[The prepared statement of Ms. Bowdler can be found on page 66 of the appendix.]

Ms. WATERS. [presiding] Ms. Burger is recognized for 5 minutes.

STATEMENT OF ANNA BURGER, SECRETARY-TREASURER, SERVICE EMPLOYEES INTERNATIONAL UNION (SEIU)

Ms. BURGER. On behalf of the 2.1 million members of SEIU and as a coalition member of the Americans for Financial Reform, I want to thank Chairman Frank, Ranking Member Bachus, and the committee members for their continued work to reform our broken financial system.

It has been a year since the financial world collapsed, showing us that the action of a few greedy players on Wall Street can take down the entire global economy. As we continue to dig out of this crisis, we have an historic opportunity and a responsibility to reform the causes of our continued financial instability, and protect consumers from harmful and often predatory practices employed by banks to rake in billions and drive consumers into debt.

The nurses, the childcare providers, janitors, and other members of SEIU continue to experience the devastating effects of the financial crisis firsthand. Our members and their families are losing their jobs, homes, health care coverage, and retirement savings.

As State and local governments face record budget crises, public employees are losing their jobs and communities are losing vital services. And we see companies forced to shut their doors as banks refuse to expand lending and call on lines of credit.

At the same time, banks and credit card companies continue to raise fees and interest rates and refuse to modify mortgages and other loans. We know the cause of our current economic crisis. Wall Street, big banks, and corporate CEOs created exotic financial deals, and took on too much risk and debt in search of outrageous bonuses, fees, and unsustainable returns. The deals collapsed and taxpayers stepped in to bail them out.

According to a recent report released by SEIU, once all crisis-related programs are factored in, taxpayers will be on the hook for up to $17.9 trillion. And I would like to submit the report for the record.

The proliferation of inappropriate and unsustainable lending practices that has sent our economy into a tailspin could and should have been prevented. The regulators' failure to act, despite abundance of evidence of the need, highlights the inadequacies of our current regulatory system in which none of the many financial regulators regard consumer protection as a priority.

We strongly support the creation of a single Consumer Financial Protection Agency to consolidate authority in one place, with the sole mission of watching out for consumers across all financial services.

I want to thank Chairman Frank for his work to strengthen the Proposed Consumer Financial Protection Agency language, particularly the strong whistle-blower protections.

We believe to be successful, the CFPA legislation must include a scope that includes all consumer financial products and services; sovereign rulemaking and primary enforcement authority; independent examination authority; Federal rules that function as a floor, not a ceiling; the Community and Reinvestment Act funding that is stable and does not undermine the agency's independence from the industry; and strong whistle-blower and compensation protections.

We believe independence, consolidated authority, and adequate power to stop unfair, deceptive, and abusive practices are key features to enable the CFPA to serve as a building block of comprehensive financial reforms.

Over the past year, we have also heard directly from frontline financial service workers about their working conditions and industry practices. We know from our conversations that existing industry practices incentivize frontline financial workers to push unneeded and often harmful financial products on consumers.

We need to ban the use of commissions and quotas that incentivize rank-and-file personnel to act against the interest of consumers in order to make ends meet or simply keep their job.

The CFPA is an agency that can create this industry change. Imagine if these workers were able to speak out about practices they thought were deceptive and hurting consumers, the mortgage broker forced to meet a certain quota of subprime mortgages, or the credit card call center worker forced to encourage Americans to take on debt that they cannot afford and then they threaten and harass them when they can no longer make their payments, or the personal banker forced to open up accounts of people without their knowledge.

Including protection and a voice for bank workers will help rebuild our economy today and ensure our financial systems remain stable in the future.

Thank you for the opportunity to speak this morning. The American people are counting on this committee to hold financial firms accountable and put in place regulations that prevent crises in the future. Thank you.

Ms. WATERS. Thank you very much.

[The prepared statement of Ms. Burger can be found on page 74 of the appendix.]

Ms. WATERS. I will recognize myself for 5 minutes. And I would like to address a question to Mr. David C. John, senior research follow, Thomas A. Roe Institute for Economic Policy Studies, The Heritage Foundation.

I thank you for participating and for the recommendation that you have given, an alternative to the Consumer Financial Protection Agency. You speak of the consumer protection agency as a huge bureaucracy that would be set up, that would harm consumers, rather than help consumers, and you talk about your council as a better way to approach this with lots of coordination and outside input.

It sounds as if you are kind of rearranging the chairs. Basically, what you want to do is leave the same regulatory agencies in place who had responsibility for consumer protection but did not exercise that responsibility. Why should the American public trust that, given this meltdown that we have had, this crisis that has been created, that the same people who had the responsibility are now going to see the light and they are going to do a better job than starting anew with an agency whose direct responsibility is consumer protection?

Mr. JOHN. Well, Madam Chairwoman, when you establish a new agency of this type, the first thing you are going to do is to move numbers of people into a new agency. You are going to disrupt existing patterns of activity, you are going to find yourself with people who are supposedly regulating. But the reality is, they are far more concerned about finding things like where their desk is and who their new reporting relationship is, and etc., etc.

What I am proposing is very simple. As the chairman pointed out, when Congress has moved the regulators and indicated to the regulators that they have not met their responsibilities, they have done a fairly good job at coming up with alternate proposals and actually doing their job.

Now, I would suggest that the coordinating council that I propose actually will serve the same purpose on a continuous basis. It keeps the regulators, the individual regulators in place, and I think it is very key that the consumer regulators have a good idea of what is going on within the financial institution that they regulate.

Regulating a bank is vastly different than regulating a credit union, which is vastly different than regulating a securities house, etc., etc.

Moving everyone into one—under one roof doesn't necessarily improve the coordination or improve the activity. It just changes things.

Ms. WATERS. Well, if I may, we just heard testimony about some of the abuses that really do need to be attended to. In this meltdown and this economic crisis that we have, as it was pointed out by one of our presenters here today, certain communities were targeted. I think it was pointed out by Ms. Bowdler, senior policy analyst, National Council of La Raza. Ms. Bowdler, do you think that these communities that have been targeted, who are suffering still today with foreclosures, who have been paying too high interest rates, were the recipients of predatory loans, do you think they would be satisfied with a coordinating council rather than a consumer protection agency?

Ms. BOWDLER. No, I don't think that more of the same is going to get us the results that we want. I think what we need is a better way to connect families to the products that they actually qualify for, which means developing new products in some cases, but it also means getting the good guys into our neighborhoods and making sure that they are actually competing for the business of our families, which they haven't been doing.

Ms. WATERS. Thank you very much.

Mr. Castle, for 5 minutes.

Mr. CASTLE. Thank you, Madam Chairwoman. Just this one little bit aside from all this, I have always felt this was a two-way street, and I think all you made some pretty good points, but I also am very concerned about the consumers and what they know and don't know. And this is not just a subject of this committee, it is in another committee I serve on, the Committee on Education and Labor, but I think that we need to do a lot more financial literacy.

I have heard from your testimony that there are many people who would have been qualified for prime loans and didn't get them because somebody sold them something or whatever it may be. But the bottom line is, if people have knowledge about what they are negotiating for, those problems would be not eliminated obviously, but could be reduced greatly. And I think we need to stress that as we go forward in dealing with this problem, which I consider to be a great problem.

I also, for the first time in my office, am starting to hear complaints about people not being able to get credit cards. And I worry sometimes about when we do these things there is a negative side to it that we have not contemplated and we need to be careful as we make changes. So I just point those things out as we go forward.

I happen to agree with Mr. John with respect to the council, I don't think it is more of the same, I think it is probably the way to go. But I want to ask the question based on that, if there is a Director of CFPA who had the exclusive authority to promulgate the consumer protection rules, and on that particular CFPA we would have the existing regulators who are able to advise a Director but there is no formal consultation process or requirements for the regulators to have a say in the rulemaking process, should we consider providing existing regulators with some kind of check and balance, or checks and balances, or veto power over the CFPA Director in the rulemaking process of safety and soundness concerns are raised for example.

That is an area I don't think we can ignore. I throw that out to whomever wishes to take a stab at it. Mr. Calhoun?

Mr. CALHOUN. Yes, if I may respond on two counts. One it seems to me if we were starting from scratch, and that might be a good place to think about here, it is hard to see that five separate consumer protection agencies are less government than one combined one. And in terms of the council, we tried a version of that over the last few years, the agencies did issue joint guidance. And it proved to not be a workable process.

For example, looking at subprime loans, despite all the requests from this committee and all the reports of problems in subprime lending, it was not until July 2008 that the joint agencies finally issued guidance on subprime loans, and then it was unenforceable. They issued guidance 10 months earlier on alternative loans and overlooked subprime loans. And the problem with the council was it became the least common denominator, there were holdouts.

Mr. PERLMUTTER. Can you pull your microphone closer, please?

The CHAIRMAN. There is a conversation going on in the back of the room that will stop and people will leave. People will not stand and have conversations while we are having a hearing.

Mr. CASTLE. I was a little worried the chairman didn't like my question.

Mr. CALHOUN. Or my answer.

Mr. CASTLE. My concern though is should they be in the room on the questions of safety and that kind of thing. That is what they are responsible for and I am concerned that decisions could be made by a council that could be disrupting to the overall balance of the financial systems in this country.

Mr. CALHOUN. We supported the addition of the oversight board that is in the current draft and the requirement for consultation and for transparency to make sure that happens.

Mr. CASTLE. Mr. John?

Mr. JOHN. I agree actually that the existing regulators and especially the prudential regulators who have a much better idea of what is going on within their particular industry, especially if you create some siloed outside CFPA, must have a very strong input and not just an advisory input but the ability to call a halt if absolutely necessary. We have already seen in a number of cases where regulators have left, shall we say, the realm of reality.

Now let me also respond to Mr. Calhoun. What I am proposing actually doesn't exist. What exists at the moment is just an informal agreement. What I am talking about is a formal structure with a formal chairman, a formal staff, a formal group of advisers who would have specific responsibilities and would hopefully meet some of the problems that we have had so far.

Mr. CASTLE. I am not going to have time for another question, but I will throw out a couple of thoughts in the remaining seconds I have. I am concerned that the legislation as currently drafted is not focused enough on the products and services that contributed to the financial crisis and perhaps in terms of its reach. I am not an expert in all the details of it, but that does concern me.

I have heard some of you mention preemption in what you are—I am also concerned about the confusion that eliminating preemption could bring into a system in terms of getting products out and is that going to end up being positive or negative.

So these are things that I intend to continue to keep my eye on. I yield back the balance of my time.

The CHAIRMAN. I will begin with Mr. John, and to clarify what you said, what you are talking about then would be not the existing informal arrangement but in effect a new agency with staff?

Mr. JOHN. Yes. What I am talking about, it is not a new agency, it is a new coordinating council of the—

The CHAIRMAN. Well, would it have staff?

Mr. JOHN. Yes.

The CHAIRMAN. Would it have new legal authority?

Mr. JOHN. I beg your pardon?

The CHAIRMAN. Would it have new legal authority?

Mr. JOHN. It would have the authority to issue—

The CHAIRMAN. Would it have legal authority that does not now exist?

Mr. JOHN. It would have limited authority.

The CHAIRMAN. But it would have some authority. Well, the point I am making is it is another new agency, so the question is we seem to be agreed that we need a new agency with staff and with new statutory powers, correct?

Mr. JOHN. Well, my agent—what I am proposing—

The CHAIRMAN. Does it have new staff and new statutory powers?

Mr. JOHN. It would have very small staff and work as FFIEC does. Mainly using—

The CHAIRMAN. It would have a staff.

Mr. JOHN. —assisting staff, yes.

The CHAIRMAN. And would it have additional statutory powers?

Mr. JOHN. It would have a very limited statutory authority.

The CHAIRMAN. It will be taking people from the existing agencies. So again I just am struck that you are proposing a new agency.

I am sorry, there appears to be a problem with the clock here. I don't see how I could be a minute-and-a-half over already. I am sorry?

I apologize. Mr. Castle, I am sorry, time expired and I began. So then I used a minute-and-a-half, so give me 3½ minutes.

The next question I do have is about preemption, and the argument is that if we do not have a total preemption of the sort that the Comptroller and the head of the Office of Thrift Supervision promulgated in 2004 we would have total chaos or serious confusion.

Mr. John, in the period before that much broader preemption went into effect in 2004, have you documented serious problems with conflicting mandates? Because it wasn't until 2004 that the Comptroller of the Currency and head of the Office of Thrift Supervision engaged in field preemption. Previously, there was case-by-case preemption. In the period before that—and they also blocked visitorial authority. Have you any studies of serious confusion in the pre-2004 period?

Mr. JOHN. I have not done any studies on that.

The CHAIRMAN. Are you aware of any that anybody has done?

Mr. JOHN. I am not aware of any. However, I would point out in many cases it was after 2004 that, for instance, San Francisco and various others entities starting looking at ATM fees.

The CHAIRMAN. I understand that, but of course the point was even before 2004, the bank regulators had the authority case-by-case to preempt any of those.

Mr. JOHN. Yes.

The CHAIRMAN. And I think that helps make the case as well. In the pre-2004 period, it seems to me people who tell us we have to maintain the field preemption exclusion of regulators from the States being involved that came in 2004 have some burden to show us that there was serious problems before that. And frankly, I think the absence of any evidence is a pretty good sign that was not the case. The standard before 2004 was that if there were conflicting things that the national regulators thought were a problem, they could preempt them case-by-case and we could still have other forms of preemption.

Second, I did want to talk about Mr. Castle's point that we were not dealing with the causes. This committee passed and this House passed, in a more partisan voice than I wish, very severe restrictions on subprime mortgages. So we have already done that. And as I have previously mentioned to him, we plan to incorporate them. I know he likes to forget that. But the fact is, over the objection of most people on the Republican side who said we were restricting credit unduly to low-income people, we passed very specific legislation which would restrict subprime mortgages and administering that would be part of the charter of this organization. It would also deal with other nonbank entities.

Look, I think we should be very clear. If only banks had been involved in the financial lending business, we would not be in the situation we are in. We would not have had the subprime mortgage problem. There are abuses with check cashing, there are some abuses in payday lending, so this is not an anti-bank entity at all. Indeed, I think much of what this entity will do will be to enforce on nonbanks the rules that have guided banks, particularly the community banks. That doesn't mean there have been no bank problems. There have been some, but I don't know why the gentleman from Delaware keeps arguing that we are leaving these other things out. They will be very explicitly covering nonbank competitors of the banks, and I think that will be enhanced.

On another point, though, I do agree with him—the gentleman from Texas, Mr. Hinojosa, the gentlewoman from New York, Mrs. McCarthy, and the gentlewoman from Illinois, Ms. Biggert, have been working together on financial literacy. We have had trouble figuring how to deal with this institutionally. One of the things that we expect to be a major part of this new agency is a significant emphasis on financial literacy, I think there is broad agreement. As I said, I think the gentlewoman from Illinois has been a part of that.

I now recognize Mrs. Capito.

Mrs. CAPITO. Thank you, Mr. Chairman. I would like to thank the panel. Mr. Shelton, I would like to ask you a question. I am concerned, I live in a more rural area, where we really are community bankers and our local lenders are the ones who are face-to-face with constituents every day. And they have voiced concerns about this because of—concerns of losing the flexibility that they believe, and I believe they do as well, offer at the local level to be able to forge financial products that meet an individual situation more on a case-by-case kind of situation. So I want to get to the issue of choice and choice of financial products, and I am wondering if you have any concerns since really the not so implicit premise of this is that consumers, some of them are simply not sophisticated enough or knowledgeable enough to invest in certain products or have certain products offered to them. Do you have any concerns that this might lead to some more insidious kind of redlining where there is a double standard or even one standard that only could be applicable maybe to a more sophisticated or wealthier borrower?

Mr. SHELTON. No, not at all. The biggest problem right now is first the lack of access of capital in the communities you are talking about. Some of the biggest challenges we have are issues not clearly covered by this bill, are issues very much like payday lending, some of those concerns. Too often in the communities that we serve there are so few legitimate financial lending institutions available that they find themselves being victimized by 456 percent APR when they go to, for instance, a payday lending facility in the local community. So the idea is to make sure: one, there is capital available in those communities; two, it is done in a fair way; and three, there is oversight to make sure the same consumers you are talking about don't get taken advantage of in the process.

What we saw happening as we saw the economic downturn is very well, even with the policies and oversight available to us now, there are many consumers who are actually led into products that they could not sustain. And we want to make sure there is oversight and transparency there as well. Brokers sat down with racial and ethnic minorities, sat down with the elderly and very well discussed products that they did not get full disclosure on how those products would actually function. As a result, tragedy occurred. There are many Americans who owned their own homes that went to refinance. For instance, elderly to buy new storm windows to address issues of climate change, or new roofs to address leakage of an aging house found themselves not only going into debt, but also going into debt at a rate they were not aware they would be going into because there was not full disclosure or full oversight.

So we very well argue that we need the products, we need the oversight, and we need a clear agency whose primary function is to provide some protection of the consumers as we enter these very challenging products.

Mrs. CAPITO. Mr. John, I would like to give you a chance to respond, because I believe you might have a different view on what this could do to consumer choice, particularly in the level that Mr. Shelton is addressing where they might not have a lot of options available and maybe at the lower economic scale. If you could—

Mr. JOHN. I am very concerned, I am one of your constituents, I live in Harper's Ferry, and we have a very limited selection of financial institutions that are available to us in the Eastern Panhandle.

One of the things we have been very concerned about is the fact that when you go into a small lender or something along that line or small bank that you—if you are directed only to a specific level of products, whether this is by government fiat or whether it is by encouragement or anything along that line, often people don't have the idea of what they are going to see. And we have had situations in—people I know in our communities who have been unable to get certain types of products because they are just not available, period. And what we do need desperately is an additional level of financial literacy, which Mr. Castle referred to.

If our schools taught what is necessary, if we found ourselves where new products would be available, for instance, some of the credit card products have fewer lower costs, some of the mortgage products, not necessarily the ones that sold to the people you are representing, have much lower costs than some of the traditional products.

The last thing that needs to happen here, whether it is by the council or a regulator, is to find ourselves eliminating or reducing incentives for new products and further improvements for consumers.

Mrs. CAPITO. Thank you. I think my time has expired.

The CHAIRMAN. The gentleman from North Carolina.

Mr. WATT. Thank you, Mr. Chairman. Let me see if I can squeeze three different things into this. Mr. John, first, the one thing I did like about what you were talking about is that there seemed to be implicit in it a strong support for State involvement in this inclusion of State regulators on the council—I am on page 3 of your testimony—States would continue to have flexibility in implementing regulations. Regulation of those entities that are currently State regulated would be preserved under your approach.

I assume that implicit in that is a strong support for the proposal insofar as maintaining State standards here, not preempting those standards at the Federal level; is that correct or am I missing something here?

Mr. JOHN. I believe that States should have—

Mr. WATT. I am just asking you, am I correct about that? Would you support, all things else aside, you seem to be a strong supporter of State involvement, would you support if we have a consumer protection agency of some kind, either yours or whatever, nonpreemption or preemption of State law?

Mr. JOHN. No.

Mr. WATT. Okay. You think we ought to preserve the State law and continue to enforce it, right?

Mr. JOHN. I believe that we need to have the States continue to have control over the entities that they have been regulating.

Mr. WATT. All right. Let me then go to Mr. Calhoun. We have gotten bogged down into the issue of whether this agency exists for and whether some other agencies—the existing regulators are going to regulate, continue to regulate consumer issues for existing regulated banks, but there is a whole world of entities out there that are not existing, regulated banks. Mr. Shelton seemed to be saying that he didn't think this applied, but I don't think that at all. I think this consumer financial protection agency would have full application to check writing, payday lenders, the whole range of things that were not under Federal regulation.

Do you see anything in this proposal that would not give the CFPA that authority?

Mr. CALHOUN. I think it is in the proposal, and I think the recent changes to the bill before the committee make that even clearer and that is one of the most critical things. Going back if I may say, the problem has been lack of oversight. We have had—

Mr. WATT. I understand that, but you—we need this consumer protection agency, even if we resolve this dispute about the regulated banks versus nonregulated, we need it for that purpose is the point I am trying to make.

Mr. CALHOUN. Yes.

Mr. WATT. Is that correct?

Mr. CALHOUN. I agree.

Mr. WATT. Now, the third issue I want to deal with is this whole preemption issue. You and I worked through this or tried to work through it on the predatory lending front, trying to find the appropriate balance about what got preempted and what did not get preempted. One approach that I want to sound out on you publicly today, and I haven't thought it all the way through, is similar to the approach that we used in the predatory lending area of actually going through and specifying some things that are not preempted, unfair and deceptive, State unfair and deceptive trade practices laws, State fraud laws. There was a list of them that we came up with. I don't have the list in front of me right now, civil rights laws, things that we know if a State legislates in, we ought not be preempting their standards because quite often a lot of those standards are set at the local level; is that correct?

Mr. CALHOUN. Yes.

Mr. WATT. Would that be an approach that might be an acceptable approach for us to start looking at in this context?

Mr. CALHOUN. It is something we certainly would work with you on. I think the key point, as the chairman made, is that the test up until 2004 was basically the Barnett Bank case of 1996, and it was that States can't enact laws unless they are significantly impaired. And then in 2004, we had regulatory competition over who could have the most preemption. Our biggest concern, and there is one point I want to make, there are proposals out, not just to preserve existing preemption, but to use this bill to greatly expand existing preemption by making all CFPA rules preemptive. We think that undercuts the benefit of the agency.

Mr. WATT. Thank you, Mr. Chairman. I yield back.

The CHAIRMAN. The gentleman from Texas, Mr. Hensarling.

Mr. HENSARLING. Thank you, Mr. Chairman. Clearly myself and a number of people on our side of the aisle continue to be very concerned about handing what we view as rather draconian powers to an unelected representative to decide upon subjective terms what financial products that our fellow citizens can enjoy. Clearly, many of you on the panel today don't seem to have that same concern.

I guess my first line of questioning then would be—I have heard a number of people talk about unfair and fair, but again those are very nebulous and amorphous terms. Mr. Calhoun, I believe I heard you say if the CFPA had been in existence a number of years ago, we probably would not have had this economic turmoil. I for one believe if it had been in effect a number of years ago, we probably wouldn't have ATM machines, frequent flier miles, and the list goes on.

But the first question I would have, given that incredible draconian powers are being suggested to be transferred to this government agency, is what are your views on what is fair and unfair? For example, payday lending, is payday lending per se unfair, Mr. Shelton? Yes, no, no opinion?

Mr. SHELTON. Well, I do have an opinion. The first part of the opinion—

Mr. HENSARLING. I am sorry, you do or do not?

Mr. SHELTON. I have an opinion. My opinion is very well that payday lending is absolutely necessary which is why the demand is so high. However, payday lending is extremely unfair in that the APR if you factor throughout most States ends up being astronomical.

Mr. HENSARLING. So I am sorry, it is needed, but it is unfair?

Mr. SHELTON. Absolutely, in an unfair way.

Mr. HENSARLING. If it is unfair, it could be outlawed by the CFPA so they could outlaw something that is needed.

Mr. SHELTON. Well, outlawing and regulating can be two different things. What we are looking for is compliance among those to provide—

Mr. HENSARLING. But I assume your association is where the proposed statutory language, does it not say that this agency would have the power to make these products unlawful, maybe they wouldn't? Does it not have the power?

Mr. SHELTON. Sure, sure. Some of the products should be made unlawful.

Mr. HENSARLING. Well, let me ask you about that. I come from Dallas, Texas, where a $200 Ace Cash Express payday loan would carry $60, 76 total finance charge, which would be 30.4 percent. Is that unfair? If you were advising the CFPA, which I believe is going to have some kind of advisory council, would you advise them to make this product unlawful?

Mr. SHELTON. If we are talking about an APR of 30 percent? Then I would say it should be considered fair.

Mr. HENSARLING. How about 40 percent, 50 percent?

Mr. SHELTON. I think you are running too high, then. I think even the Federal Government and this particular committee basically set a 36 percent cap on loans for people in the military. We think that is a good fair place to begin the conversation.

Mr. HENSARLING. Let me ask you this question Ms.—is it "Bowdler" or "Bowdler?"

Ms. BOWDLER. "Bowdler."

Mr. HENSARLING. I am sorry, I will go to you next. I saw your hand up.

Let's talk about credit cards for a moment. This committee has moved on legislation, passed into law that sense we will prescribe universal default. Now clearly, if one looked in the marketplace you could find credit cards that had universal default provisions that had lower interest rates than cards that didn't carry universal default. Is universal default unfair or abusive? And if my facts are correct that one could have received a credit card with a lower percentage rate had it been in there, is it still unfair and abusive?

Ms. BOWDLER. That is not really the approach that NCLR would recommend taking when it comes to those kinds of products.

Mr. HENSARLING. Can you pull the microphone a little closer?

Ms. BOWDLER. Yes. That is not really the approach we would recommend taking. What we recommended in our testimony is that we need to spot trends that have disparate impact. So if we look at the use of various products and it is having routinely a negative affect on our community then what we would rather see is that products that have a less disparate impact be promoted.

Mr. HENSARLING. So you don't necessarily know whether it would be fair or unfair; you would look at its disparate impact.

Previously we have had testimony, I believe probably a few years ago, from a representative of the U.S. Hispanic chamber who said a large number of their members capitalize small businesses with credit cards. And so if the CFPA were to outlaw certain credit cards and that led to less capital for small businesses which employed fewer Hispanics, would that be of concern to you and your organization?

Ms. BOWDLER. Outlawing products—NCLR has never advocated for the banning of any products from the market. I understand that the CFPA has that power. That is not—again, that is not our approach. But what my concern is, is that there are a lot of good credit cards, good mortgages, good short-term loans that are gathering dust and never see the light of day because bad practices actually replace them in the market. So if we can get incentives to get those more positive products that actually build wealth in small businesses, in modest income homes, that is what we want to do.

The CHAIRMAN. The gentleman from Kansas.

Mr. MOORE OF KANSAS. Thank you, Mr. Chairman.

Mr. John, on page 4 of your testimony, you say the CFPA proposed list was filled with poorly considered departures from existing law and practices that are as likely to damage consumers' interest has improved them. You suggest a council of consumer financial regulators would be sufficient.

Do you really think existing law and practice, in your words, worked to prevent the financial crisis last year, sir?

Mr. JOHN. For one thing, I think there are some different causes of the financial crisis and that just focusing on consumer activities and consumers lending is somewhat misleading. If the laws that exist on the books, and this includes both State laws and Federal laws, had been properly enforced and had been carefully considered, meaning the coverage of things like unregulated mortgage brokers and things like that had been covered by some of the States, I think that would have gone a long way toward preventing some of the consumer products breakdowns that caused the situation. As I say, I think there was a lot more than just that.

Mr. MOORE OF KANSAS. What laws were not enforced that should have been enforced and who was to have enforced those laws, sir?

Mr. JOHN. I think an article from the Washington Post from Sunday has already been cited here. I was deeply disturbed, for instance, to see a Washington Post article last December which pointed out a low-income immigrant couple who were moved into a multi-hundred thousand dollar housing loan despite the fact they had a very low income. We could go through the list. And the list would be very long, both on a State and a Federal area.

One of the problems the chairman has pointed out very effectively is that this is not one of the key responsibilities of the regulatory agencies. Now, I think you can make it a responsibility and make it an emphasis just as easy with a coordinating council as you can by massively disrupting the whole consumer regulatory system by creating a new agency.

Mr. MOORE OF KANSAS. But you do think existing law and practice worked to prevent the financial crisis last year?

Mr. JOHN. I think existing law and practice, had it been properly enforced and properly expanded, would have worked, too.

Mr. MOORE OF KANSAS. Thank you, sir. The provision I like about the current CFPA draft, the provisions I like are the consolidated rulemaking for consumer protection laws, expanding financial literacy efforts and, most importantly, from my perspective, strong oversight of nonbank firms, many in the mortgage market that issued too many loans families couldn't afford. As a former district attorney for 12 years, I had to prioritize resources to ensure the most urgent threats were focused on, and I believe the same lessons apply to CFPA.

Starting with Mr. Shelton and quickly going down the line, if you had to choose the larger threat to financial stability, the lack of supervision of nonbank firms, especially those that made predatory subprime loans or consumer protection or protection enforcement of banks, which would it be?

Mr. SHELTON. I would have to say the latter, consumer protection.

Mr. CALHOUN. I think you have to balance all of them. And there has been discussion of the role of banks. I think it is important to remember they did the lion's share of the so-called Alt-A loans which would have larger defaults at greater taxpayer cost than even the subprime loans.

Mr. JOHN. As I have said, I think the causes of the financial problems were far too serious and far too confusing to just limit it to those two.

Ms. BOWDLER. I don't think that you can separate those, those work like yin and yang, the fact that you had unregulated entities flooding the market and the absence of banks that had the most favorable products lead to a perfect storm. You need both.

Mr. MOORE OF KANSAS. Thank you.

Ms. BURGER. I agree you need both.

Mr. MOORE OF KANSAS. The last question, setting aside the current CFPA draft, what steps could be taken to ensure Federal bank regulators did their job on consumer protection? FDIC Chairman Sheila Bair has proposed that the CFPA could be given backup authority where they could intervene case-by-case if they saw lack of enforcement by bank regulators. Another idea I might suggest is a stronger "use it or lose it" authority requiring bank regulators to either enforce consumer protection laws or lose that authority. After being graded by the CFPA or the GAO, if a bank regulator fails to fully enforce consumer protection laws, they would automatically lose that authority to CFPA.

Mr. Calhoun, would this use it or lose it approach ensure that regulators do a better job, do you believe?

Mr. CALHOUN. We think that at the end of the day, the CFPA needs to have enforcement authority. As we detail in our written testimony, there have just been repeated instances over the last 6 and 8 years where regulators have turned their backs on enforcement, and the most striking example was the OTS, which allowed several of its institutions to back-date their capital reports and those firms subsequently collapsed at substantial cost to the taxpayers.

So you need someone whose focus is both on consumer protection and enforcing it. It does need coordination. We support that.

Mr. MOORE OF KANSAS. Thank you, sir. Mr. Chairman, I yield back.

The CHAIRMAN. The gentleman from North Carolina, Mr. McHenry.

Mr. MCHENRY. Thank you, Mr. Chairman. Clearly, increasing accountability is necessary, that goes without saying. Consumer protection goes with that increased transparency and accountability.

Ms. Burger, for nonprofits which conduct financial literacy credit or housing counseling on behalf of the CFPA or any government agency, what degree of accountability and transparency should we require of them?

Ms. BURGER. I think that there should be transparency for them as well. And one of the things that I actually suggested in my testimony was the whole issue about compensation for front-line workers as well, because one of the things that we have discovered over the last number of months that we have been really looking at what the impact of the credit crisis on our members has been is that front-line workers are often compensated at such a low base pay that the only way they can survive and support their families is try to exceed their quotas and be paid by bonuses, and the bonuses actually encourage them to push products that are unfair, unsustainable for working families. We think one of the things we should look at within this bill is a way of really looking at compensation reform, not only at the top of the financial industry but at the bottom of the industry as well.

Mr. MCHENRY. So those who are providing credit counseling, for instance, on the front lines, you have concerns about their pay. And the question I have is in—with these recent revelations about ACORN, do you think they should be precluded from being a participant in the CFPA program?

Ms. BURGER. We think that there should be, as is being done right now, a thorough investigation of ACORN. I think they have an independent investigator right now and that we should make that decision afterwards. I do think that there should be total transparency for any agent—for any nonprofit or for-profit that would be getting Federal dollars to provide counseling.

Mr. MCHENRY. Do you think the failure in ACORN, from your analysis, is that a failure of pay?

Ms. BURGER. I did not take part in the analysis of ACORN. I think that ACORN as an organization over the years has done a lot of great work in low-income communities. There is an investigation going on right now and we should make sure that violations never take place in the future.

Mr. MCHENRY. Okay. As of today, the U.S. Census Bureau, the IRS, and even Bank of America have severed ties with ACORN. And according to yesterday's, actually the day before yesterday's report from the Chicago Sun Times, the SEIU has given ACORN $4 million. Could you clarify to me the extent of your financial and programmatic ties to ACORN?

Ms. BURGER. SEIU has also cut all ties to ACORN.

Mr. MCHENRY. They have?

Ms. BURGER. We have. In Illinois, I believe that I am correct, that the ACORN institution, the consumer protection, the community organization in Illinois cut its ties to ACORN 2 years ago. And so in Illinois, there were no ties in the last 2 years between any SEIU work and ACORN.

Mr. MCHENRY. Okay. What was the extent of your financial ties with ACORN?

Ms. BURGER. I will get that information for you for the record.

Mr. MCHENRY. Because in Illinois, for instance, there was a tie based on location, even the fact that their e-mail addresses that were shared on your Web sites for the other organization.

Ms. BURGER. My understanding is that in Illinois, their offices happened to be next door to each other, not cohabitated, but I will get that information for you.

Mr. MCHENRY. Okay, thank you. In the same building, I think it was a different floor of the same building.

Mr. John, in terms of the larger issue of the CFPA, can you regulate consumer protection from financial institutions without a safety and soundness mission as a part of that?

Mr. JOHN. No. When it comes right down to it, if you don't focus on the safety and soundness aspects of products and proposed regulations of those products, you are very likely to find a situation where a practice is encouraged which may be detrimental to the financial institution and therefore to the customer.

Mr. MCHENRY. Thank you. I yield back.

The CHAIRMAN. I recognize the gentleman from Missouri, but I ask him to yield me 15 seconds to say to Ms. Burger—you mentioned cutting ties with ACORN 2 years ago.

Ms. BURGER. In Illinois.

The CHAIRMAN. That beats the Bush Administration, which continued to fund ACORN every one of its 8 years. So you were ahead of the Bush Administration, which in its last 2 years, was giving ACORN a couple million dollars while you were cutting ties.

Ms. BURGER. I just wanted to make the point that in Chicago, the organization once upon a time was ACORN, that community organization cut its ties to National ACORN, too.

The CHAIRMAN. Again, the Bush Administration, to the day it went out of office—ACORN got $14 million from the Bush Administration. So they make you look like a pica.

Mr. CLAY. Thank you so much, Mr. Chairman. Thank you for the clarification on the status of ACORN in both Administrations. I appreciate that candor.

Let me ask Mr. John, under systemic reform, the Federal Reserve has asked for additional authority to protect consumers. We know what their record has been over the last decade as far as protecting consumers when big banks like Wells Fargo and Citibank formed offshoots and companies for the sole purpose of setting up subprime mortgage companies and targeting black and brown communities. And we know the devastation that occurred under that scenario and those communities are still suffering to this day.

But do you feel as though we should give the Federal Reserve additional authority or should the CFPA or some similar agency have the authority to protect consumers under scenarios like this?

Mr. JOHN. Well, the Federal Reserve authority for systemic risk is something that I have written against, simply because I believe that a is no-win situation. It is not possible to protect against systemic risk. There are political problems, there are economic problems, etc.

In the specific case that you mentioned, which was the setting up of subsidiaries, I think the Federal Reserve made a very serious error in not following through on that. And one of the things that I would hope is that in the council that I am proposing, the staff would note that, that it would become an issue, and there would be a report sent to this committee which would hopefully hold a hearing on that. The most effective oversight is not going to be a big regulator or a small regulator or anything like that, it is going to be those of you who are going to ask nasty questions.

Mr. CLAY. Well, thank you for that response.

Let me hear from the other panelists. Ms. Bowdler?

Ms. BOWDLER. Just to add to that, even if we had a council of some sort, what I think would be missing and what has been missing from existing mandates on the regulators is the requirement to look specifically at what is going on in underserved communities. That is important because as we have all already said, our communities were targeted, both passively and actively, in different ways. I am happy to talk more specifically if somebody wants me to on that.

What you can have is a situation where entire communities are devastated and in our case entire generations of Latino wealth are in jeopardy. But it doesn't rise to the level of endangering the actual safety and soundness of the system and therefore never gets picked up. That is what we had. So we need to have somebody who specifically is looking at what is going on with vulnerable populations, minority communities, immigrants, the elderly, etc., those of modest means. Those are the most vulnerable among us and those trends will be missed unless there is a specific charge to look at them. In the new jobs legislation with the Office of Fair Lending, we think will have that.

Mr. CALHOUN. If I can add, the question boils down to who do you the Congress want to trust carrying out this authority. For me a telling statistic, we heard about the disparate lending practices, but if you look from 2002 to 2008, the OCC did not make a single referral to the Department of Justice for equal credit violations. Do you want to trust authority back to them or do you want to try a different approach?

Mr. CLAY. Sure. Mr. Calhoun, how do you envision a new agency like the CFPA, what would be their mission with the whole financial literacy piece? Do you envision any role?

Mr. CALHOUN. I think that is a key part, it is not a solution by itself but it is a key part and it would be a key part of this agency's work.

Mr. CLAY. Thank you so much. I yield back.

The CHAIRMAN. The gentleman from Texas, Mr. Marchant.

Mr. MARCHANT. Thank you, Mr. Chairman. My preference on this particular item would be to go with a council. I would like to explore a little bit of the idea of the council with you. Would you make the council be the—would they accept complaints from the public under your concept?

Mr. JOHN. I would see actually that the individual regulator should accept the complaints from the public and the like. One of the problems is that the individual regulators, whether under this system or under the CFPA as far as I can tell, is not an ombudsman, that they basically look for abusive practices and abusive situations and then go to correct them. They are not there to litigate specific complaints by individual consumers.

Mr. MARCHANT. So that would answer my second question, you would give them the power to investigate systemic abuse of consumer financial—the financial system?

Mr. JOHN. Absolutely.

Mr. MARCHANT. Would you give them the ability to make recommendations to the regulators?

Mr. JOHN. Absolutely.

Mr. MARCHANT. Would you give them the power to create a consumer protection protocol, examination protocol for the respective regulators so that they could incorporate that protocol into their regular examination.

Mr. JOHN. Yes, absolutely.

Mr. MARCHANT. Do you envision, and this question is for the rest of the panel as well, this council or agency having the ability to go to FHA, Fannie Mae, and Freddie Mac, who now originate currently 90 percent of the mortgages in the United States, and redo their documents to reflect their documents or would you allow their documents to remain intact?

Mr. JOHN. I don't see—I would allow them to remain intact. It is really the Federal Housing Finance Agency that has the authority over that type of area.

Mr. MARCHANT. Well, many of the Alt-A loans and many of the subprime loans that were made in 2007 and 2008 were actually originated and insured by—not originated by but were insured by and were done on Fannie Mae and Freddie Mac forms.

Mr. JOHN. Yes, but at the same time it becomes somewhat difficult to have one agency basically going through and regulating another agency. I think that gets a little bit—

Mr. MARCHANT. But a council could look at those documents and say, the consumer needs to be better informed here.

Mr. JOHN. Yes.

Mr. MARCHANT. And they could make a complete examination without having the authority to change those documents?

Mr. JOHN. That is correct.

Mr. MARCHANT. Would any of the rest of you like to address that whole Fannie Mae, Freddie Mac?

Ms. BOWDLER. I just want to add one quick thing, and I am going to start to sound like a broken record here, but Fannie and Freddie is a perfect example. Fannie and Freddie had really great prime products that were flexible, the 30-year fixed, they had all sorts of variations that would meet a wide range of credit needs. Those were not the products that actually made it down to retail, and they had a hard time competing on the regular market. And the reason was because they took longer to originate. In some cases, they may have actually required manual underwriting.

Somebody, Mrs. Capito mentioned community banks earlier. They have the same problem where because they were doing all the right things, because their process takes a little longer, maybe doesn't turn as much of a profit, they get pushed to the back. So in that case you can see how in one institution they had these solid products. We would like to see them put them more forward, put added incentives so those were the ones being pushed at retail, but they weren't, they were gathering dust in the back. And instead, you had products that were quicker and easier to originate that proliferated throughout the market because they earned higher profit going back to points around compensation systems.

Mr. MARCHANT. But many of those loans were made and insured by Fannie Mae and Freddie Mac.

Ms. BOWDLER. They have multiple—all these institutions have within them a wide range of products. So they will have a product that I—again just speaking for the clientele that we work with—that could have worked for Latino families, but maybe it required manual underwriting or didn't pay as high of a commission and so it wasn't put out there in a big way.

The CHAIRMAN. The gentleman from North Carolina, Mr. Miller.

Mr. MILLER OF NORTH CAROLINA. Thank you, Mr. Chairman. Mr. Castle said in his opening statement that the worst subprime loans, the bulk of the bad subprime loans were not made by depository institutions that were fairly closely regulated but by non-depository institution, independent lenders.

Mr. John, you testified a few months ago before the Investigations and Oversight Subcommittee, of the Science and Technology Committee, which I Chair, on the role—and one issue that came up was the role of the Community Reinvestment Act. Mr. Castle is right, a relatively small number of the bad subprime loans were made by depository institutions subsequent to the Community Reinvestment Act. And in fact a study by the Federal Reserve Board found that only 6 percent of all the subprime loans were made in assessment areas or in the neighborhoods where CRA encouraged lending—or to borrowers that CRA encouraged lending to. And you agreed then that CRA had a negligible effect in the subprime crisis and the financial crisis generally. Is that still your view?

Mr. JOHN. Absolutely.

Mr. MILLER OF NORTH CAROLINA. Mr. Calhoun, I ask you because I know you have been here for the 6½ years that I have been here, you have been sitting at this table when I have been sitting at this table. So has Mr. Shelton, for that matter. The industry is now saying that they support consumer protection, but not a consumer protection agency. Steve Bartlett was quoted recently saying they support the "CFP," but not the "A." That is not entirely consistent with my recollection. My recollection is that they opposed every consumer protection bill, the predatory mortgage lending legislation that I introduced, the credit card legislation that Ms. Maloney introduced, the overdraft bill that Ms. Maloney introduced. They commented publicly opposing rules that protected consumers further.

Is that your recollection? Do you recall industry pushing for stronger consumer protections?

Mr. CALHOUN. They have usually disagreed with the proposals that have been before this committee and before the regulatory agency.

Mr. MILLER OF NORTH CAROLINA. Mr. Shelton, do you remember them pushing for stronger consumer protections?

Mr. SHELTON. No, I do not, sir.

Mr. MILLER OF NORTH CAROLINA. Now the argument is, it should just be enforced better. I know that right now there are sentencing hearings going on all over America where the defendant is saying the problem was they had a permissive parent and their parent really should have set limits. But do you recall the industry at the time saying that their prudential regulators should come down harder on them, should be stricter on them, that their prudential regulator was entirely permissive and indulgent? Mr. Calhoun, do you recall that?

Mr. CALHOUN. No. In fact, the record is clear that institutions, Countrywide being one of the notable ones, the largest mortgage lender, went and pressured their regulators to ease up and in fact switched regulators because they thought the original regulator had gotten too strict with them.

Mr. MILLER OF NORTH CAROLINA. Mr. Shelton, is that similar to your recollection?

Mr. SHELTON. That is my recollection as well.

Mr. MILLER OF NORTH CAROLINA. Ms. Bowdler, I am kind of leaving you out, you have been here. Is your recollection of this consistent with theirs?

Ms. BOWDLER. Yes.

Mr. MILLER OF NORTH CAROLINA. A final point, I am struck by the arguments against CFPA that they could do something stupid, they could regulate, they could prohibit something that actually is good. The Food and Drug Administration prohibits patent medicines mixed up in bathtubs that actually don't cure cancer as advertised but are toxic, but they also, the FDA, could prohibit statin drugs. I am now 2 years older than my father was when he died from a heart attack, I am on a pretty stiff dose of a statin drug, and I have high hopes that I will stay around for a really long time, to be annoying to a lot of people for a really long time.

The Food and Drug Administration could prohibit statin drugs, but it would be stupid to do so. Does anyone think the Food and Drug Administration should be abolished because they could prohibit medicines that were actually beneficial and therefore allow patent medicines mixed up in bathtubs to come back on the market? Does anyone wish to argue for that position?

I see that no one does. Mr. Chairman, I yield back.

The CHAIRMAN. Well, if the gentleman would yield briefly to me for his remaining time. He may have been a little unfair to some of the business organizations with regard to consumer protection laws, noting that they always oppose them. That is often their initial response, but it has been any experience that once they have been adopted, several years later they are quite fond of them, particularly when people have proposed any enhancement of them. So there is a kind of retroactive falling in love with them especially when we have had them in place and then talk about maybe building on them.

The gentleman from California.

Mr. ROYCE. Thank you. Mr. John, should every State be allowed to prohibit statin drugs? Maybe that is the question we should ask ourselves next.

Let me take, Mr. John, something you wrote, most Federal laws specify a national standard that States must observe, but the CFPA would explicitly subordinate Federal regulations to stronger State laws. You said a strength of the financial market is the ability to offer standardized products that reduce costs to both firms and consumers.

However, in this paper you wrote some months ago, you laid out a little problem. Under the CFPA national firms could face up to 51 separate consumer regulatory regimes complete with disputes about whether the applicable standards that applies is the one from the State where a consumer who has made a purchase lives or the State where the firm is physically located or the State where the Internet site that was used is registered. So instead of one product, you have a whole host of products here sold across State lines.

The question I would ask you is, who would ultimately pay the price for these inefficiencies?

Mr. JOHN. That is easy, it is the consumer when it comes down to it. One of the problems we have been facing and the chairman pointed out that there were a few problems with State preemption prior to, I believe in 2005 or 2006 or so. However, we didn't have the same level of extremely activist attorneys general, most of whom are seeking to be senators or governors, who actively seek out situations and actively promote more than reasonable solutions to them. So we are much more likely in the current situation to have attempts by various ambitious State officials to move into and obstruct national markets.

Mr. ROYCE. But couldn't companies just create these multiple variations that meet this myriad of State requirements without passing that on to the consumer? Why would it be passed on to the consumer?

Mr. JOHN. There is a need to make a profit. There is a responsibility to one's shareholders, of course.

In some insurance situations, they actually have done a number of different variations to meet specific State requirements and the like, and the net result has always been a higher cost to the consumer.

Mr. ROYCE. I think there is a broad agreement that the current State-based insurance system is inefficient; the studies that I have seen have a tag of about $10 billion cost to the consumer. It also hampers U.S. competitiveness. I am thinking about the Schumer-Bloomberg study and other studies. The lack of a centralized regulator with the ability to look at the entire U.S. market, certainly those were the concerns that the Treasury Department laid out in their regulatory reform proposal.

So as we are working to streamline and consolidate regulatory authority in the insurance portion of our financial system, especially in light of some of the problems with AIG and so forth, it appears we may be taking a step back, then, in the rest of the financial services sector with this CFPA. Let me ask you, do we run the risk of replicating many of the problems that have arisen in the insurance market throughout the financial services sector with this legislation if we go down this road?

Mr. JOHN. That is specifically my concern, yes.

Mr. ROYCE. Would you like to comment for a minute just about some of the difficulties? Maybe you could expand on the problems with bifurcating solvency protection from consumer protection, put safety and soundness on one side and consumer protection on the other. Many of the regulators have explained the problems with separating these two missions. We saw that model over Fannie and Freddie. Could you give us some insight on that front?

Mr. JOHN. Well, I have mentioned this briefly in the past. One of the strong situations that I think is not necessarily going to pop up immediately, but it is definitely going to be the situation if you do create a CFPA, is that there will be a siloization; that the Chairman's Advisory Board is a good step, but the Chairman's Advisory Board is not sufficient to prevent that siloization. So essentially the consumer regulations of the future, whether that is 5 years, 10 years or 2 years down the line, are going to be made without a direct input or a direct one-on-one understanding of how particular regulated financial institutions work.

One of the things that deeply concerns me about this whole situation is that if a CFPA focuses explicitly on the largest types of financial institution, i.e. the banks, the special characteristics of smaller types of financial institutions, such as credit unions, are likely to be ignored or placed in a secondary basis. And that is going to cause problems for consumers. It is going to cause problems for financial institutions of different types, etc. You are going to see a homogenization, which is very dangerous.

Mr. ROYCE. Thank you, Mr. Chairman.

The CHAIRMAN. The gentleman from Georgia, Mr. Scott.

Mr. SCOTT. Thank you, Mr. Chairman.

I would just like to kind of focus my remarks on unintended consequences, one-size-fits-all dangers of this, as well as the confusion between State and Federal laws as we move forward. It is an important legislation.

Let's take my first problem of unintended consequences and whether or not this would work, particularly with some unique situations. I am sure you all are familiar with the Farm Credit Administration. The Farm Credit Administration is very, very unique. They already have what they call a borrowers' bills of rights, which basically covers much of what we are attempting to do in this bill, resulting in if they were into this duplicatory obligations, burdensome regulatory concerns as well.

Consumer lending is a very, very small part of what they do. Mortgage lending, for example, is only allowed in communities with less than 2,500 individuals. Their products were not anywhere near the toxic level that caused the problem in the first place.

So my question is, would not we be doing a better service here if we allowed the farm credit to continue to operate under its own current regulatory process away from this legislation?

I take it all of you agree that it would be the best thing to do in this situation, to allow farm credit. The reason I mention that is, also, farm credit does not come under the jurisdiction of financial services. It is an agricultural area. And I am simply saying that it makes sense—this is a complex, complicated area, covers a lot of the waterfront when we are dealing with the financial services industry. And it might be wise as we move forward with this to look inward-outward instead of outward-inward. And I think that what I am getting from the committee here is that you agree that the Farm Credit Administration should be left away from this or doing what they are doing with the bill of rights; weren't a part of the problem in the first place; and this would be a duplication.

Mr. CALHOUN. Congressman Scott, I would like to express concerns about creating these exemptions because of the difficulties that has created in the past. One of the biggest examples was, just a few years ago, in fact even when we were looking at the predatory mortgage bill hear this committee, there were efforts to exclude FHA with the argument that FHA loans are a very small part of the market. They were about 2 percent a few years ago, and they were the generally safer loans.

However, in the last year, we have seen the very subprime lenders invade FHA. You can go on the Web sites and see ads for, here is how you transfer your business. And there are subprime lenders who have literally converted into FHA lenders. One of the beauties of and I think real core strengths of this bill is it looks at products, not the label that is put on the product or the label that is put on the financial services provider, because that has created a lot of problems. In this specific limited exception, it may be okay. But these exceptions have created a lot of dangers in the past.

Mr. SCOTT. I think my point is, to allow them to operate under their current regulatory reform and to monitor the situation if that is not sufficient, then we can come back and address it. This Draconian approach here makes a lot of duplication.

Mr. CALHOUN. I think the bill would allow that to happen. But I think it needs to be careful how it is used.

Mr. SCOTT. Absolutely.

Let me ask one other question about the States. States are currently licensing providers that I think results in some confusion as it applies to what we are currently trying to do. And under the bill, H.R. 3126, it grants authority to the CFPA to establish new baseline rules, a prospect that would see a number of State laws rendered mute. So the question becomes, how would the CFPA decide which laws and regulations to leave in place and which to preempt?

Would the CFPA have to show a record of compliance or a failure of enforcement by State authorities in order to preempt State laws? And then finally, comparison with State laws are not often apples to apples, and so if you could comment on that, that would be helpful.

The CHAIRMAN. I am sorry. There will be no time to comment. Members have to understand, if you ask a question after the light is on, you will have to get the answer in writing. It is 40 seconds in. We won't have to time to get an answer.

Mr. SCOTT. I will be glad to get it in writing, Mr. Chairman.

The CHAIRMAN. The gentleman from Texas.

Mr. GREEN. Thank you, Mr. Chairman.

And I thank the witnesses for appearing.

Mr. John, thank you for your creative concept. I would like to visit with you for a moment about it. You have indicated that the council, and this is in your testimony, would be charged with creating uniform standards for examination of financial institutions. But you also indicate that these standards would not be imposed. My assumption is, if they are not imposed, they would be recommended. And the question becomes, how would the recommendation become a standard that would be enforced?

Mr. JOHN. The recommendations would be enforced through a combination of two things. One would be, if a regulatory or a statutory change is needed at the State level—

Mr. GREEN. How do you get the regulator to embrace the standard that is recommended? Because the agency that you are proposing cannot impose standards. It can merely say, here is a thought. How would you get the thought to become a reality within the regulator?

Mr. JOHN. It would be a very simple matter that, in the event that the regulator does not adhere to a particular standard, understanding of course there may be specific adjustments necessary for—

Mr. GREEN. I have to ask you to move it a little faster.

Mr. JOHN. The bottom line is that it is your responsibility.

Mr. GREEN. Congress? So let me get it right. Hold on. Your agency recommends—well, you have a board that works with the president of this agency that you are recommending.

Mr. JOHN. Right.

Mr. GREEN. And they make recommendations to these various regulatory agencies. And if the agency does not abide by the recommendation, then this council would then make the recommendation to Congress, and Congress would then move on it?

Mr. JOHN. The regulatory board would, for one thing, the agency that is in question would have been a part of the process—

Mr. GREEN. I understand. But ultimately, it would take an Act of Congress to act on the recommendation if the recommendation is not adhered to?

Mr. JOHN. It would be a matter for Congress to put pressure on the agency just as you would put pressure on the Federal Reserve for—

Mr. GREEN. Well, the way we put the pressure on some of these agencies has been to threaten legislation, and thus we then go through that process, and then they have this epiphany.

But what you are saying is that it will take an Act of Congress to do something ultimately if the regulator doesn't do it. And that means that you have to have a Congress that is willing to act, which means that we would have to go through all that we are going through right now to try to simply get an agency in place.

What you are doing is putting all of this back within the purview of the Congress of the United States of America, which is where we are right now in terms of trying to establish the agency because you don't give any authority to impose the regulations on the various regulators.

Now, let me go to another point. With reference to what you are proposing, you have indicated that there should be one representative from each Federal Agency and elected representatives from councils among the various States.

Mr. JOHN. Right.

Mr. GREEN. Would we have at least one from each State? Is that what you are saying?

Mr. JOHN. No, that is actually not what I am proposing. What I did not want to have happen here is that you would have 300 State representatives out-voting six Federal regulators.

Mr. GREEN. How many would you have from each State?

Mr. JOHN. We would have roughly one—no, it is not one from each State. It is one representing, for instance, the State credit union regulators; one representing the Congress and State bank supervisors; one representing the various insurance regulators; etc.

Mr. GREEN. And would they all have voting power?

Mr. JOHN. Yes. But the goal here is not to have things that were done by votes.

Mr. GREEN. I understand. But they would have the authority to vote?

Mr. JOHN. Yes.

Mr. GREEN. And it would be the vote of this body that would ultimately decide whether or not a recommendation would be adhered to?

Mr. JOHN. Yes.

Mr. GREEN. And how many total would we have on this body?

Mr. JOHN. Frankly, it depends on whether Senator Dodd's approach—

Mr. GREEN. Let us talk about your approach. This is your recommendation.

Mr. JOHN. Yes. But the thing is, the testimony specifically says that the number could vary depending on whether regulators are merged or not merged—

Mr. GREEN. I understand. But how many are you envisioning?

Mr. JOHN. I am not envisioning a particular number. I recognize that this is all part of the existing regulatory restructuring process.

Mr. GREEN. I thank for your information.

Let me just share with you that it seems to me that this is going to be a rather awkward way of doing business, and it brings us right back to where we are now, needing congressional oversight to get something done.

And I yield back.

The CHAIRMAN. The gentleman from Missouri.

Let me just say, we are going to finish up with this panel, and then we will go right into the second panel at 12:30, about, it looks like because there are going to be votes about 2:00, and we are going to go until then. So let us move right along.

The gentleman from Missouri.

Mr. CLEAVER. I will save my questions for the next panel. I would ask Ms. Burger, do you think that ACORN was involved in any way with the provocative testing of an Iranian missile on this past Saturday?

Ms. BURGER. No.

Mr. CLEAVER. Thank you.

I will reserve my questions for the next panel.

The CHAIRMAN. I thank the gentleman.

And I now recognize the gentlewoman from Illinois.

Ms. BEAN. Thank you, Mr. Chairman.

And thank you to our witnesses for bringing your expertise to us today on this important issue.

There seems to be general consensus that Federal consumer protection laws were not adequately updated through rulemaking by the Federal Reserve. And some feel that is because the other responsibilities that the Fed has took priority over consumer protections, which is why so many of us do support the creation of a CFPA that would put the consumers' interest first, prioritize that so that we would have effective and consistent protections.

Do you believe—and I guess I will direct this to Mr. Calhoun first—that the CFPA would do a better job of updating the rules and providing more robust consumer protections than the Federal Reserve?

Mr. CALHOUN. Yes. And if they don't, I think the Congress, you will take action as you have done with other agencies that you have delegated authority to who have not used that authority.

Ms. BEAN. Okay. Are there others who would like to comment on that?

Ms. BURGER. I think that what we really need is an agency that actually looks at the interests of the consumer first as opposed to last or never. And I think that the whole purpose of this is so that we actually have someone who is an agency that is making sure that the products available to consumers, that the consumer is protected.

Ms. BEAN. Ms. Bowdler?

Ms. BOWDLER. A lot of the conversation in the hearing so far has been on everything that the CFPA would supposedly prohibit or ban from the market when, in fact, we think this is an opportunity to promote and advance really good products and make sure they get to the consumers. So I hope we can talk more about all the promotion and advancement that they are going to do as well.

Ms. BEAN. Okay. Mr. Shelton?

Mr. SHELTON. I would only add that I can give you many, many examples of, in the past, of how organizations like ours have talked to regulators, have talked to various associations about the kind of exploitation we have seen of our members and our constituents, and then very well, under the existing construct, there has been little to no response. We do need an agency that will specifically focus in on the issues of concerns of the consumers of the United States, not putting the banks and others first.

I can tell you stories about us taking our predictions about the foreclosure crisis 3 years ago to very high-ranking members of the Bush Administration, and very well, in each and every one of those agencies, we were told, and I will capsulize by saying that we would let the market work it out. And indeed the market working it out led to the crisis that we are still trying to get out of.

Ms. BEAN. Thank you.

I would also like to ask—first of all, I would like to concur. I think that is why so many of us do support the creation of a CFPA. But we also feel that those robust consumer protections that we are expecting them to create, that we should feel comfortable, then, that banks and thrifts that operate nationally should be able to operate under that single set of robust protections, which will allow streamlined compliance and reduce costs to customers.

Let me move to another question. Given the States' experience with nonbank actors, how large of an examination and enforcement staff would be needed at the CFPA to actively enforce the nonbank sector? I will start with Mr. Calhoun again.

Mr. CALHOUN. I don't have an exact number for you, but a substantial part of the problem as has been discussed today has been in the unregulated sector, and again, I think that there are ways, though, to encourage compliance and streamline this. CRL is an affiliate of self-help; 80 percent of our employees work solely on providing credit and expanding access to credit. So we will be subject to the CFPA, and we encourage it to be done on a streamlined basis.

I am concerned, though, about unlimited preemption because the power to act is also the power to not act, as we saw with the Fed, and the power to insulate abusive behavior. I have fears about putting all our eggs in one basket. And if one person authorizes a practice, it can prohibit anyone else, any State from providing any protections and wipe out existing protections.

Ms. BEAN. That is exactly what we are expecting the CFPA to do, to create a high standard that can apply universally and nationally for all, also recognizing that, even from testimony from some of the groups that are here today, many reports indicate that over two-thirds of the subprime mortgages that created the problem were done by nonbank lenders that were regulated by the States.

Let me ask, do you believe the CFPA would have the ability to actively examine and enforce consumer protection laws on both banks and nonbanks? And wouldn't it be more effective to put coverage where there hasn't been and leave those examiners that are already in place to do what they have been doing? Is he allowed to answer?

Mr. CALHOUN. I will be very quick. I think the bill is right in giving enforcement and supervisory, even for banks, to the CFPA, but to require careful coordination and to especially make sure for community banks that it does not create a regulatory burden.

Ms. BEAN. Thank you.

I yield back.

The CHAIRMAN. The gentleman from Minnesota.

Mr. ELLISON. Thank you, Mr. Chairman.

Let me pick up right there, Mr. Calhoun.

I have been in conversation with a number of community banks, and some of them have been concerned that they are going to get another layer of regulation. But isn't it also true that they are competing with people who haven't had any regulation, and therefore, CFPA could help level the playing field?

Mr. CALHOUN. I think community banks, including Self-Help, our financial institution lost a lot of their market share to people who were offering abusive products. Abusive products crowded out the good products, and quite frankly, they have gotten the least amount of assistance from the bailout. The community banks have been sort of in the middle, have gotten the worst of the competition, and the worst of the assistance from the bailout.

Mr. ELLISON. I saw some other heads nodding.

Ms. Bowdler, do you think that the CFPA could be beneficial to community banks?

Ms. BOWDLER. Yes, absolutely. Again, a lot of the products that are offered there, those are the kinds of—those are the kinds of products and practices that we want to promote. There is a lot of concern about the inefficiencies that this might create, but it is really hard to imagine less choices being available to our families or the market operating even more efficiently for our families.

Again, in my written statement I walk through how exactly that has been happening, but they have not had choices, and the market has not been working well for them. So this is an opportunity again to get those good practices and good products out there and give them a chance to compete, which they have not had.

Mr. ELLISON. Let me ask you this. There has been an argument out there that the CFPA should only apply to presently unregulated entities. I found a little information that I want to ask you about, and it suggests that while there is no question that independent mortgage finance companies were major players in the subprime marketplace, the affiliates of national banks and other insured depositories also played an important role. Indeed, HMDA data show that depository institutions and their affiliate subsidiaries originated 48 percent of the higher-priced loans in 2005 and 54 percent of the higher-priced loans of 2006. Can somebody help me understand what this means, for the record?

Mr. SHELTON. I can simply begin by saying it has been very difficult in the more recent present to tell the difference between the regulated financial services institutions and those that are unregulated. So, very clearly, we need a more robust oversight process that very well includes a consumer protection agency.

Mr. ELLISON. Ms. Burger?

Ms. BURGER. And I would also just say that even those, the financial institutions that were regulated, have regulators that were looking at them from the perspective of what was good for the institutions and not what was good for the consumers. We still need a consumer protection agency that actually looks at the products from the perspective of the consumer. And that is why they should be included.

Mr. ELLISON. Ms. Bowdler?

Ms. BOWDLER. Yes. That kind of structure actually allowed a bifurcated outreach strategy, especially to minority and low-income communities. So we saw an example—I read about it in my testimony—where in conversations with a major lender, we found that their subprime wholesale unit, which offered exclusively subprime products, 80 percent, 90 percent of their lending was going to African Americans, while their retail unit went predominantly to their white bank consumers. It allowed them to actually split these outreach—

Mr. ELLISON. Kind of a Jim Crow within one institution.

Ms. BOWDLER. And we have seen it in other whistleblower cases. In Wells Fargo *v.* Baltimore, there was a big New York Times article about this. Other places where we see that—employees are actually coming forward, much as Ms. Burger describes, saying, this was our strategy. As soon as we create loopholes, we are going to give people the opportunity to just shift the way they do business a little bit or shift their label.

Mr. ELLISON. And I just want to give a little voice to the point that Ms. Burger made which is that low-level employees are saying that we are enforced and incentivized to push more accounts, to not relieve people of unfair overdraft fees, and this is part of the issue that we need to consider.

I am running out of time. So I just want to ask this. Do you think that it is essential for the CFPA to have supervisory and enforcement powers in addition to rulemaking authority? Both the Fed and the OCC failed to exercise their powers with respect to consumer protection over the nonbank affiliates of national banks. How do we know that they wouldn't drop the proverbial ball again if they retain their supervisory powers?

Mr. CALHOUN. I think definitely yes. And particularly in light of the fact that, it hasn't been discussed today, this bill does not have a private right of action. CFPA rules cannot be enforced by individual consumers. We think that should be changed, but it makes it all the more important that you have as many other enforcement mechanisms as possible.

Mr. ELLISON. Anybody else? I think I am done.

The CHAIRMAN. The others, we encourage you to answer in writing. And I also want to note while we have general leave, approximately 100 professors of consumer law and banking law from universities from a large number of States have submitted a letter in support of this agency and some of the specifics, and it will be part of the record.

And the gentlewoman from California will be our last questioner.

Ms. SPEIER. Thank you, Mr. Chairman.

I guess I have one overriding question. At what point does the bill become so watered down that it is not worth pursuing? And I ask that question not facetiously, because one of the interests that are being promoted is that we preempt all State regulation. And while the bill right now does not have preemption, if we move in that direction, is that going too far? At that point, do you walk away from the table and say, this isn't a consumer-friendly bill?

Mr. CALHOUN. I will start with that. The bill currently pushes preemption back close to what it was in 2004. So the one issue is, do you roll back some of what many of us believe was excessive preemption that led to the problems that we have now, not just the mortgages, but in credit card overdraft.

There is a second question that there are proposals to actually increase the amount of preemption that we have in the bill and, specifically, to make any rule of the CFPA preemptive, even though most of its authority comes from statutes such as truth in lending which today are not preempted. States are allowed to build on those protections. And I think, importantly, truth in lending is a good example. There has been virtually no State activity, although it is permitted, because you have comprehensive regulation. States like North Carolina moved in and Georgia attempted to move in, in predatory mortgage lending, due to the failure of the Federal regulators to take action. When Federal regulators have taken action, typically States adhere to those standards because they are beneficial to the community in that State.

But I think that is the line that it crosses. If it becomes fully preemptive, it undercuts current protections in a wide array, consumer car purchases, furniture purchases across-the-board, payday lending, all of that could be swept aside by a single administrator.

Ms. SPEIER. Let me move on to payday lending, because in the bill, it prohibits the CFPA from establishing a usury limit. Now, I feel pretty passionately about that issue, I realize. But nonetheless, why would we want to tie the hands of a consumer protection agency from actually putting in place a usury limit of let us say 36 percent?

Mr. CALHOUN. I think again that is particularly troublesome if you put it in the context that the consumer protection agency could wipe out other State protections, for example, in the field of payday lending. Then the usury prohibition in the bill becomes even more problematic.

Ms. SPEIER. It doesn't offend you that we are tying the hands of the consumer protection agency on one of the biggest financial boondoggles and most egregious conduct by the financial services industry and basically saying that this consumer protection agency can't even deal with that issue? Anyone else have any—

Mr. SHELTON. Let me just say, on behalf of the NAACP, we were probably more in agreement with you that very well—we have seen so much exploitation across the country and what happens in local communities where we don't have a very clear standard set forward on to prevent the exploitations that we have experienced in the past. So very well, it does raise concerns, and it is something that we would love to see discussed further.

Ms. SPEIER. I yield back.

The CHAIRMAN. If the gentlewoman would yield her remaining time—and I appreciate her raising that question. While there is no usury flat prohibition, I believe that you could not deal with unfairness without taking into account duration, interest rate, etc., and I believe the legislation should be clarified to make it clear that that could be an element in an overall judgment this was an unfair and abusive practice. So that will be.

Ms. SPEIER. I have an amendment in mind.

The CHAIRMAN. It wouldn't be a flat across-the-board thing, but it is clearly an element—as with our credit card bill. Interest rates—we can set a flat number, but interest rate calculations were part of the bill in terms of deciding what was fair and not fair, retroactive interest rate increase, etc. So I agree that is an important point. I thank the witnesses and the members, and I ask the second panel to come forward.

Let us move quickly, please. You can have all the conversations outside. Will the witnesses please take their seats? I appreciate the patience of the witnesses. And we will begin with Mr. Michael Menzies, who is the president and CEO of the Easton Bank and Trust company, testifying on behalf of the Independent Community Bankers of America.

Mr. Menzies?

STATEMENT OF R. MICHAEL S. MENZIES, SR., PRESIDENT AND CHIEF EXECUTIVE OFFICER, EASTON BANK AND TRUST CO., ON BEHALF OF THE INDEPENDENT COMMUNITY BANKERS OF AMERICA (ICBA)

Mr. MENZIES. Chairman Frank, thank you so much.

I am Mike Menzies, president and CEO of Easton Bank and Trust in Easton, Maryland. We are a $160 million State-chartered community bank. And I am proud to be chairman of the Independent Community Bankers of America representing our 5,000 community-bank-only members at this very important hearing. There are 8,000 community banks in this country, Mr. Chairman, most of which are below a billion dollars in total assets.

Community banks do not have 50,000 ATMs; 5,000 branches; 100,000 employees as their primary assets. They have only one real asset that they own, their relationship with their customer. That relationship must be strong enough to overcome overwhelming odds regarding product prices, product offerings, convenience and size and economies of scale.

The only thing I can do to compete in this industry is to serve my customer better than the competition. That means I must serve and protect and know and own that relationship. If I don't do that, then I lose the only asset which produces a return to my 100 stockholders, my associates, and my community.

Community banks do not have geographic reach into every State of the land or huge legal departments that operate under the theory that forgiveness is easier than permission. We cannot afford to place consumer protection beneath any other core value. Community bankers across the country have made it clear that a new regulator for them is not the answer to protecting consumers. Adding to their regulatory costs and burden will not help community bankers protect consumers better and will make it harder for community banks to offer the variety of competitive products at better rates and terms that customers expect and deserve.

To protect consumers, Congress should address the overleveraged, "too-big-to-regulate," "too-big-to-fail" firms whose concentration risks have cost taxpayers over $10 trillion in net worth. Congress should also address the many nonfinancial banking institutions that are unencumbered by most forms of government regulation or accountability.

An important part of the solution to the "too-big-to-fail" problem is contained in the Bank Accountability and Risk Assessment Act of 2009, introduced by Representative Gutierrez, and we urge the committee to incorporate this measure into any broader financial regulatory reform proposal it considers in the future.

Mr. Chairman, we deeply appreciate the steps you have taken to improve the CFPA, most notably by removing the plain vanilla product mandate and the reasonableness standard which would invite litigation and create tremendous uncertainty. To be sure, community banks offer a consumer basic products whenever it is appropriate. But simpleness as a doctrine should not be promoted at the expense of a consumer's unique and individual needs.

ICBA remains very concerned with the overall approach. While we appreciate efforts to encourage coordination, we object to the separation of consumer protection compliance from safety and soundness regulation. For community banks, the prudential regulators have done an excellent job of enforcing consumer protection in a way that protects the safety and soundness of the bank and the integrity of its customers.

Also, an agency with the sole focus of consumer protection will not likely write rules for a community bank that adequately considers safety and soundness. If a bank regulator is not equally interested in safety and soundness of the lender, it is likely to promulgate unnecessarily burdensome or contrary rules to those issued by the prudential regulator.

The chairman's discussion draft also modifies the leadership structure of the CFPA, creating an autonomous director while establishing an advisory board with essentially no authority. ICBA is concerned with this approach which lacks substantive checks and balances and provides no meaningful voice for community bank viewpoints in the agency's decision-making process.

In conclusion, ICBA agrees that a lack of sufficient regulatory oversight, particularly among unregulated mortgage lenders and "too-big-to-be-regulated" entities led to significant abuses of consumers. However, we disagree with the response that places community banks into an entirely new regime with only vague limits and checks on its powers instead of focusing on the real regulatory gaps and augmenting the existing system. We really look forward to working with this committee to improve our financial system to better protect consumers while not restricting the ability of community banks to serve their customers.

Thank you, Madam Chairwoman.

[The prepared statement of Mr. Menzies can be found on page 130 of the appendix.]

Ms. BEAN. [presiding] Thank you for your testimony and we will now go to Mr. Andrew Pincus from Mayer Brown on behalf of the U.S. Chamber of Commerce.

STATEMENT OF ANDREW J. PINCUS, PARTNER, MAYER BROWN LLP, ON BEHALF OF THE U.S. CHAMBER OF COMMERCE

Mr. PINCUS. Thank you, Madam Chairwoman.

I want to thank Chairman Frank and Ranking Member Bachus for the opportunity to testify here on behalf of the U.S. Chamber of Commerce. The Chamber strongly supports the goal of enhancing consumer protection. Consumers need clear disclosure and better information, they need more vigorous, effective enforcement against predatory practices, and they need the elimination of regulatory gaps that allow some financial service entities to escape the regulations that are applicable to their competitors.

The Chamber opposes H.R. 3126 because it believes the bill will have significant and harmful unintended consequences for consumers, for the business community, and for the overall economy. Last week, the Chamber released a study by Thomas Durkin, an economist who spent 20 years at the Federal Reserve. He concluded that H.R. 2136 would reduce consumer credit and would likely increase the cost of credit that is available. Small businesses' access to credit would be hurt as well.

We appreciate the recognition in Chairman Frank's September 22nd memo of a number of the specific concerns that the Chamber has raised about H.R. 3126. But the difficulty of transforming principles into legislative language in this very complicated area of the law and the need for careful assessment of the impact of proposed provisions is demonstrated by the fact that the changes made in the revised bill do not resolve the concerns that the Chamber has expressed. Let me give a few examples. One critical issue is whether ordinary retailers and merchants that extend credit to their customers were covered by the original bill. The revised bill does provide that the agency will not have authority regarding credit issued directly by a merchant or a retailer. But a business that merely accepts credit cards could still be classified as a covered person on the ground that it indirectly engaged in financial activity, which is one of the grounds for a covered person under the bill, or that it was providing a material service to the credit card network.

Accountants, lawyers, and tax preparers have expressed concern about their status under the bill. The revised bill does contain an exemption for these professionals but provides that the exemption shall not apply to the extent such a person is engaged in the financial activity or is otherwise subject to the existing Federal consumer laws. That means that any activity by an accountant or a lawyer that falls within the broad financial activity definition, for example, providing tax planning, advice in connection with estate planning would trigger the applicability of the statute.

The revised bill's exemptions for real estate brokers and auto dealers suffers from the same flaw; the exemptions don't apply if the Realtor or the auto dealer is engaged in financial activity or is otherwise subject to the laws.

In addition, even the limited protection provided by these exemptions doesn't cover activities in which these individuals routinely engage. For example, the real estate broker exception doesn't include negotiations relating to financing. And the auto dealer exemption does not apply to leased transactions and excludes all activities relating to the arranging of financing. That means auto dealers likely will be covered by the statute for all activities other than all cash vehicle sales.

Another aspect of H.R. 3126 that provoked considerable concern is section 132(b), which would have required businesses to determine the extent to which consumers comprehended particular information. Although that provision has been removed from the revised bill, new language has been added to section 138.1 making it unlawful for any person to engage in any unfair, deceptive or abusive act or practice. This new provision imposes broad liability on anyone, not just a covered person, any time there is a determination in hindsight that the person's conduct was unfair or deceptive or abusive, even if there was no regulation requiring a particular disclosure or prohibiting the particular practice.

The revised bill does not include the provision of H.R. 3126 that imposed the plain vanilla product requirement, but the agency could impose that very same requirement through its broad authority to prevent abusive acts or by invoking its fair dealing authority. And States would be free to impose a plain vanilla requirement even if the agency did not do so.

Next, separating the regulation of financial products from safety and soundness threatens consumers as well as the stability of the financial system. Although the bill creates a dispute resolution process, that process doesn't apply to the adoption of regulations by the agency which would still be entirely separated from the safety and soundness regulators.

And finally, at a time when harmonization has been identified as a priority by all stakeholders, the proposed agency will do the opposite. It rolls back 150 years of banking law by subjecting national banks to State regulation, and it gives the States independent power to interpret and enforce the new separate standards, even if they adopt an interpretation different from the agency's. Again, thank you for the opportunity to testify, and I look forward to answering the committee's questions.

[The prepared statement of Mr. Pincus can be found on page 139 of the appendix.]

Ms. BEAN. Thank you.

We will now move on to Mr. Yingling, president and CEO of the American Bankers Association.

STATEMENT OF EDWARD L. YINGLING, PRESIDENT AND CHIEF EXECUTIVE OFFICER, AMERICAN BANKERS ASSOCIATION (ABA)

Mr. YINGLING. Thank you, Madam Chairwoman.

When I testified here in July, I asked the committee to look at this issue not only from the point of view of consumers, whose concern should be paramount, but also from the point of view of community banks, the great majority of which had nothing to do with causing the financial crisis, which are struggling with a growing mountain of regulatory burdens.

Recently, I asked the ABA staff to determine the total amount of consumer regulations to which banks are subjected. The answer is 1,700 pages of fine print, and that is just in the consumer area. Since the median-sized bank has 34 employees, that means the median-sized bank has 50 pages of fine print for each employee. That means that half the banks in the country have more than 50 pages per employee in the consumer area alone.

I want to express our appreciation for the consideration many members of this committee have given to the situation of traditional banks and to the unnecessary burden that would be placed on these banks.

While there are many causes of the financial crisis, failures of consumer protection in the mortgage arena certainly contributed. As Congress moves to strengthen consumer regulation, however, it is important to focus on what the problem areas were. The two areas that have been identified as needing reform are the need for more direct focus by regulators on consumer issues and the need for more enforcement on nonbanks. The ABA agrees that reforms are needed in these two areas. On the other hand, in our opinion, no real case has been made for changes to other areas.

The first area is requiring additional enforcement on banks and credit unions. While the argument is made that Federal regulators should have developed stronger regulations and sooner, there is little indication that once the regulations are issued, they are not enforced on banks and credit unions.

The second area is giving the CFPA vast new powers. It is not clear why new authorities are needed. As has been talked about earlier this morning, the Fed had the mortgage regulatory authority and has the clear authority to address credit card issues, which is already done, and overdraft protection, which is in process. In fact, the expanded use of UDAP by the Fed creates a powerful tool in addition to specific consumer laws.

The CFPA, unfortunately, goes well beyond addressing the two weaknesses identified. The Administration's proposal unnecessarily imposes new burdens on banks and creates an agency with vast new powers. We are pleased that the chairman's discussion draft addresses several issues the ABA has raised and seeks to lessen the additional burdens on community banks.

One of our major concerns with the CFPA as proposed is that it would not adequately focus on the nonbank sector where the subprime mortgage crisis really began. The discussion draft rightly focuses regulation more on nonbanks than the original proposal did.

The ABA still has major concerns in three areas.

First, the ABA supports the preemption of State laws under the National Bank Act. We believe, without such preemption, we will have a patchwork of State and local laws that will confuse consumers and greatly increase the cost of financial services.

Second, as I just stated, there has been little justification for the broad new powers given the CFPA. The draft removes two of these explicit powers, plain vanilla products and requiring communications to be reasonable.

However, even with those changes, the proposed CFPA will be given unprecedented powers. Vague legal terms, such as "abusive" and "fair dealing" will create great uncertainty in the markets because no one will know what the new rules of the road will be. This will undoubtedly cause firms to cut back on the extension of credit and to avoid offering new products.

From the broader perspective, the delegation authority of the CFPA is so vast that it renders all previous consumer laws enacted by Congress, including the recently enacted credit card law, mere floors. Several members of the committee have rightly raised concerns about this broad delegation.

Third, the ABA opposes the creation of an entirely new agency on the fundamental principles that: first, you cannot separate the regulation of products from the entity; and second, that safety and soundness and consumer protection are too intertwined to be separated. ABA is committed to working with Congress to strengthen consumer protection while avoiding undermining the availability of credit and imposing new unnecessary costs on consumers and financial service providers. Thank you.

[The prepared statement of Mr. Yingling can be found on page 151 of the appendix.]

Ms. BEAN. Thank you.

And now we will hear from Mr. Bill Himpler, executive vice president of the American Financial Services Association.

STATEMENT OF BILL HIMPLER, EXECUTIVE VICE PRESIDENT, THE AMERICAN FINANCIAL SERVICES ASSOCIATION (AFSA)

Mr. HIMPLER. Thank you, Madam Chairwoman, and members of the committee.

I appreciate the opportunity to give the finance company perspective on the proposal to create a CFPA. In light of the revisions put forward last week, I would like to thank the Chair, Mr. Frank, for his willingness to listen and consider different perspectives on this very important proposal.

At the same time, we have noted that Mr. Frank was quoted as saying last week that Congress would enact death panels for nonbanks. I think this quote is indicative of the sense in Washington that many have that State-regulated correlates to unregulated. Therefore, I would like to take a minute to set the record straight regarding the regulation of consumer finance companies.

Finance companies have been around for over 100 years. They come in many shapes and sizes. Some are independently owned and specialize in personal loans to consumers and businesses. Others are captives that provide financing to vehicles or other products manufactured by their parents, and I can assure you that finance companies are already heavily regulated.

In addition to being subject to Federal consumer protection laws, such as TLA and ECOA, finance companies are licensed and regulated by States and abide by the consumer protection statutes in all the States in which they do business. Like banks, finance companies undergo regular and vigorous examination by State regulators. These companies have been successful at meeting the credit needs of communities in part because they are subject to oversight by State regulators who have familiarity with local situations and issues faced by lenders and consumers. State regulators frequently are among the first to identify emerging issues, practices or products that may need further investigation.

AFSA strongly supports the efforts by this committee to improve consumer protections for financial service consumers. However, we do have a philosophical difference about how to achieve this goal and remain concerned that the proposal would reduce and perhaps eliminate a critical source of consumer credit for the following reasons.

First, the CFPA would try to fix what is still working and use a one-size-fits-all approach, as mentioned by Mr. Scott, to financial service products. For instance, it makes no sense to compare terms such as APR for a 30-year fixed mortgage with those of short-term installment loans used to buy a new washer or dryer. Many of the companies that would be subject to these intensified requirements, greater restrictions, and higher compliance costs would be those who didn't contribute to the mortgage crisis at all.

Second, there is no guarantee that the CFPA would be better able to weed out bad practices in the financial services sector than existing agencies. Policymakers should not be tricked and trapped into thinking that more bureaucracy is what is needed to improve consumer protection.

What is more, putting an untested, inexperienced agency in charge of consumer protection for the entire financial marketplace could exacerbate existing problems rather than reducing them.

Third, if the CFPA were to become a reality, financial services customers are likely to have less borrowing flexibility, even with the elimination of the the plain vanilla requirement. The new regulator would still retain expansive rulemaking authority and the ability to determine allowable consumer products.

Under CFPA's jurisdiction, finance companies will face considerable compliance costs that will get passed on to borrowers, imposing a new tax on consumers at a time when they can least afford it.

Fourth, AFSA believes that consumers will be better served by a regulatory structure where prudential and consumer protection oversight is housed within a single regulator. FHFA Director James Lockhart recently cited the separation of these functions as one of the primary reasons for the failure of Fannie and Freddie.

For the reasons I have just stated, AFSA believes the creation of CFPA will not fulfill the goal of improving consumer protection for financial services customers. It is hardly in the consumers' best interest to add new layers of bureaucracy, reduce credit choices, and raise prices for financial services.

In addition, I would like to point out that if the proposal focuses on nonbanks, it could reduce and perhaps eliminate many finance companies, which are a critical source for credit for consumers and small businesses. Take for example, an unanticipated car repair. Vehicles play a critical role in sustaining employment because most Americans still use cars to get to work. Without the ability to borrow money from finance companies, repairs necessary for such transportation may not be possible for many less-advantaged Americans.

Ultimately, if installment lenders, auto lenders and other finance companies are required to shoulder much of the compliance burden resulting from CFPA, it will undoubtedly affect their ability to provide safe, convenient, and affordable loans just as we are starting to get the economy back on track.

Thank you, Madam Chairwoman, and I look forward to answering any questions.

[The prepared statement of Mr. Himpler can be found on page 112 of the appendix.]

Ms. BEAN. Thank you all for your testimony.

And now to begin questions, I will turn to the gentlewoman from California, who is recognized for 5 minutes.

Ms. WATERS. Thank you very much.

And I thank our panelists for being here today.

I don't know if you have heard about the fact that, in my office, we got very much involved in loan modifications because we were receiving so many complaints. Not only complaints from my district, but everywhere I go, whether it is at church or at a social event, American Airlines that I travel, the workers there, everywhere, I am bombarded with people who are in mortgages that they can't afford for whatever reason. They lost their job. They got into a predatory loan. And we are overwhelmed because we do help. We help connect people with servicers. We help to interpret to servicers the problems that people have. We get waivers from constituents so that we can talk about their loans and help guide the servicers and make sure the servicers are taking everything into account.

But I just want to share something with you, why I am so exercised about having a consumer financial protection agency. I want to tell you about Mrs. Himpler. This is one of the hundreds that we are working with. She is a 77-year-old woman, of course, who called our office. She has a fixed income of $1,025 a month, which she earns from a widower's pension. When she took out the loan 2 years ago, her income was only $950 per month. She was approached about refinancing her home. Her home was worth $248,000 at the time. I guess they appraised—she owed rather, $248,000. The home was appraised at $480,000. The loan amount was $336,000. They gave her a refi, and they charged her $70 a month for her refi, and this is the way it operated. It was a variable rate mortgage. She pays $70 a month in 2011. Her payment will reset to $2,973.44 a month. The loan will reset again in 2012 to $3,067.84 a month. And finally the loan will reset a third time to $3,825.20 a month in 2017. What are we supposed to do with this kind of mess?

Mr. Himpler, you represent GMAC Financial as part of your industry group. This was one of those loans that was made by Paul Financial. It was one of those warehouse mortgage lenders. But they sold it to GMAC. I guess GMAC and others are happy to accept these kinds of loans because they know that they are going to get the house. They know that they are eventually going to get this house, that this 77-year-old woman will die before she is even able for the third reset. What are we supposed to do, Mr. Himpler? What are we supposed to do?

Mr. HIMPLER. Well, let me ask first, did I hear you say your constituent's name was Ms. Himpler?

Ms. WATERS. No. I am sorry. That is your name.

Mr. HIMPLER. I just thought it was a really interesting coincidence.

Ms. WATERS. No. Please—that is a mistake. But that is not the point. The point is, this is a predatory loan that I am confronted with time and time again, and you come here to tell us about why a consumer protection finance agency is not wise thinking. What should we do?

Mr. HIMPLER. Our position at AFSA is that finance companies face heavy regulation at the State level. At the State level, consumer credit administrators in 2008 alone have brought 7,000 enforcement actions in the mortgage sector alone, as compared to what Mr. Calhoun made mention of with respect to OCC enforcement actions taken to the Attorney General, the Department of Justice. We think that, as my colleague Mr. Calhoun made mention, that you have very strong State statutes to protect against the very abuses—

Ms. WATERS. My time is out. And I see where you are going. No, we are not—I am not here to complain about the State statutes. I am here to talk about trying to protect consumers from the Federal—I want you to help me with this loan. I want you to get the servicer on this loan on the phone with me and Ms. Jones, who is

77 years old, who has been—spent $70, is now going to reset and reset and reset. I want you to help me modify this loan. That is all I want from you today. Thank you.

Ms. BEAN. The gentleman from Texas is recognized for 5 minutes.

Mr. HENSARLING. Thank you, Madam Chairwoman.

I guess I want to start out with a rhetorical question. I heard that one of my colleagues said we really have nothing to fear from the CFPA and used the comparison to the FDA allowing statin drugs on the market, that even though they might have had the power to keep them off the market, they allowed them. I think I would be interested to actually conduct the research to find out how many people might have actually lost their lives waiting for the FDA to approve that drug.

Prior to coming to Congress, I was a member of the board of directors of the American Cancer Society in Dallas, Texas. And I can assure you there are a number of families in the Dallas area who are convinced they lost their loved ones waiting for the FDA to finally approve cancer treatments.

So I also am curious, if we had a CFPA, how many homes would be lost, how many small businesses would be compromised as we sit around waiting for the CFPA to decide whether or not people have the liberty in a free society to decide what kind of credit cards, home loans, and auto loans they have.

And that is a rhetorical question.

I have heard some on the other side of the aisle earlier today say that the primary reason or certainly a significant reason that we have economic turmoil is because people I suppose in financial institutions represented by your organizations steered consumers into risky products because there was high profit to be found.

I guess the first question I have is, how much more profit do you make on a defaulted loan as opposed to one that remains in compliance?

Mr. Menzies, let us start with you. When the customer defaults, do you make more profit?

Mr. MENZIES. Pretty simple answer, you don't make any money on a defaulted loan, and you lose a relationship. So when you underwrite a loan, you don't underwrite a loan with the hopes that it will default and you can go collect legal fees and that sort of thing.

But, Congressman, let's understand what really caused the crisis. Do we believe that it was community banks and lenders who live with the people that they lend to? They go to Rotary with them. They sit on the hospice board with them. They live with them.

Underwriting products and sticking them into SIVs on Wall Street that are then rated by rating agencies that don't know what they are looking at and selling to investors that don't understand what they are buying; do we really believe that the community banking industry was a player in that game?

Mr. HENSARLING. Mr. Menzies, speaking for myself, the answer is "no."

Given the limited time I have, let me skip ahead. I think I have heard in your testimony—I don't have it right in front of me—that not withstanding the chairman's new bill, that you still had concerns—I suppose we are no longer in the mandatory plain vanilla, but maybe possibly highly suggested plain vanilla. I am paraphrasing what I think I heard in your testimony. Do you still have concerns that the regulator will essentially steer you to standardized products?

Mr. MENZIES. I don't think we have done a very good job of explaining to this committee and to Congress that community banks are not in the product business. We don't sell products.

Mr. HENSARLING. So is it fair to say that you—

Mr. MENZIES. We try to create solutions. And if this legislation takes away our ability to create a solution to satisfy the need of a consumer, if it is a product-driven approach to dealing with this problem, we are going to lose the competitive advantage that community banks have to create solutions for people in need.

Mr. HENSARLING. So is it fair to say that you still retain that fear?

Mr. MENZIES. Absolutely.

Mr. HENSARLING. I met with some community bankers over the congressional recess in August. One described to me a very customized—you don't like the term "product," but I don't have another term at the tip of my tongue—a very customized product for a lady who was trying to buy school supplies for her children as the children returned to school. And they customized a product totally for her, and I don't remember all the details, somehow tied to the paycheck, 6-month payout, different provisions, that would allow her to push the loan back.

My community banker in Kaufman County, Texas, said under this legislation, I don't think I could have offered that product. And so I am describing, I suppose, a relationship-driven credit opportunity that you would fear might disappear under this legislation.

Mr. MENZIES. We believe we have to maintain the flexibility to offer solutions and choices to small businesses and to consumers. We do not believe you can standardize or vanilla-ize, or whatever, financial products and serve the needs of America's communities.

Mr. HENSARLING. Thank you, I am out of time.

Ms. BEAN. The gentleman from North Carolina, Mr. Watt, is recognized.

Mr. WATT. Thank you, Madam Chairwoman.

Let me start by expressing publicly what I have expressed to a number of your representatives privately, which is just an absolute sense of exasperation for the positions that you all have taken on this, which really have been—we are going to oppose this and oppose it and oppose it. And we are going to make all kinds of discussions for not doing this. We are going to lay down on the road and we are really not going to come and sit down and talk about how to resolve the issues. There are some issues that I think need to be resolved and I just am just exasperated at the approach the industry has taken on this.

And here today, you all tell me, Mr. Yingling, that there is no real case for change here. After all of the experiences that we have been through that demonstrate the case for change, to hear testimony that says there is no case for change having been made—

Mr. YINGLING. Congressman, I never said that.

Mr. WATT. —it is exasperating to me.

Mr. YINGLING. I never said that.

Mr. WATT. Go back and listen to what you said.

Mr. YINGLING. No, that is not what I said.

Mr. WATT. I am not going to get into an argument. Let me tell you I hear you all say that you are concerned about one-size-fits-all, but there is not but one size to safety and soundness. When we say protect consumers, there is no size differential that we are talking about here for community banks.

If the shoe doesn't fit, then you won't wear it. Just like in safety and soundness, if the shoe doesn't fit a particular bank, if you are providing services and nothing is going wrong, the notion that behind every tree there is some big boogeyman that is going to make you do something different is just—I don't understand that. The standard that says go out and protect consumers is no more one-size-fits-all than a standard which says go out and assure safety and soundness in the industry.

The double standard that you are talking about that would require this agency to have some kind of oversight panel when there is nothing that exists with the other regulatory agencies is just beyond me. I don't understand that.

We put—the proposal puts a council there that they consult with. There is no veto authority that anybody has if the Fed determines that you are taking some kind of action that is unsafe and unsound. Yet you would continue to make this agency a stepchild in the whole regulatory structure. I think that is exactly what the public is saying is unacceptable. And I don't understand what your position is.

You tell me there are 1,700 pages. Well, let's write into the authority of this agency the authority to go in and review those 1,700 pages and reduce them.

Part of the reason we have 1,700 pages now is because you have consumer protection spread out all over every agency in the regulatory framework. You say it is acceptable to go out and impose this agency on non-banks, yet something is wrong with the agency when we try to do exactly the same thing for bank entities. I don't understand this, and I am exasperated by it. And I am disappointed.

Go ahead and say whatever you want to say in response to that, but I can't tell you how exasperated I am with the posture you all have taken on this. With consumers out there in the public demanding that we do something to protect them, you all are saying that we ought to be catering to your industry still. And I think that is unacceptable.

Ms. BEAN. Time has actually expired.

Mr. YINGLING. May I respond?

Ms. BEAN. A brief response.

Mr. YINGLING. Well, first, Congressman Watt, there is nobody who has worked harder in this Congress to try to resolve these kind of issues than you have. So we don't want you exasperated.

Mr. WATT. Which is exactly why I am exasperated.

Mr. YINGLING. I know it is. If you interpreted what I said as that changes are not needed, that is not what we are saying. What I am trying to say is that the focus of such change needs to be on the two factors that really seem to cause the problem primarily.

One is a lack of focus within the regulatory agencies on these issues, which is really what happened.

Two, that the enforcement part of it, the enforcement part of it, was on the non-bank side, not on the bank side.

What I said which was, I am afraid easily misinterpreted, was if you look at the actual authority, the actual authority wasn't the problem. The Fed had the HOEPA authority; the regulators have the authority Under Unfair and Deceptive Practices, UDAP, to address all these issues, and they haven't. So it is an issue of focus, not an issue of powers, in my opinion.

Ms. BEAN. Time has expired.

The gentleman from Minnesota, Mr. Paulsen is recognized.

Mr. PAULSEN. Thank you, Madam Chairwoman.

Mr. Menzies, maybe I can start by asking you a question. During the debate that we had in the committee here on the Credit Card Act, there was significant discussion and actually concern on both sides of the aisle regarding possibly accelerating the implementation of the deadlines that were put in the bill.

I was working on an amendment with Mr. Moore of Kansas to make sure there was proper time to implement the legislation as it went forward.

Now, even though the law is on the books and the Federal Reserve Board, just on Monday now, introduced 800 pages of proposed rules, there is talk of Congress accelerating these dates and deadlines even further.

Since we are talking about consumer products today and credit products, from your perspective what does speeding up these deadlines mean to small issuers that have had concerns about the legislation as it has been moved forward?

Mr. MENZIES. Congressman, the simple answer is that it could cause small issuers just to exit the business and sell portfolios to the larger issuers, which would create more consolidation in the industry, which we don't believe is healthy.

The more detailed answer is that the new legislation is complex and comprehensive when it comes to dealing with changing the statements, changing the disclosures, testing the new systems. It represents a major reconfiguration of the credit card requirements. And we are hopeful that community banks can make it by July of next year, which, if I am correct, is the currently scheduled kick-in date for this new legislation.

If the legislation is moved forward too quickly and community banks are unable to reconfigure to deal with an advancement of the legislation, then that part of the business could result in them saying, well, I will just exit the portfolio business and sell it to a larger aggregator, which we don't belive is in the interest of the consumer.

Mr. PAULSEN. Well, I thank you for that and that is something we will have to pay closer attention to on this committee. In particular, I know the chairman has made some announcement recently that he may move the deadlines up further. But to think of losing smaller issuers in terms of exiting the business altogether, I don't think that is good from a competitive standpoint or more consolidation as well.

I remember the regulators who sat at that table were testifying specifically about the implementation dates that are on the books already, and so I think we need to be really prudent and cautious about that.

Mr. Yingling, maybe I can just offer you an opportunity, we kind of ran out of time on your last series of questions there, but you referenced focusing on two different factors: the lack of focus that was currently going on in the regulatory environment as well as the enforcement side.

Can you expand a little bit about the enforcement side, and right now with the proposal of CFPA sort of having separation of enforcement versus the oversight?

Mr. YINGLING. It seems to me there is a lot of consensus around the fact that there is not—

Mr. GREEN. Would you pull your microphone a bit closer, Mr. Yingling?

Mr. YINGLING. It wasn't on—that there was not an adequate focus on consumer issues. And if you would look at the history, particularly the history of what caused this crisis, you can go back to a point in time and say, if the Fed had implemented HOEPA in an aggressive fashion, with the powers in HOEPA, from the consumer side we would not have had the degree of problem we had.

One of the weaknesses that the Fed had to face at that point was that HOEPA gave them at the Federal level no enforcement over the non-banks. So with the mortgage brokers, even though HOEPA technically would have applied to them, the enforcement would have been left to the State level. And in that case, we know that the enforcement was inadequate.

So if you look at that history, it seems to me that you draw the conclusion that the problem is a lack of focus at the Federal level on consumer issues, and an inability to ensure enforcement at the State level. In many cases, there is good State enforcement but, clearly, in the mortgage area there was not.

What I was attempting to say in my testimony—and maybe didn't say it very well—was I don't think the case has been made that there aren't enough powers out there. The regulators have all the laws that you all have enacted, and there are a lot of them, the 1,700 pages of regulations I talked about. Plus they have a new aggressive tool that the Fed used in the credit card case, the Unfair and Deceptive Acts and Practices. You combine those, then I think that the power is there; and if it is not, you all can enact new laws.

So what I am trying to say is, if you focus on the problems, the problems are a lack of focus at the Federal level and a weakness in certain mechanisms for enforcing at the State level.

Ms. BEAN. I will now recognize myself for 5 minutes.

My first question is to Mr. Yingling in follow-up to Congressman Hensarling's question about what does one earn more or less relative to a delinquency versus a foreclosures?

My question is in relation to servicers. I certainly agree with Mr. Menzies's contention that community banks aren't going to earn more in that situation. But can you please comment on how much more servicers make servicing a delinquency or servicing delinquency versus foreclosure?

Mr. YINGLING. I don't know the full answer to that, Madam Chairwoman. I would have to come back to you. I do think we have issues, and servicing was designed for servicing. And nobody ever anticipated—unfortunately, they should have—that servicing would be doing what it is trying to do today, which is to rework literally millions of loans. We all know that—

Ms. BEAN. Let me interrupt you and ask you this way: Are you saying that there aren't occasions where servicers are making more when property is foreclosed than if they continue to service them in delinquency?

Mr. YINGLING. No. I think the servicing process has a lot of incentives and nooks and crannies and bottlenecks, because it wasn't set up for this.

Ms. BEAN. So you have no knowledge of how that compares to some of the incentives that were put in place by the Administration to incentivize loan modifications?

Mr. YINGLING. Not off the top of my head, but we will get you that.

Ms. BEAN. Let me move to Mr. Pincus.

Are you aware of Federal consumer protection laws that set a nationally uniform standard for nonfinancial-oriented products that the States cannot exceed?

Mr. PINCUS. Yes, Congresswoman. I can think of two off the top of my head: one, the Consumer Product Safety Commission statute, which does preclude State action when it acts with respect to some kind of a safety concern; and two, the National Highway Traffic Safety Administration, NHTSA, also with respect to auto safety issues, has a preemption standard.

Ms. BEAN. So having nationally uniform standards is something that has been done before, and, by not rolling back those same protections in the financial arena wouldn't be unprecedented.

Mr. PINCUS. Yes, it would. And just to comment on some statements earlier, I think this bill moves way back from any standard of preemption in recent times for the national max. It is not close to what was in effect before 2004. There is much less Federal uniformity under this approach.

Ms. BEAN. Thank you. I yield back and I now recognize the gentleman from my neighboring district in Illinois, Congressman Manzullo.

Mr. MANZULLO. Thank you, Madam Chairwoman.

I look at you four, and some people think that the existing regulatory agencies are very cozy with you and give you all kinds of passes, are not concerned about the thousands of hours that you may spend in audits, and think that organizations like the FDIC give you a pass on soundness and safety, such as the latest one requiring assessments 2 years in advance and destroying liquidity within community banks.

I say that facetiously, because, being very close to the community banks back home, which had not been a problem and did not cause this meltdown, all of a sudden we see that simply by setting up a brand new agency, that everything is going to be resolved.

In fact, in the testimony that took place by Mr. Calhoun earlier, he already said there are enough laws that are on the books and it is simply a matter of enforcement.

So my question is, just because a so-called new agency would be independent, what makes people think that they would be any more prone to enforcing so-called consumer issues than, for example, the Fed, which had the power to outlaw 2/28 and 3/27 mortgages and the power to require underwriting standards of having written confirmation of a person's income? Why would things change? Who would these new regulators be?

Mr. Menzies, welcome back. I think this is the third time I have seen you here. And you have been an excellent witness on behalf of the Independent Community Bankers Association. Do you understand the tenor of my question?

Mr. MENZIES. I hope so, Congressman.

Mr. MANZULLO. Could you pull the microphone closer?

Mr. MENZIES. As you know, Congressman, I get married on Saturday. I am going to understand the meaning of living by new rules.

But I would agree that the community banks of this Nation not only didn't create the train wreck, but if you had had the opportunity to sit through my safety and soundness exam 2 months ago with 7 members of our board of directors and receive the FDIC's report on safety and soundness and compliance and CRA and everything else, you wouldn't think that they are passing us over, or cozy, or anything like that.

Mr. MANZULLO. That is precisely—

Mr. MENZIES. They have taken their responsibilities very, very seriously. And that is one of the reasons that the community banks are well-capitalized, well-managed, and well-regulated. They are small enough for the regulators to get their arms around, to deal with them, and to effect the 1,700 pages of legislation and the safety and soundness simultaneously.

Mr. MANZULLO. Mr. Himpler, would you like to comment on that?

Mr. HIMPLER. Yes, Mr. Manzullo. I think it is worth noting for the committee members that apart from mortgage—and all the discussion has been on mortgage—according to Federal Reserve data, there is at any given time $2.5 trillion of outstanding consumer credit, that doesn't include payday. We are talking personal loans, student loans, small business loans, vehicle loans. Over half is generator-originated by nondepository lenders that put their own money at risk and are not a risk to the system.

I think what concerns us is exactly how broad this is and the single focus. We all recognize on both panels a need for consumer protection. But if you went to the Department of Transportation and created this agency and said, we want you to protect drivers with a single focus, if I were that agent and I had no other responsibility, I would reduce the speed limit from coast to coast to 25 miles an hour. That is what we are afraid of.

Mr. MANZULLO. I agree with that. I guess the issue is the powers have already been out there to stop the subprime meltdown. But it is interesting that some of the people who complain now that those powers were not used, were the first in line to say, we have to have housing for everybody. Housing became a right, and then an entitlement, and then the meltdown started on it.

Thank you.

Mr. GREEN. [presiding] Mr. Driehaus of Ohio is recognized for 5 minutes.

Mr. DRIEHAUS. Thank you very much, Mr. Chairman. And thank you, gentlemen, for testifying today for the umpteenth time for some of you.

I spent the better part of the last 8 years in the State legislature in Ohio. And I fully agree with you that the community banks and the small independent financial institutions were not part of the problem. But I think you would concede that you have not been part of the solution either.

For years, we tried to pass predatory lending legislation in the State of Ohio, and were stopped. We were stopped in large part because so many financial institutions said, look, we are already the most regulated industry in the country, the last thing we need is more regulations. And the legislature too often bought into that.

It wasn't until Governor Strickland was elected in 2006 that we finally created a foreclosure task force in the State of Ohio, and finally started actually doing something. And even then, I served on the task force, the bankers were very reluctant to work on legislation that would have gotten at some of the predatory lending issues.

Now, I grant you that the vast majority of the legislation should have been Federal in nature because the State-chartered institutions were few, and they weren't causing the problem. But I just have a problem with this revision as history.

I agree, and I have been fighting for the community banks and this legislation. I was on the phone with the FDIC yesterday, talking about assessments and trying to protect community banks. But my problem is that in the last 8 years, we saw this thing run away; we saw predatory lending legislation introduced in this body in 2001 and every year since, and we did nothing about it.

We saw the problem, but people were making money off the system when real estate was increasing. And until the bubble burst, that is when everybody said, okay, we need to do something about it.

Well, we were paying the price in foreclosures in Cincinnati back in 2001 and in 2002 and 2003. I now live in a neighborhood that has hundreds of homes that have been foreclosed on because we failed to act back then, and the banks were part of that inertia.

What I am trying to get at is I want to come up with a solution that works. I believe very strongly in consumer protection. I also believe you don't need another regulatory burden. Is there a way that we structure this that we are achieving the consumer protection—and maybe it is not by giving the CFPA examination authority, maybe it is by allowing them to create rules and regulations, and they then have enforcement authority but they don't have examination authority, because you don't need another examiner.

I want to make this thing work because the consumers are demanding it, and the consumers deserve it. We in our neighborhoods are paying the price for it. It is not those folks who were foreclosed on, it is not the big banks that have the mortgage-backed securities, it is the neighborhoods who are paying the price. And we continue to pay the price.

So I want you to help me make this work. And I think many of us are willing to work with you in trying to reduce the regulatory burden, but help us understand how we make that happen.

Mr. Yingling?

Mr. YINGLING. Congressman, I just want to say I agree with you completely. I think that our industry—I will speak on behalf of the ABA—made a big mistake. We didn't look at this hard enough, we didn't look at it more globally. We looked at it previously on what does it mean for our regulatory burden on banks.

And not to justify but to explain it, it is because we have such a heavy burden that we get paranoid about it, sometimes for good reason, but we should have been more aggressive in looking at this bad lending and looking at the trends and seeing what was happening in communities. And we should have worked with you at the State level; we should have worked with the Fed earlier on to say, look, something is wrong here and it is going to blow us up.

One of the lessons for the future is we can't just look at what is going on in our narrow interest, but we have to look at what is going on in the economy and in neighborhoods like yours. So your criticism is justified.

Going forward, we need to sit down and figure out how to make this work so we do have more focus on consumer protection, so we don't have the bubbles and bad actors that eventually gobble up all of us. And you have our pledge we are going to work with you to help solve this. We do have concerns about how it is done, but we need to make sure we have protections in place.

Mr. DRIEHAUS. And because I am running out of time, although I don't see any other folks here, so maybe the chairman will allow me a little more, do we get part of the way there by taking away examination authority of the CFPA, by allowing it to be a rule-making body with enforcement power but not examination authority, do we get part of the way there?

Mr. MENZIES. Coordination is important on anything that can be done to produce greater coordination between the regulatory agencies and the CFPA will produce a positive benefit.

But, Congressman, community banks and our customers were equally injured by predatory lending. And in our State, we have been aggressive about that, because predatory lending benefits no one.

Mr. GREEN. Mr. Lee of New York is recognized for 5 minutes.

Mr. LEE. Thank you. I was pleased to hear my friend from Ohio talk about the idea of what we can do to promote less bureaucracy and greater efficiency.

If we are ever going to emerge from this economic downturn, it has to be through job creation in the private sector. Your industry has been one of those bright spots, especially community banks who have been good stewards, well-capitalized, and without them during this downturn, the situation could have been much worse.

I am astonished because you look at Congress and it seems that Congress has a way of adding restrictions, regulatory burdens, more bureaucracy, frankly, in some cases to industries that have done well. My concern here is how we impact, again, the community banks in getting through this. I look at what the CFPA represents, and especially with the issue on preemption.

I guess maybe I can start with, Mr. Yingling, your concern. What are the potential consequences, unintended or not, if this issue of no longer having Federal preemption takes place?

Mr. YINGLING. First, very briefly, there was some discussion in the last panel as though preemption were created 4 or 5 years ago. I have behind my desk, and have had for 30 years in my office, a copy, with Abraham Lincoln's signature, of the National Bank Act. The preemption goes back to that law signed by Abraham Lincoln.

And we have always had preemption in the consumer area. What happened 5 years ago is all of a sudden there were cases all over the country. We had the City of Santa Monica, the City of San Francisco, passing ordinances that they basically—and the courts said it was the case—violated the National Bank Act. So the Comptroller came in with a rule that was designed to clarify to everybody, here is what is going on and, you, the City of Santa Monica, will violate this rule and you are going to lose in court. And that is in effect what happened.

We have always had preemption. It became much more contentious in the last 10 years as States tried to do things and as attorneys general tried to do things.

There has to be a happy medium somewhere. I don't know why we have to go to court all the time to settle this. There has to be some way to receive the input from the States, to let them deal with really egregious issues, while not having 50, and then add the locals, different rules.

The visual I use is we all want to have a very simple credit card disclosure. Everybody talks about having one page. You are not going to have one page, because you are going to have one page, plus 40 or 50 or 60 disclaimers on it. I saw one the other day that said if you were married in one State it is this; if you are not married, it is that. So it is very hard to function; it would be very inefficient.

And one key point: chilling new products. It is one thing to say I am going to offer and design a new product and figure out what law applies to it. It is another thing if you have to go through an analysis of 50 laws, 10 of which could change while you are doing the analysis.

Mr. LEE. Is it fair to say if we don't get our arms around this, it will stifle the ability for these businesses to grow and add employment?

Mr. YINGLING. Right. And more than that, it is going to stifle the ability of consumers and small businesses to get credit products or other financial products.

Mr. LEE. Thank you. With that I yield back.

Mr. GREEN. Thank you. I thank all of the witness for appearing and especially thank one witness, Mr. Menzies, for appearing. This is 2 days before your wedding. I imagine there may be one or two things you could be doing elsewhere. So thank you for taking the time to come in. I also trust this will not be your last appearance with us, we will see you in the future.

Mr. Yingling, I do take seriously your comments. You indicated a lack of focus was a part of the problem. Explain to me how we can—how you would have us cause the proper amount of focus to be generated such that these things that escaped us previously would not escape us going forward. How would you handle the focus question?

Mr. YINGLING. I am not sure I have the total answer. I think the hearing today brought out a lot of options that we can look at. I think part of it is making it more explicit in the statute that you should do this. I think part of it may be the structure of whatever we end up doing here, whether it be within something that looks like the existing framework or something new that builds in an explicit focus. Part of it could be in staff requirements. Frankly, a lot of it is in who is appointed.

If you think through who was sitting on the Federal Reserve Board at this critical time or who has been in some of these seats, perhaps there could have been somebody on the Federal Reserve Board with more of a focus on it.

But I don't think you can rely totally on people, that is a major part, but I think we have to in some way institutionalize in whatever we end up doing here, something that says there will be focus.

One way to do it also that we have suggested is you have the regular Humphrey-Hawkins type hearings before this committee, that you have regular hearings on the consumer issues.

The other thing is, this doesn't get down into the trees, but as you consider the creation of a systemic regulator, the systemic regulator should also have built in a consumer focus, because systemic problems are not just a huge institution, they are not just credit default swaps. The mortgage crisis was a systemic problem.

Mr. GREEN. Continuing, so as not to confuse those looking in perhaps for the first time, do you all agree that there is a necessity for some sort of consumer protection—and without going farther and saying "agency," just consumer protection? If there is someone who differs and you are of the opinion that we don't need some sort of consumer protection, will you kindly extend a hand in the air?

Mr. HIMPLER. I would nuance it this way, Congressman. Yes, there is a need but it is AFSA's position that finance companies that are State-licensed and regulated face that consumer protection in a vigorous fashion at the State level.

Mr. GREEN. Anyone else?

In moving toward consumer protection, Mr. John, who was with us earlier, mentioned a council. Have you had an opportunity to review his concept of a council? I am just curious as to whether you support his council.

Mr. Menzies, have you reviewed it?

Mr. MENZIES. No. It is logical that more minds collectively produce a better analysis of the situation, like our board of governors or our board of directors, but we haven't studied his proposal.

Mr. GREEN. I see. Anyone? Mr. Himpler, you studied it?

Mr. HIMPLER. I think Mr. Menzies testified to the importance of coordination. And AFSA finds Mr. Minnick's proposal very intriguing, and we are looking to explore it further with him because we think there is a very important role in terms of collaboration between the Feds and the States.

Mr. GREEN. Mr. Yingling?

Mr. YINGLING. Well, I have not studied it in detail. The one advantage of that over, say, the Administration's proposal is that one of our big concerns has been this potential clash, and we are confident it would take place, between safety and soundness and consumer.

To the degree that you can have the people who are in charge of both writing the rules, it would be very helpful. I would have one concern that if you have a group that is a council, of course, it can get very bureaucratic and very slow. I don't think that is what you want, Congressman. You want something that is designed—and maybe you can do it through this council in some way—but something that is designed that when they need to adopt a HOEPA regulation, it doesn't take 2 years to do it. Anything like that would have to be designed in a way that is efficient.

Mr. GREEN. I appreciate your indicating that I might not favor certain aspects of it. I also concern myself with the notion that ultimately if the council doesn't act, that it is brought back to Congress, and then you have 435 Members of the House and 100 Members of the Senate who will have to come to some accord before the action that the council has recommended will be acted upon. That, to me, puts us right back where we are.

Mr. YINGLING. I was anticipating you might have that concern.

Mr. GREEN. Well, let me thank all of you for coming. I do it on behalf of the Chair, who had to step away.

At this time, we would like to enter a statement from the Mortgage Bankers Association for the record. And without objection, it is so ordered.

Also at this time, we are going to bring the hearing to closure. And in so doing, the Chair notes that members may have additional questions for this panel which they wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses, and the witnesses on the other panel as well, and to place their responses in the record.

The hearing is now adjourned.

[Whereupon, at 1:40 p.m., the hearing was adjourned.]

A P P E N D I X

September 30, 2009

NCLR
NATIONAL COUNCIL OF LA RAZA

Laying the Foundation for Equal Access to Credit:

How Improved Financial Oversight Can Build Wealth for Hispanic Borrowers

Submitted to:

U.S. House of Representatives Committee on Financial Services

Submitted by:

Janis Bowdler

Deputy Director, Wealth-Building Policy Project

National Council of La Raza

Raul Yzaguirre Building

1126 16th Street, NW

Washington, DC 20036

September 30, 2009

Good morning. My name is Janis Bowdler. I am the Deputy Director of the Wealth-Building Policy Project at the National Council of La Raza (NCLR). NCLR is the largest national Hispanic civil rights and advocacy organization in the United States, dedicated to improving opportunities for Hispanic Americans. I oversee our research, policy analysis, and advocacy on issues critical to building financial security in Latino communities, such as homeownership, consumer credit, auto lending, and financial counseling. During my time at NCLR, I have produced a number of publications on housing issues important to the Latino community, including *American Dream to American Reality: Creating a Fair Housing System that Works for Latinos* and *Jeopardizing Hispanic Homeownership: Predatory Practices in the Homebuying Market*. In addition, I have served as an expert witness before this committee, the U.S. Senate Committee on Banking, Housing, and Urban Affairs, and the Board of Governors of the Federal Reserve. I would like to thank Chairman Frank and Ranking Member Bachus for inviting us to share our views on the creation of the Consumer Financial Protection Agency (CFPA).

For more than two decades, NCLR has actively engaged in relevant public policy issues such as preserving and strengthening the Community Reinvestment Act (CRA) and the Home Ownership and Equity Protection Act (HOEPA), supporting strong fair housing and fair lending laws, increasing access to financial services for low-income people, and promoting homeownership in the Latino community. For the last ten years, NCLR has been helping Latino families become homeowners by supporting local housing counseling agencies. The NCLR Homeownership Network (NHN), a network of 52 community-based counseling providers, works with more than 38,000 families annually and has produced more than 25,000 first-time homebuyers in its first decade. More recently, our focus has shifted to helping families keep their homes. NHN members have counseled more than 7,000 homeowners facing foreclosure. Our subsidiary, the Raza Development Fund (RDF), is the nation's largest Hispanic Community Development Financial Institution (CDFI). Since 1999, RDF has provided $400 million in financing to local development projects throughout the country. These relationships have increased NCLR's institutional knowledge of how Latinos interact with the mortgage market, their credit and capital needs, and the impact of government regulation of financial services markets.

The economic consequences from the recession and historically high foreclosure rates are broadly and deeply felt by middle-class families nationwide, and communities of color have been hit particularly hard. Congress has a responsibility to plug the holes in a broken financial system that allowed millions of families to watch their savings and wealth evaporate and their debt skyrocket.

In my testimony today, I will discuss the structural flaws in the credit market that led to millions of families being shuffled into ill-fitting credit products. Then I will offer NCLR's feedback on the proposed CFPA, followed by recommendations.

A Broken System

Most Americans share a fundamental goal of achieving economic sustainability and wealth that they can pass to their children. To do so, they rely on financial products such as mortgages, car loans, credit cards, insurance, and retirement accounts to facilitate their upward mobility. Unfortunately, structural flaws in our financial market have resulted in unequal access to those products key to economic success and the proliferation of deceptive practices. As a result, Hispanic families routinely pay more for credit, often accompanied by risky terms. Not surprisingly, they also bear a disproportionate share of the consequences, as demonstrated by declining income, wealth, and homeownership levels.

Despite having the necessary authority and mandates, federal regulators failed to reign in the worst practices or advance policies that could have set families up for financial success. In fact, rollbacks on regulations and oversight paved the way for many troubling practices. Borrowers that were otherwise qualified for credit but considered hard-to-serve were often shut out of the market and forced to rely on inferior products. Issuers of subprime mortgage and credit frequently targeted minority communities as fertile ground for expansion, often as a *replacement* of prime products rather than a complement. Much of this lending was conducted by under-regulated finance companies. In the years before the burst of the housing bubble, true market oversight was nearly impossible and gaming the system became widespread.

Under such a regime, Latino borrowers and neighborhoods fared poorly. The lack of strong oversight, inability to identify disparate impact trends, and general inactivity to prevent deceptive practices have manifested real consequences for struggling families. Specifically, deficient oversight failed Latinos, other communities of color, and those of modest means in the following ways:

- **Access to prime products was restricted, even when borrowers had good credit and high incomes.** This most often occurred because short-term profits were prioritized over long-term gains. For instance, many Hispanic borrowers have unique profiles that creditors often consider "hard-to-serve."[1] Despite the fact that sound underwriting models and products exist that can service consumers with these characteristics, there was little incentive to sell them in the marketplace. Such models earned issuers little profit, while subprime models had streamlined underwriting processes and were easy to line with high fees and inflated interest rates. The profitability of the models was also set in part by the price that Wall Street was willing to pay for risk. As their appetite for risk grew, expensive and risky subprime credit became readily available while affordable and low-risk prime credit was restricted. In this way, expensive and risky products drove out those that were most favorable to borrowers. As a result, Latino families have paid more for credit in most market segments. They are 30% more likely to receive high-cost mortgages, nearly twice as likely as White families to have credit card interest rates over 20%, and more likely to be charged costly markups on their auto loans.

- **Disparate impact trends and practices were not properly identified, investigated, or acted upon.** Despite clear evidence that minority borrowers were paying more for credit and being steered into subprime credit when they qualified for prime, the trends went unnoticed by federal regulators. Federal analysts claimed that not enough data was available to take enforcement action against specific lenders. However, the Federal

[1] See Janis Bowdler, *Jeopardizing Hispanic Homeownership: Predatory Practices in the Homebuying Market*, Issue Brief no. 15 (Washington, DC: National Council of La Raza, 2005).

Reserve and other agencies did not exercise their authority to further investigate clear and obvious signs of trouble. For example, a recent study shows that even after controlling for percent minority, low credit scores, poverty, and median home value, the proportion of subprime loans originated at the metropolitan level correlates with racial segregation.[2] In fact, a study conducted by the Department of Housing and Urban Development (HUD) in 2000 found that *high-income* Blacks living in predominately Black neighborhoods were three times more likely to receive a subprime purchase loan than *low-income* White borrowers.[3] Simple investigations would have turned up enough information to justify new lending rules and guidance, and possibly enforcement action. In fact, in one private meeting with a major mortgage lender, NCLR discovered that the company's wholesale portfolio consisted almost entirely of Black clients and only offered high-cost loans. The company was clearly targeting minority communities with its subprime affiliate while catering to affluent White households with its retail operation. A similar practice has also been revealed by whistleblowers in *Baltimore v. Wells Fargo*, who claim that deliberate strategies were employed whereby agents would target communities of color to market subprime mortgages.[4] Other research has shown that payday lenders, "buy here pay here" auto dealers, and other fringe financial providers tend to cluster in minority and low-income communities.[5]

- **Shopping for credit was nearly impossible.** Many experts pointed to the growing complexity of credit products and many reports demonstrated that consumers lacked the information necessary to make sound decisions. Credit card, auto, and mortgage offers are not transparent, and borrowers are often unaware of the hidden costs in their loans. Few shopping tools exist that can help borrowers create true apples-to-apples cost comparisons. As a result, many borrowers forego shopping all together. According to one survey, only 7% of Hispanic consumers who carry a credit card balance report "substantial" shopping for credit, compared to 12% for similar White consumers; approximately 25% of Hispanic card users that had been denied a loan did not reapply for fear of rejection.[6] In the case of mortgage and auto loans, mortgage brokers and auto dealers serve as an intermediary between the borrower and the lender. While many borrowers believe these agents are shopping for the best deal on their behalf, they are under no legal or ethical responsibility to do so. While most consumers do not proactively shop for credit, credit issuers shop aggressively for borrowers. Roughly 5.2 billion credit card solicitations were sent to U.S. households in 2004.[7] Through the

---

[2] Gregory D. Squires, Derek S. Hyra, and Robert N. Renner, "Segregation and the Subprime Lending Crisis" (paper presented at the 2009 Federal Reserve System Community Affairs Research Conference, Washington, DC, April 16, 2009).

[3] U.S. Department of Housing and Urban Development, *Unequal Burden: Income and Racial Disparities in Subprime Lending in America.* Washington, DC, 2000.

[4] Michael Powell, "Bank Accused of Pushing Mortgage Deals on Blacks," *New York Times*, June 6, 2009, http://www.nytimes.com/2009/06/07/us/07baltimore.html?_r=2&pagewanted=1&sq=wells%20fargo&st=cse&scp=2 (accessed September 29, 2009).

[5] See Wei Li et al., *Predatory Profiling: The Role of Race and Ethnicity in the Location of Payday Lenders in California* (Washington, DC: Center for Responsible Lending, 2009).

[6] Unpublished data from the *2004 Survey of Consumer Finances* tabulated by the Federal Reserve on behalf of NCLR.

[7] Government Accountability Office, *Credit Cards: Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers.* Washington, DC, 2006.

collection of consumer financial information, issuers essentially prescreen and select their customers. Meanwhile, federal regulators sat on major reforms for years that could have improved shopping, such as a revised Good Faith Estimate and other documents made available under the Real Estate and Settlement Procedures Act (RESPA) and reforms defining unfair and deceptive marketing practices.

While some would be happy to allow market forces to continue unchecked, this regulatory philosophy has had serious consequences for families and local and national economies. For example, credit card companies made over $17 billion in penalty fees in 2006[8] and banks will make $38.5 billion in customer overdraft fees in 2009,[9] money that could otherwise be used for household expenses or savings. Subprime foreclosures are estimated to cost states and local governments $917 million in lost property tax revenue,[10] while payday lenders drain nearly $5 billion per year from the earnings of working people.[11] After reaching an all-time high, the homeownership rate for native-born Latinos has declined by nearly three percentage points in just three years.[12] As wealth and savings have eroded, families are left with no safety net for emergencies and an uncertain financial future.

Establishing Commonsense Oversight

As members of this committee seek to revamp our financial regulatory system to prevent further crisis, they must fill the gaps in oversight and accountability that left Hispanic borrowers vulnerable to steering and other unfair practices. Specifically, lawmakers must ensure that borrowers have the opportunity to be matched to credit products that truly reflect their risk of nonpayment in the most affordable terms possible. This includes improving competition and transparent shopping opportunities, promoting a viable and nonpredatory subprime market, advancing new consumer decision-making tools, and increasing product innovation to serve a wide range of credit needs. Furthermore, any reform must also establish strong market accountability. Credit markets and practices are dynamic, as are the tricks bad actors use to lure borrowers into products laced with risky and expensive features. While some argue that it is the borrower's responsibility to be on the lookout for deception, it is unreasonable to expect individual families to be able to regulate the market and, in effect, detect what the Federal Reserve did not. Lessons from the market implosion suggest that simply having good products available does not guarantee that they will reach the intended population. Bad practices often kept best practices and products at bay. The ideal regulatory structure would be able to identify and eliminate deceptive practices and enforce strong consumer protection laws.

---

[8] U.S. PRIG Education Fund, "A Consumer's Guide to Credit Cards" (Boston, MA: U.S. PIRG Education Fund) http://www.uspirg.org/html/Credit_Card_Booklet.pdf (accessed September 2009).
[9] Reuters, "U.S. banks to make $38 billion from overdraft fees: report," August 10, 2009, http://www.reuters.com/article/newsOne/idUSTRE5790YM20090810 (accessed September 2009).
[10] Majority Staff of the Joint Economic Committee, *The Subprime Lending Crisis: The Economic Impact on Wealth, Property Values and Tax Revenues, and How We Got Here*. Washington, DC, 2007, http://jec.senate.gov/archive/Documents/Reports/10.25.07OctoberSubprimeReport.pdf (accessed September 2009)
[11] Center for Responsible Lending, "A 36% APR cap on high-cost loans promotes financial recovery" (Durham, NC: Center for Responsible Lending, 2009), http://www.responsiblelending.org/payday-lending/policy-legislation/congress/payday-and-the-economy.pdf (accessed September 2009).
[12] Rakesh Kochhar, *Through Boom and Bust: Minorities, Immigrants and Homeownership* (Washington DC: Pew Hispanic Center, 2009).

The Consumer Financial Protection Agency (CFPA), proposed by the Obama administration and members of this committee, is the dominant policy proposal currently under consideration to address these issues. NCLR supports the creation of a new agency dedicated to consumer protection, product innovation, and equal access to financial markets. While some are pointing to recent actions by federal regulators as evidence that the necessary regulatory capacity exists, conflicts of interest prevent federal agencies from focusing expressly on the needs of consumers, especially those of color. Federal regulators missed key trends impacting Latinos and all consumers, acting only when it was too late to stop an implosion of the credit market. That said, the CFPA must be established with the authority, jurisdiction, and funding necessary to carry out to accomplish its mission. As laid out in the discussion draft of the "Consumer Financial Protection Act of 2009,"[13] the agency stands to improve market oversight in critical ways. Other aspects, however, still require strengthening.

As this committee moves forward with its deliberations, we urge you to retain the following aspects of the discussion draft:

- **Elevation of fair lending laws.** As described above, many Latino consumers were steered into subprime loans, even when they had high incomes and good credit. Had federal regulators better enforced fair lending laws, many such tactics would have been eliminated. The discussion draft authorizes CFPA to assume responsibility for overseeing the financial industry's compliance with fair lending laws currently under the jurisdiction of the federal regulators. It also explicitly incorporates civil rights into the agency's mission, as well as its structure, by establishing an Office of Fair Lending and Equal Opportunity. These additions elevate the enforcement of fair lending as a major priority within the agency. We urge lawmakers to go one step further in tasking CFPA with identifying trends and practices that have disparate impact on minority and underserved populations, and taking the steps necessary to curb such behavior.

- **Strong supervision and consumer protection rule-writing ability.** In the most recent draft, CFPA has been granted robust rule-writing authority that will allow it to consolidate enforcement of consumer protection laws and better protect financial services consumers. It also provides the agency with an independent Executive Director, which will allow the agency to stay objective in its assessments of the market. Moreover, rules issued by CFPA will not preempt stronger laws elsewhere, ensuring that no borrowers lose protection as a result of CFPA action. These provisions should not be weakened.

In addition to these provisions, NCLR has also been working closely with members of the committee to lay the groundwork for greater access to financial advice. Timely advice and information is critical to improving the way consumers make decisions, promoting wealth-building and preventing cycles of debt. It is not enough for CFPA to develop passive and generic materials. Instead, they must actively promote the delivery of financial counseling from trained professionals to families that need it most.

---

[13] Available at http://www.house.gov/apps/list/press/financialsvcs_dem/discussion_draft_of_cfpa_bill_092509.pdf (accessed September 28, 2009).

CFPA could be a strong vehicle for improving the way financial markets serve their Latino clients. However, more could be done to ensure that this new agency can fully accomplish its goals. NCLR strongly encourages Congress to strengthen or reinstate key provisions to guarantee that Hispanic consumers are well-served. Specifically:

- **Improve access to simple, prime credit products.** Ensuring that one can obtain the most favorable credit product and terms for which one qualifies should be a principal goal of federal efforts to reform financial oversight. Provisions that would have required financial institutions and entities to offer basic, straightforward car and home loans or credit cards have been removed. This leaves a gaping hole in protections for households that struggle to connect to the most favorable products for which they qualify. CFPA must be able to promote and advance simple, standard products in the marketplace. This includes fostering innovation in product development to meet the needs of underserved communities. Borrowers should be qualified against that product first and opt for other products as necessary based on niche needs or qualifications.

- **Eliminate loopholes for those that broker financing and credit bureaus.** Cut off or underserved by many retail outlets, borrowers of color or those with modest incomes often rely on finance brokers to help them find a loan. Financing offered by auto dealerships, mortgage brokers, or real estate agents are major sources of credit that demand greater attention and oversight. Many of the worst abuses in the auto and home loan markets were at the hands of brokers and dealers. As those closest to the transaction, dealers, brokers, and agents have an extraordinary responsibility and opportunity to ensure that credit deals are fair and fitting to the borrower's circumstances. Moreover, an exemption was also made for credit bureaus. While not direct lenders, the practices of credit bureaus directly impact the quantity and quality of credit that flows to consumers. For example, credit bureaus set rules around the manner in which credit scores are calculated. Also, by making their data available to certain vendors, creditors are able to shop for consumers, limiting the information and offers made available to all. Real estate agents, brokers, auto dealers, and credit bureaus should not escape greater accountability. Committee members should ensure that they are within the jurisdiction of CFPA.

- **Reinstate community-level assessment in CFPA.** CFPA must be able to assess product offerings at a community and regional level. Without such an assessment, favorable credit products may be developed but will remain unavailable in entire neighborhoods. Subprime lenders, creditors, and fringe financial providers often target entire neighborhoods based on the demographics of the area. Their efforts are often successful because those offering more favorable products are physically absent or do not cater to the needs of local residents. With CRA removed from the jurisdiction of CFPA, there is no mechanism for promoting access to credit and eliminating abuses at the community level. To be successful, CFPA must be able to assess the delivery of products at the community level, as well as the products and industries themselves. Including CRA in the CFPA will give the agency the authority necessary to make such an assessment.

Conclusion

Poor oversight and market inefficiencies have diverted untold sums of hard-earned income and savings away from households. Rather than waste money, a sound financial market should provide opportunities to achieve financial security. NCLR supports the committee's efforts to improve market oversight and accountability with this shared goal in mind. As one of the hardest-hit communities by the current recession, Latinos stand to benefit from an improved market where credit is more equitably distributed. We support the concept of a strong, independent CFPA that can serve as a consumer watchdog and level the playing field for those of modest means. We also look forward to working with the committee and other policymakers on further reforms of the financial oversight system and credit markets.

SEIU
Stronger Together

ANDREW L. STERN
International President

ANNA BURGER
International Secretary-Treasurer

MITCH ACKERMAN
Executive Vice President

MARY KAY HENRY
Executive Vice President

GERRY HUDSON
Executive Vice President

ELISEO MEDINA
Executive Vice President

BRUCE RAYNOR
Executive Vice President

DAVE REGAN
Executive Vice President

TOM WOODRUFF
Executive Vice President

SERVICE EMPLOYEES
INTERNATIONAL UNION
CTW, CLC

1800 Massachusetts Ave NW
Washington, D.C. 20036

202.730.7000
TDD: 202.730.7481
www.SEIU.org

Testimony of SEIU Secretary-Treasurer Anna Burger
"Perspectives on the Consumer Financial Protection Agency"
House Financial Services Committee
September 30, 2009

On behalf of the 2.1 million members of the Service Employees International Union (SEIU), and as a coalition member of Americans for Financial Reform, I want to thank Chairman Frank, Ranking Member Bachus and the Committee members for their continued work to reform our broken financial system.

It's been a year since the financial world collapsed, showing us that the actions of a few greedy players on Wall Street can take down the entire global economy. As we continue to dig our way out of this crisis, we have an historic opportunity—and a responsibility—to reform the causes of our continued financial instability and protect consumers from harmful and often predatory practices employed by banks to rake in billions and drive consumers into debt.

The nurses, child care providers, janitors, and other members of SEIU continue to experience the devastating effects of our financial crisis firsthand. Our members and their families are losing their jobs, their homes, their healthcare coverage, and their retirement savings. As states and local governments face record budget crises, public employees are losing their jobs and communities are losing vital public services. And we see companies forced to shut their doors as banks refuse to expand lending and call in lines of credit. At the same time banks and credit card companies continue to raise fees and interest rates and refuse to modify mortgages and other loans.

We know the cause of our current economic crisis. Wall Street, big banks and corporate CEOs created exotic financial deals, took on too much risk and debt in search of outrageous bonuses, fees and unsustainable returns. The deals collapsed and taxpayers stepped in to bail them out. According to a recent report released by SEIU, once all crisis-related programs are factored in, taxpayers could be on the hook for up to $17.8 trillion.

The proliferation of inappropriate and unsustainable lending practices that sent our economy into a tailspin could have and should have been prevented. The regulators' failure to act, despite abundant evidence of the need, highlights the inadequacies of our current regulatory system, in which none of the many financial regulators regard consumer protection as a priority.

We strongly support the creation of a single Consumer Financial Protection Agency to consolidate authority in one place with the sole mission of watching out for consumers across all financial services.

I want to thank Chairman Frank for his work to strengthen proposed Consumer Financial Protection Agency language—particularly the strong whistleblower protections. We believe to be successful, CFPA legislation must include: a scope that includes all consumer financial products and services; sole rulemaking and primary enforcement authority; independent examination authority; federal rules that function as a floor, not a ceiling; the Community Reinvestment Act; funding that is stable, and does not undermine the agency's independence from industry; and strong whistleblower and compensation protections.

We believe independence, consolidated authority and adequate power to stop unfair, deceptive and abusive practices are key features to enable the CFPA to serve as the building block of comprehensive financial reform.

Over the past year, we've also heard directly from several frontline financial services employees about their working conditions and industry practices. We know from our conversations that existing industry practices incentivize frontline financial workers to push unneeded and often harmful financial products on consumers. We need to ban the use of commissions and quotas that incentivize rank-and-file personnel to act against the interests of consumers in order to make ends meet, or simply to keep their job. The CFPA is the agency that can create this industry change.

Imagine if these workers were able to speak out about practices they thought were deceptive and hurting consumers? The mortgage broker forced to meet a certain quota of subprime mortgages. The credit card call center worker forced to encourage Americans to take on debt they cannot afford and then threaten and harass customers when they can no longer make their payments. The personal banker forced to open up accounts for people without their knowledge.

Including protections and a voice for bank workers will help rebuild our economy today and ensure our financial system remains stable in the future.

Thank you for the opportunity to speak this morning. The American people are counting on this Committee to hold financial firms accountable and put in place regulations that prevent future crises.

Testimony of Michael Calhoun, Center for Responsible Lending
Before the U.S. House of Representatives Committee on Financial Services
"Perspectives on the Consumer Financial Protection Agency"

September 30, 2009

Good morning Chairman Frank, Ranking Member Bachus, and members of the Committee. Thank you for inviting me to testify on H.R. 3126, a bill to establish a Consumer Financial Protection Agency to keep the market for financial products and services free of unfairness, deception and abuse.

I. **Introduction.**

I testify today on behalf of the Center for Responsible Lending (CRL), a non-profit, non-partisan research and policy organization, and Self-Help, a non-profit credit union and lender that would be subject to the supervision and enforcement of the proposed Consumer Financial Protection Agency (CFPA). It is unusual for a financial institution to welcome change that strengthens lending oversight, but in this case we believe that the current regulatory structure has worked so poorly, and the need to prevent another crisis in the future is so vital, that we unequivocally support the creation of a strong and independent consumer protection agency that preserves the ability of the states to protect their residents—one that would streamline the current system and eliminate the conflicts of interests that played a key role in the economic crisis we are grappling with today.

I serve as President of CRL, which is dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, a non-profit community development financial institution that consists of a credit union and a non-profit loan fund. For close to thirty years, Self-Help has focused on creating ownership opportunities for low-wealth families, primarily through financing home loans to low-income and minority families who otherwise might not have been able to get affordable home loans. In total, Self-Help has provided over $5.6 billion of financing to 62,000 low-wealth families, small businesses and nonprofit organizations in North Carolina and across America. Self-Help's lending record includes an extensive secondary market program, in which we partner with for-profit lenders to encourage and enable sustainable loans to borrowers with blemished credit.

The financial oversight system we have today is fundamentally broken, hobbled by conflicts of interest and strong incentives to ignore lending abuses. Nowhere is this more starkly evident than in the area of consumer protection. Thirty-five years ago, Congress vested all the federal banking regulators with the responsibility to prevent unfair and deceptive acts and practices by the banks, thrifts and credit unions they regulate. Yet in recent years none of these agencies has pursued this mandate diligently, and, in fact, often denied their authority to do so or refused to take enforcement actions.

To the extent that Americans have received decent, up-to-date protections from unfair and deceptive products, those protections have come primarily from the states. For example, many of our states were years ahead of federal regulators in recognizing and taking action to curb abusive mortgage lending. Yet some of the very same institutions that helped cause this crisis, and their regulators that stood by passively, are fighting hard to keep the locus of their power here in Washington.

We strongly support a robust and independent Consumer Financial Protection Agency, but we would actively oppose such an agency if the price of enacting it would be to overturn existing state consumer protection laws or to restrict the ability of the states to respond to new "innovations" in the marketplace that harm their residents. The most robust system for consumers and for our economy as a whole would be a strong federal agency that establishes minimum standards, allowing states to take stronger action when necessary. We urge Congress to stand up for the states they represent, and to refrain from any action that would undermine our states' ability to protect their residents and their local economies.

In considering all aspects of this proposal, the stakes are high. Unfair and deceptive credit card, overdraft and mortgage products have been allowed to proliferate, injuring millions of individuals and families across the country. The result was that Americans have had less choice in financial products, and every year families lose billions of dollars in unnecessary overcharges and fees.

It is no mystery why lenders would aggressively market high-cost credit cards, load their overdraft loans with staggering fees, or steer people into more expensive loans than they qualify for. These practices yield high fees for lenders who face pressure to keep up with competitors that are doing the same. In fact, responsible financial institutions that refuse to engage in these aggressive anti-consumer practices are put at a competitive disadvantage.

Less obvious are the reasons why the banking regulators permit these abusive practices, but a review of the current regulatory structure is helpful in understanding those reasons. Currently, five different banking agencies are responsible for the safety and soundness of banks, thrifts, bank holding companies and credit unions, and also for protecting consumers against harmful practices by these entities. Each has its own consumer affairs department responsible for receiving and acting upon consumer complaints and enforcing federal law against unfair and deceptive acts and practices, and three of the agencies are responsible for writing regulations to further the purpose of preventing unfair acts and practices. Only one of the agencies has authority to write regulations covering non-depository lenders.

In this testimony, we identify numerous failures by the regulators who have been entrusted and charged with preventing lending abuses, particularly failures by the Office of the Comptroller of the Currency (OCC), the Office of Thrift Supervision (OTS), and the Federal Reserve Board (FRB). We also identify several flaws built into the system that produced the banking regulators' worst failures: conflict of interest; competition to attract lending institutions; the ability to pressure the States into weakening their lending rules to match the lowest common denominator; failure to set minimum standards for all relevant market participants, and the absence of a mechanism for enforcing them.

Our current system that relies on five separate agencies—creating inherent conflicts and regulatory sprawl—has proved both wasteful and ineffective. Rather than guarding against lending abuses, the agencies have been distracted by the demands of protecting their turf. The current structure encourages them to focus on competition amongst themselves, to misdirect resources to market themselves to regulated companies; to litigate against States to prevent consumer protection enforcement; and to maintain five separate consumer protection departments that overlap with each other, but still leave large portions of the market uncovered. It would be much better to harness these resources into a single, well-resourced agency that is capable and highly motivated to accomplish its consumer protection mission.

Another key part of this testimony highlights the importance of making the proposed CFPA comprehensive enough to avoid loopholes that could drastically undermine the agency's effectiveness. Meaningful financial reform will benefit legitimate small businesses and financial providers of all sizes, reducing the necessity of competing against market distorting forces of unfair and irresponsible businesses. But meaningful financial reform will only come if the reform is not riddled with exemptions that create loopholes, since it is inevitable that any gaps and exclusions will be exploited for opportunistic abuse. We urge Congress to resist pressure to include unnecessary exemptions.

We also urge absolute clarity about where the systemic vulnerabilities lie, so we can design a better system for the future. Any effective system will include these minimal requirements:

(1) The agency must be separate from the safety and soundness regulators to focus on consumer protection;

(2) It must have rule-making authority over *all* providers of consumer financial services and products to avoid gaps in coverage that create opportunities for abuse and force competitors into a race to the bottom;

(3) Strong enforcement authority is required so that rules are backed by meaningful consequences;

(4) Examination or supervisory authority is required to detect problems before they become widespread; and

(5) Consumer protection regulation and enforcement must honor our federalist system, allowing the States to step in when local conditions require action.

In other areas of economic life, American markets have been distinguished by the standards of safety and fairness that are fundamental to economic stability. The financial services sector is too important to fail to meet these standards. A strong, properly incented, independent Consumer Financial Protection Agency will help restore consumer confidence, reassure secondary market investors, and protect our economy from the consumer financial dislocations that helped produce the global economic collapse of the past year.

We look forward to working with the Committee to create a strong, effective and efficient CFPA.

II. Perverse Incentives and Lack of Consumer Choice

One of the central causes of the current economic crisis was the absence of sustainable choices of financial products for many American families—choices that would have been win-win for working Americans, for financial institutions, for investors, and the economy.

We got on this rocky road because many companies made bigger fees by pushing bad financial products. In its final form, the proposed Consumer Financial Protection Agency must ensure that never again will we have a market that only offers millions of families "options" from the bottom of the barrel.

The box below outlines a few examples of bad practices and products crowding out good ones, reducing both consumer choice and honest competition.[1] The market pushed the products that generated the biggest short-term revenues, depriving people of the ability to make the financial choices that best suited their needs, such as a loan they had a real chance to repay,[2] a checking account that did not hemorrhage their hard-earned money to the banks, or a credit card that did not arbitrarily change the rules on them.

Examples of Bad Practices that Reduced Consumer Choice and Honest Competition

Mortgages

- **In 2003**, nearly $2.5 trillion in prime mortgages were originated. In sharp contrast, less than $500 billion in the riskier nonprime[3] mortgages were originated.
  By 2006, non-prime mortgage originations (jumbo loans, Alt-A, and subprime) of nearly $1.5 trillion had surpassed prime mortgage originations, which had decreased to $990 billion.[4]
- A 2007 Wall Street Journal study found that 61% of subprime borrowers may have qualified for a conventional loan. [5]

Overdraft Fees

- **In 2004**, 80% of institutions simply denied ATM and point-of sale debits that would have overdrawn their customers' accounts.
  Now 80% of institutions fund these debits *with loans that their customers didn't ask for and most don't want,* taking well in excess of $20 billion from their customers' accounts this year alone.[6]

Credit Cards

- Before Congress passed the Credit Card Act this year, it was virtually impossible for credit cardholders to "choose" a card that had honest accounting and that gave them the benefit of low-rate balance transfer deals they were offered.7 Even now, the card companies are devising new ways of scamming customers to make up for lost revenue.

III. Regulatory Failures

A. Congress has repeatedly vested the federal banking agencies with the authority and obligation to prevent unfair and deceptive lending, yet the agencies have repeatedly refused to use this authority.

For more than half a century, the federal banking agencies have had the responsibility for protecting consumers from unfair and deceptive acts in practices by financial institutions within their jurisdiction. Unfair or deceptive acts or practices in commerce have been illegal under federal law since at least the 1930s.[8] In 1966, Congress gave all the federal banking agencies authority to bring enforcement actions and issue "cease and desist" orders against companies that violate laws or regulations, including those involving unfair or deceptive acts or practices. This mandate was further strengthened in 1975 when Congress expressly required each banking agency to establish a separate division of consumer affairs to act upon consumer complaints alleging unfair or deceptive acts or practices.[9]

Also in 1975, Congress gave the Federal Reserve Board rulemaking authority to define with specificity unfair and deceptive acts and to promulgate regulations to prevent them. The same authority was given to the Office of Thrift Supervision ((OTS), then the Home Loan Bank Board) and the National Credit Union Administration, with respect to the institutions they cover.[10] This new rule-making authority supplemented the banking agencies' existing authority to enforce federal prohibitions on unfair or deceptive acts or practices, which Congress had granted to the federal banking agencies in 1966.[11]

Finally, reacting to the rise of abusive mortgage loans, in 1994, Congress passed the Homeowner Equity Protection Act, which gave the FRB further rulemaking authority to prohibit acts or practices in connection with mortgages that the Board determines are unfair, deceptive, or designed to evade HOEPA, or that are made in connection with a refinancing of a mortgage loan that the Board finds to be associated with abusive lending practices, or that are otherwise not in the interest of the borrower.[12] Importantly, this authority extends to all financial institutions, both depository institutions (banks, thrifts and credit unions) and non-depositories (such as non-bank mortgage lenders).

Thus, for over fifty years, Congress has repeatedly authorized and required the federal banking agencies to set and enforce consumer protection standards to prevent unfairness and deception in by financial institutions. These delegations do not represent abdication of legislative responsibility; rather, they represent common sense. In enacting the original FTC Act, Congress recognized that "there is no limit to human inventiveness" in creating unfair practices. If Congress reserved the obligation to define such practices itself, "it would undertake an endless task."[13] (To see a few examples of how failures on safety and soundness are linked to failures on consumer protections, see Appendix A.)

B. The federal banking agencies have been unwilling to ban the unfair and deceptive acts and practices that have proliferated in mortgage lending, credit cards, overdraft loans, and other areas.

In recent years, the banking agencies remained remarkably passive in the face of increasingly risky lending practices—practices that were highly visible in the marketplace and the media. Neither the FRB, which has the rule-making authority to ban unfair and deceptive acts and practices across the market, nor the other banking agencies, which have the authority to ban them as to their own institutions through the issuance of "guidance," supervisory activity, and enforcement actions, took any steps to regulate such practices.

1. A long record of inaction.

Through all the years leading up to the 2008 foreclosure crisis and financial collapse, the federal regulators failed to act. The two frontline national banking regulators, the Office of Thrift Supervision (OTS) and the Office of the Comptroller of the Currency (OCC), came to view the banks they regulate as their paying customers, and they have been reluctant to take action that could cause their customers to switch their charter to another regulator. As a result, these agencies have defended practices that hurt consumers. Moreover, they have intervened to prevent state authorities from acting to stop harmful lending practices, preempting state laws and blocking state law enforcers from investigating banks that were taking advantage of consumers.[14] Consider these examples:

- The OCC did not exercise its consumer protection authority to address unfair and deceptive practices under the FTC Act for twenty-five years.[15] The OCC's first action using its power to go after a bank's unfair and deceptive practices came only after a decade in which the target bank "had been well known in the ... industry as the poster child of abusive consumer practices" and after the OCC was "embarrassed ... into taking action" by a California prosecutor.[16]

- From 1987 to the present, the OCC brought only four formal enforcement actions under the Equal Credit Opportunity Act, 15 U.S.C. § 1691c(a)(1)(A), and its implementing regulations, and from 2000 to 2008 the OCC made no referrals under ECOA to the U.S. Department of Justice of matters involving race or national origin discrimination in mortgage lending.[17]

- Between 2000 and 2008, as the mortgage market grew wildly and abusive practices against homeowners flourished, the OCC took only two public enforcement actions against banks for unfair and deceptive practices in mortgage lending – both against small Texas banks.[18]

- Although the OTS has recently increased the number of ECOA referrals to the Department of Justice (DOJ), from 2000 to 2006 the agency made no referrals for race or national origin discrimination in mortgage lending. Despite the lack of referrals, in 2002 the DOJ filed a complaint alleging that Mid America Bank, an OTS-regulated bank, engaged in a pattern or practice of redlining on the basis of race.

- Another federal bank regulator, the Federal Deposit Insurance Corporation (FDIC), in 2002 gave Centier Bank a satisfactory rating under the Community Reinvestment Act. However, when the Department of Justice reviewed data from 2000-2004 they found that Centier failed to serve the credit needs of minority communities. Centier eventually settled DOJ's redlining suit.[19]

2. Failure to ban abusive mortgage lending practices.

Fourteen years ago, Congress required the Federal Reserve Board (the FRB) to prohibit mortgage lending acts and practices for all originators that are abusive, unfair or deceptive. Although borrowers, state regulators, and advocates repeatedly raised concerns about abuses in the subprime market, and hard evidence demonstrated the destructive results of abusive practices, *the Board took no action until July 2008.*[20] Federal banking regulators could and should have banned the most egregious mortgage lending practices:

- They should have prohibited lenders from making loans where it was clear that the borrower lacked sufficient income to sustain the loan when the interest rate reset two or three years after the loan was originated.
- They should have prohibited lenders from offering mortgage brokers financial incentives to steer their customers into more expensive loans than they qualified for.
- They should have prohibited large prepayment penalties that trapped borrowers into high cost loans or stripped large amounts of home equity with each refinancing.

Regulators were well aware of highly questionable lending practices. For example, a 2005 OCC survey of credit underwriting practices found a "clear trend toward easing of underwriting standards as banks stretch for volume and yield," and the agency commented that "ambitious growth goals in a highly competitive market can create an environment that fosters imprudent credit decisions." In fact, 28% of the banks eased standards, and the 2005 OCC survey was its first survey where examiners "reported net easing of retail underwriting standards."[21]

In late September 2006, several agencies (the FDIC, FRB, National Credit Union Administration, the OCC and the OTS) issued joint guidance on underwriting nontraditional loans, years after the problems they addressed had become apparent and a full nine months after they first solicited comments on proposed guidance on that topic.[22] It is unclear to what degree the nontraditional guidance was enforced as lax underwriting standards continued in the nontraditional market until the market collapse.[23] While the agencies explicitly required lenders to evaluate a borrower's ability to repay a nontraditional loan based on the fully indexed rate and based on a fully amortizing repayment schedule, they did not implement similar explicit rules for subprime loans for another ten months, finally issuing parallel guidance on underwriting subprime loans in July 2007.[24]

Even without the new guidance, the regulators could have used rules already in place at least to mitigate the impact of abusive subprime lending, but they failed to act. The agencies did issue guidance as early as 1999 on subprime lending,[25] with a second guidance in 2001 that explicitly described predatory lending as including: "Making unaffordable loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation..."[26] Despite these guidances, there is no evidence of instances where the agencies prevented lenders from devising new products that similarly failed to evaluate the borrowers' ability to repay the loan.

It was not until 2008 that the FRB finally acted by issuing new regulations to address unfair, deceptive and abusive mortgage lending practices that prevailed during the prior eight years—but the regulations came too late to have an impact on the current economic calamity. Indeed, some of the new FRB rules are only taking effect now, on October 1, and some have yet to become effective. Moreover, they apply to subprime loans alone; they do not address the widespread payment option ARMs and Alt-A loans whose worst collapse is still ahead of us.

3. Abuses not confined to finance companies – banks played a role.

The federal banking agencies and the American Bankers Association have claimed that their institutions have not engaged in abusive mortgage lending. If only this were so.
Under the OCC's watch, national banks moved aggressively into risky "Alt-A" low-documentation and no-documentation loans during the housing boom.[27] A 2004 OCC rule prohibiting the origination of unaffordable mortgages "was vague in design and execution, allowing lax lending to proliferate at national banks and their mortgage lending subsidiaries through 2007," as law professor Patricia McCoy has testified.[28]

Big national banks continued rolling up huge volumes of poorly underwritten subprime loans and low- and no-documentation loans. For example, in 2006 more than 62 percent of the first-lien home purchase mortgages made by National City Bank and its OCC-supervised subsidiary, First Franklin Financial, were high-priced subprime loans. As these loans began to go bad in large numbers in 2007 and 2008, National City Corp. reported five straight quarters of net losses. It was saved from receivership only by a "shotgun marriage" to PNC Financial Services Group.[29]

OCC inaction is even more troubling given the evidence of potential discrimination among national banks. Studies show national banks routinely originate a disproportionate number of subprime loans among minority borrowers. For example, one study found that national banks were 4.15 times more likely to make higher-cost refinance loans to African-Americans than they were to make higher-cost loans to white borrowers.[30] In addition, two former Wells Fargo employees have signed declarations that the bank's sales staffers steered minorities into high-cost subprime loans.[31]

OCC Ignores First Union Case
The case of Dorothy Smith, a 67-year-old homeowner is East St. Louis, Illinois, illustrates the OCC's lack of concern for consumers. As described in a 2007 article in the *Wall Street Journal*,* Ms. Smith, who was living on $540 month in government benefits, was taken in by a home repair contractor and a mortgage broker who landed her in a mortgage from First Union National Bank. The loan contract required her to pay two-thirds of her income – $360 a month – for 15 years, followed by a balloon payment of more than $30,000. After receiving Ms. Smith's complaint about First Union, the OCC brushed her off, saying that it couldn't intercede in a "private party situation regarding the interpretation or enforcement of her contract. . . . The OCC can provide no further assistance."

*Greg Ip and& Damian Paletta, *Lending Oversight: Regulators Scrutinized In Mortgage Meltdown --- States, Federal Agencies Clashed on Subprimes As Market Ballooned*, Wall Street Journal (March 22, 2007).

4. *Failure to ban abusive credit card practices*

While destructive lending proliferated in the mortgage market, the credit card companies were also becoming increasingly bold in implementing abusive practices that had an adverse effect on consumers. Here are a few examples of credit card abuses that became commonplace:

- Retroactive changes in interest rates: Credit card companies were routinely raising their customers' interest rates and applying the higher rate to charges that had been made before the rate increase.

- Adverse allocation of credit card payments: Many credit card companies allocated their customers' payments in a manner that made promotional rates disappear quickly and artificially kept high APR balances on the books as long as possible.

- Universal default rates: Credit card customers who paid their credit card bills on time were getting penalty interest rate increases for late charges on completely different accounts or for any credit score decline. For example, customers who had a late charge on a light bill or who had their credit score decline because they closed an inactive account might be hit with steep increases on their credit card rate—even as applied to existing balances—even though the late bill had no connection to the credit card.

- Double cycle billing: Some credit card companies were charging customers interest based on balances from the prior month as well as the current month in a practice known as "double-cycle billing."

Abusive practices have not been exclusive to the largest card issuers; some community banks have engaged in them as well. In just the last three months, cards issued by community banks carried penalty rates approaching 30 percent—often more than double the regular rate; penalty fees as high as the largest issuers; cash advance fees higher than most of the largest issuers; and the same payment allocation policies as the largest issuers. Here are several examples:

Skylands Community Bank Visa Platinum Business Rewards Card (offered through Elan Financial Services), 8/2009

- 28.99% penalty rate (more than double the regular rate)
- $2 minimum finance charge (the highest seen with large banks)
- $2.50 account management per month if you have a closed account with a balance
- Cash advance fee of 4% (higher than most of the top issuers)
- Late fee: $39 for balances $250 and over (as high as the highest among top issuers)
- Other fees and practices are in line with the more aggressive of the top issuers
- Same payment allocation policy as top issuers

New York Community Bank Business Card (offered through B of A), 7/2009

- Penalty rate of up to 29.99%
- Cash advance fee of 4% (higher than most of the top issuers)
- Introductory rate is lost after being late just one day

- Other fees and practices are in line with the more aggressive of the top issuers
- Same payment allocation policy as top issuers

Riverview Community Bank Visa (offered through Elan Financial Services) 6/2009

- 28.99% penalty rate (more than double the regular rate)
- $2 minimum finance charge (the highest seen with large banks)
- $2.50 account management per month if you have a closed account with a balance
- Cash advance fee of 4% (higher than most of the top issuers)
- Late fee: $39 for balances $250 and over (as high as the highest among top issuers)
- Other fees and practices are in line with the more aggressive of the top issuers
- Same payment allocation policy as top issuers

As credit card abuses became widespread, agencies in charge of oversight showed very little interest in credit card problems or other issues that affected consumers. From 1997 to 2007, the Federal Reserve Board reported just nine formal enforcement actions against banks by the OCC under TILA. An academic researcher found that most OCC actions regarding violations of consumer lending laws have targeted small national banks, even though "ten large banks accounted for four-fifths of all complaints" received by the OCC's Customer Assistance Group in 2004. The Customer Assistance Group receives roughly 70,000 complaints and inquiries each year on consumer issues. Despite the hundreds of thousands of complaints and inquiries it fielded between 2000 and 2008, the OCC took just a dozen public enforcement actions during this span for unfair and deceptive practices relating to home mortgages, credit cards and other consumer loans combined.[32]

Finally, in December 2008, the FRB did take action to address some of the practices listed above. By then, credit card holders had paid billions of dollars in unnecessary fees, making millions of families more vulnerable to the negative effects of the economic recession.

5. ***Failure to address abusive overdraft practices***

Today, consumers pay well over $20 billion a year in overdraft fees—more than the financial institutions extend to cover the overdraft loans themselves—and that figure is rapidly rising.[33] From 1997 to 2007, the average overdraft fee charged increased by over 75 percent.[34] The most common triggers of overdraft fees are small debit card transactions that institutions could easily deny for no fee.[35] Institutions pay consultants for specialized proprietary software and implementation strategies designed to increase overdraft fees. And the majority of institutions enroll customers in these programs without their affirmative consent.

The federal banking regulators first recognized overdraft practices as a potential problem at least as early as 2001. In the years since, as regulators have failed to take meaningful action to curb abuses, overdraft practices have grown exponentially worse.

In 2001, the OCC refused to give a bank a program evaluation/comfort letter in connection with an overdraft program that a third party vendor was marketing to depository institutions.[36] Instead, it articulated a number of compliance concerns about the program, while devoting its greatest discussion to FTC UDAP, supervisory and policy concerns. The letter noted "the complete lack of consumer safeguards built into the program," including the lack of limits on the numbers of fees charged per month; the similarities between overdraft fees and other "high interest rate credit;" and the lack of efforts by banks to identify customers incurring numerous overdraft fees and meet their needs in a more economical way. In 2002, the FRB issued a preliminary request for comment on overdraft programs.[37]

Four years later, the regulators issued joint guidance addressing overdraft fees. Rather than conducting a rigorous UDAP analysis, the agencies transformed what the OCC had in 2001 described as policy issues, many created by the "complete lack of consumer protections," into "Best Practices."[38] The guidance recommended several practices CRL has strongly supported, including requiring affirmative consent to overdraft coverage; considering limiting overdraft coverage to checks alone (i.e., excluding debit card and other transaction types); alerting customers before an overdraft is triggered; establishing daily limits on fees; and monitoring excessive usage.

The identification of "Best Practices" in the proposed rule had generated requests from some industry representatives for clarification on whether examiners would treat the best practices as law or rules when examining institutions offering overdraft protections.[39] The agencies clarified: "The best practices, or principles within them, are enforceable to the extent they are required by law."[40]

There is little evidence to suggest that the OCC has instructed its examiners to even evaluate overdraft practices—much less attempted to encourage best practices. A search of the OCC's Compliance Handbook for depository services finds no reference to the guidance. And a search of the OCC's "Other Consumer Protections" Compliance Handbook finds no reference to overdraft protection, or, indeed, to the FTC Act's UDAP provisions at all. Moreover, the OCC's message to its banks' customers has essentially been that the banks can do as they please. For example, the OCC's online consumer reference "HelpWithMyBank" has a FAQ on its overdraft section concerning transaction posting order (generally manipulated by banks to maximize overdraft fees) that simply mirrors the line we so often hear from banks—they can post transactions in whatever order they please.[41]

So it's not surprising that, by and large, these best practices have not been followed. There was never a clear signal from regulators that they needed to be followed. And some best practices have only become *less* common since the regulators identified them as such: As recently as 2004, 80 percent of institutions declined debit card transactions when the account lacked sufficient funds;[42] today, 81 percent of banks surveyed by the FDIC allow debit card and ATM overdrafts, charging a fee for each overdraft transaction.[43]

In 2005, the FRB also chose to exempt overdraft loans from cost of credit disclosures by addressing overdraft programs under the Truth in Savings Act rather than the Truth in Lending Act,[44] meaning consumers receive no disclosures to aid in comparing fee-based overdraft to far less expensive alternatives.

The latest proposed regulatory action on overdraft is a FRB proposal suggesting two alternatives with respect to debit card purchases and ATM withdrawals.[45] The first alternative requires institutions to give customers the right to opt out of overdraft coverage; the second requires institutions to obtain customers' affirmative consent to coverage before charging the customer an overdraft fee. Even if the stronger opt-in alternative is adopted, the FRB's approach is inadequate. It does not address checks and electronic payments at all; it condones the approval of debit card overdrafts that could easily be denied for no fee; it does nothing to address the dramatic disparity between the amount of the overdraft and the amount of the fee institutions charge for covering it; and it does nothing to address the excessive number of overdraft fees borne by a relatively small portion of consumers who are least able to recover from them.

IV. HR 3126's preemption provisions must not be weakened. Preemption was part of the problem, and more of it cannot be part of a wise solution.

One way to leave the nation vulnerable to a repeat of the financial crisis is to do more of the same and call it "reform." For the last two decades or more, preemption (i.e., overriding state laws) has been touted as a cure-all to make credit delivery efficient, enhance competition, and democratize credit. Just in the past few days, the same record has started playing over again.[46] Amidst the rubble of a collapse only narrowly averted, in part by taxpayer bailouts and cheap government loans, some of the very same institutions that got those bailouts and loans, and their primary regulators, want to go back to the *status quo ante* or even to expand preemption further.

But the facts speak for themselves. Preemption was part of the guidance system that drove us to the precipice. Not all of it, granted, but part of it absolutely. And make no mistake, the last thing taxpayers want to hear is that the institutions want to return to business as usual, and that Washington let it happen.

Let's look at some of those facts, first as to the supposed benefits of preemption.

A. Examining the purported benefits of preemption.

The improved access to credit was facilitated by the abandonment of underwriting. That led to a credit bubble that, in turn, fed the housing bubble. It also created over-leveraged households struggling under mounds of debt, making full recovery from the recession more risky. The debt-to-disposable income ratio for households more than doubled from 60% in 1980 to 133% by 2007.[47]

The "democratization of credit" was vaunted as improving homeownership rates, without any empirical support for that claim. But the data belied that claim even before the foreclosure crisis, and the homeownership rate has now declined to 2002 levels.[48] According to Census data, Black homeownership peaked at 49.7% in 4Q2004 and is at 46.5% as of 2Q2009. It dropped a full percentage point between 3Q2008 and 4Q2008.

The supposed benefits to competition, too, are overstated. The most deregulated segment of the consumer credit market, courtesy of preemption, is the credit card market. Yet just three issuers control nearly 60% of card balances.[49] Nearly half (47%) of America's 708.6 million cards last year were issued by one of these three banks, and an astonishing 82% by just the top 10 issuers.[50]

Testimony to a Congressional Antitrust Task Force last year noted that the credit card industry met Department of Justice merger guidelines for a "highly concentrated" industry.[51]

Uniformity can be a benefit or a harm—or neither. Uniformly bad practices, unchecked, as we have seen, create a self-feeding cycle that can spiral out of control. But, sometimes uniformity is simply not an appropriate polestar. There is a national market for the traffic in commercial paper relating to mortgages; but what lies behind that paper is as local as anything comes – a family's home, a neighborhood, a community. Mortgages may be a national market; but real estate is most decidedly local. Sometimes, uniformity is just a red herring.

B. Examining the contributions to problems in the financial services market by beneficiaries of preemption.

The "we didn't do it" claim rings hollow. The banks, and the federal banking regulators that have marketed their charters by touting preemption, have repeatedly argued that they did not create this mess. But they stand by a table of shattered crockery and deny breaking a cup.

We cannot cover all the examples relating to preemption and irresponsible practices made easier by preemption, but here are a few.

*1. **Preemption, federally chartered institutions, and risky mortgages.***

Federally chartered banks and their supervisory regulators repeatedly deny originating the "subprime mortgages" that first melted down. But that is a half truth, at best. The mortgage market that went awry because of irresponsible underwriting and reckless selling was the *non-prime* market, not just the higher-cost "subprime" loans. Because the irresponsible subprime activity started earlier than the equally irresponsible Alt-A market, that wave was the first to crash. But the Alt-A wave began to follow shortly thereafter.

The Alt-A market ballooned from $85 billion in 2003, to $938 billion in just three years. In 2006, that $938 billion Alt-A market was a third higher than the $600 billion subprime market. Together, that $1.5 trillion *non-prime* market dwarfed the $990 billion prime market in 2006.[52] Concentrated in states with higher housing prices, the explosion of these loans contributed to the bubble.

Many of the so-called non-traditional loans—interest-only loans and payment option ARMS (POARMS)—are considered "Alt-A" loans, instead of "subprime loans." These loans are typically layered with risky features—underwriting only to the teaser rates, adjustable rates, prepayment penalties, negative amortization, yet, astonishingly, *only 17%* of payment option ARMS originated between 2004-2007 were fully documented.[53]

Neither federally chartered banks nor their federal supervisory regulators can credibly deny that they did not participate in the *non-prime* mortgage meltdown, when all non-prime lending is considered. Four of the top seven Alt-A originators between 2004-2007 had federal charters, and enjoyed both the benefits of preemption, and light touch regulation.[54] While the federal regulators issued a non-traditional "guidance" in 2006, there is little evidence that it was enforced. Professor

Patricia McCoy has detailed in other Congressional testimony, the litany of familiar names of federally chartered banks that were involved in risky non-prime lending – Bank of America, Wachovia, Wells Fargo, among them. In one Alt-A prospectus, Wells admitted "that it had relaxed its underwriting standards in mid-2005 and did not verify whether the mortgage brokers who had originated the weakest loans in that loan pool complied with its underwriting standards before closing." (By mid-2008, nearly a quarter of that loan pool was delinquent or in default.)[55] The three largest failed institutions in 2007 and 2008—IndyMac, WaMu and Downey—were all federally chartered institutions, free from state law restraints.

That list of federally chartered institutions that contributed to the mess also includes National City Bank, and its then-operating subsidiary, First Franklin. National City asked for the OCC's 2003 determination that state anti-predatory lending laws would not apply to national banks or their op subs, subsequently memorialized by sweeping preemption rules in 2004. First Franklin alone had 4.4 % of the subprime market share in 2005.[56] Six years after obtaining the OCC's preemption determination, First Franklin made the OCC's own list of the "Worst Ten in the Worst Ten"—the originators with the largest number of foreclosures in the metropolitan areas with the highest foreclosure rates – a list which includes two other significant subprime lenders under OCC watch.[57]

2. Credit cards and preemption.

The sector of the credit card market that is perhaps the most completely deregulated, thanks to preemption, is the credit card market. The combination of the judicially-created right of exportation under the National Bank Act, augmented by OCC and OTS regulations, mean that federally chartered card issuers are almost completely immune from state regulation. This preemption was expanded to state chartered banks by Riegle-Neal, which permits state banks to do whatever a national bank is free to do when it operates interstate. That, in effect, means that, until 2008, the OCC set the gold standard for what was permissible in terms of credit cards.

Not surprisingly, then, institutions supervised by federal regulators dominate the credit card market. We noted above that three institutions together, hold about 60% of the credit card account balances – Bank of America, Citi, and Chase, all national banks.[58] The majority of the top 10 credit card issuers are federally chartered.

Under this federal preemption regime and the eye of the federal supervisory regulators, the abusive practices grew so widespread and so out of hand that the Fed, the OTS, and NCUA along with Congress, finally stepped in. That hardly qualifies as a success story for preemption.

Overdraft and preemption: By definition, only depository institutions can engage in abuses related to deposit accounts. I earlier detailed the dismal history of federal regulatory failures in this regard. We know that states would like to respond to their citizens about this abuse. New York, in fact, did limit these fees. But because federally chartered institutions did not have to comply, the race to the bottom kicked in, and the state-chartered institutions got a "level playing field," allowing them to do what the national banks could do.[59] This is a perfect example of the silent, but potent side effect of deregulatory preemption—it encourages a race to the bottom.

3. Preemption and payday lending.

While more and more states have recognized how the debt treadmill of short-term, high-rate loans wreaks havoc on family finances, at least three national banks are offering payday loans of their own – and not the affordable small loan alternatives that the FDIC has suggested.[60]

4. Preemption by product, not charter.

The above examples illustrate how the so-called "charter" preemption has undermined consumer protection and allowed bad practices to spread. (Charter preemption is available to federally chartered institutions, and has been aggressively expanded by their supervisory regulators, the OCC and the OTS.). But any discussion of the contributory role that federal preemption played in the mortgage crisis cannot stop with the charter preemption. The 1982 Alternative Mortgage Transaction Parity Act (AMTPA) also cast a long shadow into the debacle of the mid-2000s. AMTPA preempts the right of states to regulate such "creative financing" terms *even for state-chartered non-bank mortgage lenders*

Adjustable rate loans, interest- only loans, and negatively amortizing loans flooded the market, and were made without regard to whether they could reasonably be expected to pay. Uniformity in allowing appreciation-based lending was a bad idea in housing bubble states, but preventing states from acting on such products where appreciation could not even support such loans in the best of circumstances was disastrous. In other words, the very kinds of disastrous non-standard loans that displaced sustainable, fixed mortgages, were *encouraged* by a 27-year old federal preemption law.

These are just a few examples of the myths about preemption, and about the role played by entities that enjoy the benefits of preemption at consumers' expense. There are three distinct kinds of preemption provisions in H.R. 3126, and all three are important to assuring fair and balanced regulation over the long term:

1) The CFPA's rules would preempt inconsistent state laws, and would define inconsistency in a manner similar to existing federal consumer protection laws;

2) H.R. 3126 would restore the state of "charter-preemption" (applicable to federally chartered depositories) back to approximately 2003, before the bank supervisory agencies became even more aggressive about pushing the preemption envelope (The OCC is 1 for 1 on these efforts in the Supreme Court, but other key preemption rules have not been examined by the Court; and

3) H.R. 3125 would make long-overdue amendments to the 1982 AMTPA preemption described above.

C. Broadening preemption would pose a high risk of making matters worse.

We understand that the preemption provisions of the bill are controversial, but we believe that they are central to assure that there are fair and balanced rules of the game over the long haul. The notion of state regulation as a drag on credit is utterly belied by experience. State regulation of consumer credit started with small-loan laws in the first two decades of the twentieth century; retail installment sales acts were the underpinning of the growth in the post-war boom. Indeed, the problems in the consumer credit market that ultimately destabilized our financial system tracked the period of the *greatest* federal preemption. Further, some of the most damaging abuses have been in the market segments where that preemption was most prevalent – mortgages and credit cards.

The proposed changes in governance of the CFPA would put the Agency's policy in the hands of one person. While we believe that overall, an Agency with the American family as its "customer" instead of the financial provider, is structurally more likely to be an honest referee, it would be unrealistic to assume that sometimes the Agency's director would not make some bad calls. It is imperative for the states to be able to act as back-up referee.

A perfect example is the payday lending industry. The green light laws that authorized payday started in the states, typically with some ostensible protections. But experience showed that the protections in those green light laws were insufficient, miring customers in a quicksand of loan-shark priced debt. States increasingly looked at that data, looked at the consequences, and started passing yellow and red light laws. We believe that the CFPA will monitor the market for evidence about the impact of developments, and use that evidence to guide its actions. But if it fails to act, or, as has been known to happen, takes a decade to act, states would be helpless to prevent their citizens from the loss of billions of dollars if the CFPA were to be preemptive.

Another example can be taken from the recent history books. HUD has the authority to address the yield-spread premium for mortgage brokers that became such an important distorting fact in flooding the market with risky loans instead of sustainable ones. In fact, it took a step in that direction ten years ago. But it later took a step back again. The rest is history. But, as the pernicious effect of yield-spread premiums became more obvious, several states stepped up. The Massachusetts Attorney General addressed the unfair and deceptive practice of yield spread premiums, promulgating rules (effective January 2008) that prohibited broker compensation when there was a conflict of interest, such as when broker compensation increases based on the terms of the loan. Within a year North Carolina had followed suit, banning YSPs on all subprime loans. These state laws may well be the impetus behind the Federal Reserve's recent proposed rules banning all compensation based on the terms of the loan.[61]

If a less than vigorous referee at the helm of the CFPA were to do something similar to what HUD did, preemption would prevent the states from acting, and problems could metastasize. It also means that when the CFPA does act, it would do so without the benefit of lessons learned from these state law pilot projects. We believe that the federal consumer protection and equal access federal landscape would be greatly improved with the enactment of the CFPA. As long as it does its job well, then states will have no reason to depart from that federal floor. Not all local problems will become national, and Washington should not set itself up as the arbiter of all local solutions. States must also have the flexibility to be first responders, dealing with local problems before they get out of hand. And experience has shown that it is from these state solutions that we learn what works, and what doesn't, based on real experience, not arcane models or unfounded fears. Many of the federal consumer protections, among other laws, were adopted and adapted from successful state laws. There is no basis in experience or policy in a federalist system like ours to centralize consumer protection exclusively in Washington.

V. The CFPA should have full jurisdiction over financial activities irrespective of the identity of the provider; if there must be exemptions, they should be narrowly drawn.

Recent proposed changes to HR 3126 offer some exemptions to certain business sectors. As we understand this proposal, it would:

- exempt retailers, regardless of size, from CFPA's organic rule-making, and all of its oversight and enforcement duties, and from assessments. Rule-making authority under existing transferred statutes would apply to the extent that the retailers are covered now by those statutes, but without oversight or enforcement by the Agency;

- exempt auto dealers from rule-making, oversight and enforcement duties, and from assessments as to the part of the transaction involving the sale of the vehicle, but would retain full CFPA jurisdiction when dealers engage in financial activities,

- exempt credit reporting agencies as to their primary functions., and

- limit CFPA jurisdiction over certain other professions to their activity in regard to financing products.

Meaningful financial reform will be beneficial to legitimate small businesses and financial providers of all sizes, reducing the necessity of competing against market distorting forces of unfair and irresponsible businesses. But meaningful financial reform will only come if we take care to assure that it is not riddled with loopholes.

One of the fundamental purposes of consolidating the existing fragmented system is to ensure that the regulation applies to the activity, not to the provider. Exceptions by category of provider run counter to that purpose, which we believe is the preferred approach, and therefore any exceptions should be few, and carefully drawn.

Recommendation: We believe one provision could help ensure against the possibility that exemptions are exploited. The Act should assure that there are periodic reviews of these exemptions to determine whether they are responsible for loopholes that undermine the integrity of the market and the implementation of the goals. Congress should give the Agency authority to close those loopholes, a tool used successfully in the past to close one of the most serious statutory loopholes in the original HOEPA law.[62]

A. The merchant exception should be narrowly crafted to balance the interests of small business with the clear need for sensible regulation of the consumer credit market.

We understand the fears of legitimate small businesses facing strains from the recession and from high health care costs. But this partial exemption covers much more than the butcher's tab or the local independent dress shop's lay-a-way plan.

The exemption would forbid the CFPA from *enforcing* existing federal consumer protection laws that *currently apply* to merchants, retailers and sellers -- including giants such as WalMart and large department stores. (The exception to the exemption allows only for rule-making under enumerated statutes, not investigation or enforcement under them.) The exemption would prevent the CFPA from addressing unfair and deceptive practices in connection with seller financing of goods or services, even though such unfair and deceptive practices are already banned under the FTC Act.

Giving certain industries an exemption also leads to confusing and inconsistent treatment of similar products and tempting loopholes that scammers will work to exploit.

- Some payday lenders have described themselves as "catalogue" sellers or Internet service providers.[63] Does Section 124 create a bizarrely fragmented system whereby payday lenders who admit that's what they are would be subject to CFPA's full panoply of authority, while payday lenders who disguise themselves as merchants would be under the FTC's jurisdiction?[64]

- Would individual merchants or a collection of merchants at a mall offering store or mall gift cards with hidden fees that eat up the value of the card be subject to FTC jurisdiction while branded gift cards issued through a bank are subject to CFPA jurisdiction?

- How will the twin goals of level-playing-field rules governing the activity and consistent enforcement be met if two-party merchant-issued credit cards have a different regulatory scheme from the retail-branded cards that are actually issued by banks?[65]

- What would be the regulatory scheme applicable to a Wal-Mart that issued payment cards and its own two-party credit cards,?

- What of the "feeder merchants" – the retailers who sells goods with "seller-financed" paper but who assign the installment sales agreement to finance companies? These kind of transactions are often associated with abuses, including misleading "no interest for x months' deceptive practices, and with the subsequent "flipping" by the finance companies to whom they feed the account.[66]

Compounding the regulatory disparities, the providers subject to FTC jurisdiction are not subject to routine monitoring (an authority the FTC does not have), while the non-merchant providers of the same services subject to the CFPA authority would be.

We recently heard of a new program which illustrates the danger of categorical exemptions like this one. In a particularly disturbing development, some large, for-profit colleges have begun making a lot of their own private loans directly to high-risk students.[67] For example, in a recent call with investors and analysts, Corinthian Colleges, Inc. said it plans to make $130 million of such loans in the current fiscal year, on top of $120 million last fiscal year. They fully expect a shocking 56 to 58 percent of the borrowers to default. Yet they consider these loans good investments because they will increase enrollment and with it a profitable flow of federal grant and loan dollars that outweighs the planned writeoffs. Corinthian owns more than 80 colleges across the U.S. through its Everest brands.[68] According to the Associated Press, ITT Education Services, Inc. also expects to make $75 million in loans directly to its students this calendar year, and Career Education Corp. expects to reach $50 million.[69]

The proposal to allow the CFPA might to retain rule-making authority under some transferred enumerated statutes is helpful, but not adequate. The absence of its organic authority may leave gaps. For example, the federal Debt Collection Practices Act does not cover creditors collecting their own debts, and the FDCPA explicitly denies any rule-making authority. Consequently, citizens being harassed for general purpose credit card collections by a collection agency have one set of protections; while citizens subjected to the very same conduct by in-house collectors for a large retailer on its own credit cards would have no federal protections. (And, if the preemption provisions are weakened, they might even be deprived of any state protections.)

Recommendation: Any exemption should be limited to ensuring that small merchants are not subjected to significant new burdens, without carving out any new exceptions to current laws. Thus, merchants, retailers and sellers who do not have a substantial credit business should not be subject to examinations or to assessments. But the CFPA should be able to exercise its full authority under the enumerated statutes and to address any unfair and deceptive practices regardless of the identity of the actor.

B. The proposed auto dealer exception may be difficult to implement, and its interaction with the merchant exception must be clarified.

We commend the effort in the proposed auto dealer exception to separate the dealer's role as seller of goods, and as a provider of financial products. That is fair and necessary recognition of the key role that auto dealers play in the auto finance market. Overall, dealers are the gatekeepers for financing on an estimated 41 percent of the vehicles sold.[70] In many respects, dealer-assisted auto finance operates in a fashion parallel to third-party mortgage originations. Abuses in that market bear a remarkable similarity, as well, and are equally rampant. In Appendix B to this testimony, we describe such areas of abuse—abuses which are as harmful to honest competitors as they are to consumers: the "yo-yo", which involves changing the terms of the financing after the sale; dealer mark-ups, which are basically yield-spread premiums on car loans, with the dealer passing on higher interest rates than the consumer qualifies for to earn more fees; and the "buy-here, pay-here subprime market." It is critical that the CFPA be able to bring its full range of authority to bear on these providers of financial services, including rule-making, oversight, and enforcement.

Operational challenges: One concern is that when the prospective buyer does not bring her own funds to the dealership, the sales and negotiations do not fall cleanly and easily into a sale of goods phase and a sale of financing phase. They more often than not become intertwined. "Packing" an auto sale, for example, can be done with a set of bundled add-ons that include both non-financial services and non-financial services, (e.g. both service contract and "gap protection", that insures against a deficiency.) The valuation on the trade-in (ostensibly part of the goods sale part of the transaction) may be inflated so as to disguise from both the buyer and a subsequent assignee of the credit contract that the loan amount actually refinances the balance on the trade-in, as well as the purchase price of the car. (For more examples, see Appendix B.) How overlapping jurisdiction would disentangle these common scenarios is difficult to see.

Lack of clarity about the intersection between the dealer exemption and the general merchant exception. Auto dealers are merchants, and it is quite common for the dealer to be the "creditor" in the sale. When the dealer is involved in the financing, it is common for the retail installment sales contract to be between the dealer as both "seller and creditor." The dealer does not intend to keep that loan, but rather will assign it immediately or within a few days to an indirect lender. The assignee often has approved the loan before the consumer signs the contract, so the assignment can be immediate. (When the deal hasn't been approved by a potential assignee first, the abuse called the "yo-yo" that we describe in the Appendix comes into play.) Additionally, the dealer and the creditor are the same in the "buy-here, pay-here" subprime auto market. Dealers therefore are quite often sellers who would also fall under the merchant exception of proposed new Section 124(a).

The question is what happens when the exception to the auto dealer exemption under proposed new Section 124(g)(2) is applicable. Does it default to the merchant exception? Or does it default to standard CFPA jurisdiction. This must be clarified, and it should be clarified to full CFPA jurisdiction. Otherwise, there will be significant gaps, and consumer protections and fair access would be undermined in this large section of the consumer credit market. Oversight would be missing (because the FTC does not have that authority), and enforcement would be fragmented.

Even the CFPA's rule-making authority under transferred statutes would leave gaping holes. The most critical example is that Truth in Lending's $25,000 threshold has never been updated for inflation, and now the average motor vehicle loan is not even subject to TIL: the average amount financed for a new car loan crossed that $25,000 threshold.[71] (We and others have long urged Congress to make inflation adjustments to the TIL threshold for this reason.) The transferred federal Fair Debt Collection Practices Act would not apply, as it only applies to third party collectors.

Recommendation: At a minimum, it should be absolutely clear that the proposed dealer exception is the sole exception applicable to dealers engaged in financial activities, not the merchant exception.

C. Credit Reporting Agencies

Credit reports are fundamental to the financial life of American families – not only to what they pay for credit, or whether they get it at all, but to their job prospects, their ability to rent an apartment, and what they pay for insurance. Yet despite the FCRA, the system remains rife with inaccuracies, as documented by multiple studies with some finding serious errors in 25% of credit reports. Furthermore, the dispute system that Congress carefully crafted to enable consumers to correct errors has been turned into a travesty of automation, with the credit reporting agencies (CRAs) spending pennies on each dispute to do less than the bare minimum that we believe is required under the FCRA.

D. Other exemptions

We are pleased to see that the proposed exemptions for tax preparers and attorneys strike a reasonable balance. As you know, tax preparers are the brokers and sales channel for the high cost Refund Anticipation Loans that are often sold deceptively, and even undermine the earned income tax credit program. And attorneys are unfortunately often involved in equity-skimming schemes, foreclosure prevention scams, debt collection abuses and currently in loan modification scams. We understand these exceptions to permit the CFPA to regulate such entities when they participate in such activities to the same extent as it does non-lawyers and accountants engaging in the same conduct.

VI. The agency should have the authority to offer carrots as well as sticks to ensure that consumers have the full range of choices, including the safe ones.

One of the significant proposed changes to H.R. 3126 would assure that the Agency cannot mandate a provider to offer meaningful choice of products to consumers. We are not going to urge you to reconsider that. But we do believe that one of the worst features of the past crisis was that the proliferation of unsound, financially de-stabilizing products and practices actually *deprived* consumers of choice. We have often pointed out here and elsewhere, for example, that the lop-sided rate of prepayment penalties in prime loans (rare) compared the high rate in subprime belied the notion that borrowers "choose" prepayment penalties. Investigations and enforcement actions confirmed that these were just part of the loan package given, partly because they were linked to higher compensation for the originator.

Earlier in my testimony, I cited other examples of the way in which bad practices and products crowded out responsible, sustainable products in relation to credit cards and deposit accounts as well. We can avoid that without mandates. Concrete, certain, and measurable market incentives to encourage responsible practices that are sustainable over the long term is consistent with the consumer choice, and is "win-win" for American families, for providers of financial services, for investors, and the economy.

At the same time, responsible providers can be rewarded for being part of the solution instead of part of the problem. Less regulatory burden, and lower compliance costs reward those providers who make sure that Americans really have a sustainable option as well along with the options that are riskier for them.

The kind of practices and products that overwhelmed fair competition and America's economies cost everyone more when they get out of hand. Those who create greater risks for the economy, hurt genuine competition and deprive consumers of real and honest choices should absorb more of the cost of making sure things don't spin out of control again.

A. The Agency Should Have the Power to Offer Working Market Incentives And Reduce Regulatory Costs

Risky financial products metastasized to dominate the market because, in the short term, the market thought the potential gains outweighed the potential costs, both in operational losses, reputational losses, and litigation or regulatory risks. That is why the head of the first major mortgage lender to suffer an enforcement action for targeting minorities, women, and the elderly predatory loans just turned around and started a second company that targeted customers for predatory loans.[72] The regulatory and litigation risk did not outweigh the potential rewards. We can change that dynamic with "win-win" incentives: enhancing consumer choice and rewarding responsible providers.

Reduced regulatory burden for simple, comprehensible, and sustainable products and practices

- These products and practices would be subject to minimal supervision and reduced reporting. Regulation would be minimal, if any, in any event. This offers relief from both regulatory burden and regulatory risk.

"Risk-based pricing" for assessments to pay for supervision[73]

- We know that too little regulatory attention was paid to risky products and practices, one of the causes of the crisis. And we know that those who engage in those practices ultimately cost the public more than the ones who do not. Just as higher-risk drivers have to pay more for auto insurance, and higher-risk borrowers have to pay more for credit, it is only fair to ask those who put more of the higher risk practices out into the economy should pay more to make sure they do not again lose control and damage us all.

VII. There must be adequate means of holding those who violate the law accountable.

We continue to support the right of the state attorneys general to enforce CFPA rules. This is a vast country with over a hundred million households and about $13 trillion in household credit outstanding. It is unrealistic to suggest that federal enforcement alone is adequate. Consumer protection is a traditional state function, and states have considerably more experience in enforcement than the federal financial regulators. This right should be an essential feature of this reformed system.

We also strongly recommend that consumers have a private right of action to enforce the Agency's rules. Public enforcement, even with state concurrent enforcement, will never have adequate resources. That means that many consumers would never get relief at all, or not when needed. The existing foreclosure crisis is a prime example. Public enforcement officials cannot defend individuals in foreclosures. To deny private enforcement is to deny a homeowner the benefit of these consumer protection and fair lending rules at precisely the time when it is most important.

Conclusion:

Thank you for the opportunity to share my views. I look forward to working with you and the Committee to help make our financial markets work again.

APPENDIX A

Failures on Safety and Soundness Linked to Failures on Consumer Protection

The desire of the OCC and the OTS to protect the institutions they regulate and their reluctance to enforce rules and regulations was not limited to consumer protection. In safety and soundness and other areas, there have been similar lapses. In some instances these lapses also illustrate how a more focused consumer protection agency could have mitigated the scope of the crisis.

- ***It wasn't the market downturn.*** Defenders of the OCC and the OTS have argued that the banks and thrifts under their supervision were largely victims of unforeseeable market downturns. This argument is belied by the superior performances of banking institutions overseen by other regulators. State-chartered thrifts and banks performed significantly better during the crisis in terms of loan quality than OTS-supervised national thrifts and OCC-supervised national banks, FDIC data shows. As of Sept. 30, 2008, the rate of 1-4 family residential loans from national banks that were past due or in "nonaccrual status" was *twice* that of state banks; federal thrifts' rate was *more than four times* that of state thrifts.[74]

- ***Countrywide: A three-part failure.*** The implosion of the nation's largest mortgage lender is instructive, given that three of the main federal regulators – the OCC, the OTS and the Federal Reserve – shared responsibility for overseeing Countrywide Financial and Countrywide Bank. Investigations by CRL and law-enforcement authorities produced compelling evidence that Countrywide targeted borrowers for unfair and unsafe loans that have left many struggling to save their homes.[75] Under the watch of the OCC and, later, the OTS, the company boosted its loan volume by making large numbers of poorly underwritten pay option ARM mortgages and home equity lines of credit—loans that were approved with little scrutiny of borrowers' long-term ability to stay current as monthly payments began to rise.[76] Investigators with the California Attorney General's Office concluded that Countrywide's non-bank subsidiary misled borrowers on a widespread basis; obfuscating, for example, the true terms of its Pay Option ARM loans by misrepresenting the impact of negative amortization and the amount of time the interest rate would be fixed.

- ***Inspector General Reports Criticizing the Agencies.***

    - Reports by the Treasury Department's inspector general have supported the conclusion that the OCC did a poor job of making sure that banks underwrote loans responsibly. ANB Financial failed in 2008 due to risky lending, unsound underwriting and other problems; the inspector general found that the OCC identified most of ANB's problems in 2005, but it "took no forceful action" until 2007, when it was too late to save the bank.[77] The inspector general found a similar pattern in the 2008 failures of FNB Nevada and First Heritage Bank; the OCC knew about problems as early as 2002, and found additional problems in 2005, 2006 and 2007, but failed to take timely and aggressive action to curb the affiliated institutions' risky practices.[78]

- In 2008, the OTS presided over a flurry of unprecedented financial meltdowns. Five thrifts with assets totaling $354 billion collapsed, led by Washington Mutual Savings Bank, the largest banking failure in American history. Seven others holding assets totaling another $350 billion have been sold or were caught up in their parent companies' bankruptcies. The failures of these institutions – and the harm they caused consumers – were the fruits of years of inaction by the OTS.[79] The OTS turned a blind eye as WaMu, IndyMac Bank and other thrifts engaged in a spree of unsafe, abusive lending.[80] A series of inspector general reports have concluded that the OTS failed to rein in reckless lending practices at the institutions it oversaw. The reports cited serious supervisory shortcomings leading up to the failures of Superior Bank[81] in 2001, NetBank[82] in 2007 and IndyMac[83] and Downey Financial[84] in 2008. The reports criticized the OTS for moving too slowly to respond to obvious problems at the thrifts and for failing to quell the institutions' breakneck lending strategies.

- The inspector general also found that the OTS was so pliable in its supervision that it allowed some thrifts to hide the consequences of their imprudent business strategies by falsifying financial reports. The OTS expressly allowed two institutions to backdate capital infusions, and took no action against four others that did so without permission. [85]

- In 2005, a group of senior risk managers crafted a plan requiring that loan officers document that borrowers could afford the full monthly payment on option ARMs. A former bank official told the *Washington Post* that the OTS signed off on the plan, but "never said anything" after top bank executives rejected the plan.[86]

APPENDIX B

Auto Dealers: Lack of Oversight Costs Americans Billions Each Year

✓ **The "yo-yo" – bait and switch financing in the dealership**

Car buyers who leave the lot with a vehicle and a signed car loan are often surprised to some days later (or sometimes weeks later) get a call saying the "financing fell through," and they have to either return the car, pay it in full, or come back and sign new car loan papers at more expensive terms.

Dealerships sometimes do this simply so as not to lose a sale. A buyer who wants to "go home and think about it" may decide against it. Waiting to get approval from the lender to which the dealer will subsequently assign the contract may result in a lost sale, so the dealer closes the window by binding the consumer to a one-sided contract – the consumer is bound, but not the dealer. If the dealer can't sell that contract to an assignee at those terms for that buyer, the dealer considers itself not bound.

Returning the vehicle at that point may be difficult for the consumer. At a minimum, he may have become psychologically committed to the transaction, or economically invested, as with purchasing new insurance. But the more egregious situation is where the dealer pulls the string on the yo-yo back *after* it has disposed of the buyer's trade-in, so there is no way to return both parties to *status quo ante.*

CRL's research, unfortunately, gives some weight to the notion that yo-yo sales have a bait and switch taint to them. Sadly, it adversely affects low and low-moderate income buyers, and buyers with lower credit scores. We found that, of those who used dealer financing for their last purchase, 1 in 8 buyers with an income less than $40,000, and 1 in 4 with an income less than $25,000, reported experiencing a yo-yo deal.[87] While at first blush it might be argued that it is simply harder to find financing for lower income buyers, that seems overly simplistic. Assuming again that the credit professionals at the car dealers are familiar with underwriting standards and consequently with what should be an affordable credit sale, as they should be, then it is difficult to understand why there is such a distorted impact. But more to the point, those who report being "yo-yo'd" pay more than equally positioned buyers who were not, on average, five percentage points more.

✓ **Subprime auto market: "Buy-Here, Pay-Here"**

Buy-Here, Pay-Here (BHPH) dealerships are geared toward borrowers with no credit or damaged credit, typically advertising used cars and less stringent underwriting standards. The dealerships finance borrowers in-house, but because of higher risk (or just because the customer wandered onto the lot), borrowers may see rates between 12 and 25 percent. The BHPH industry has had a history with predatory lending and accusations of selling overpriced and faulty cars with this expensive credit.

In this market, the sale of the vehicle is more often secondary to the sale of the credit. According to one expert,

> **"BHPH has always been a finance business, not necessarily a sales business. What we're seeing now with the subprime market having the dent in the housing side and also from the automotive side has actually helped BHPH because it is forcing some of those customers down to our financial level."[88]**

Realizing opportunities to capitalize on subprime borrowers, franchised and independent dealers are creating BHPH branches to have more options.[89]

✓ **Yield spread premiums: reverse competition in auto loans**

Auto dealers typically mark-up the interest rate on the car loan over that for which the buyer qualifies. The practice imposes substantial extra costs on consumers, just as the analogous "yield-spread premium" does in the mortgage market. In the mortgage market, we know that perverse market incentives encouraged brokers to steer their clients toward more expensive loans than the borrower would qualify for, because the brokers could increase their own fees by doing so. Because the dealers get to keep all or part of the mark-up, this yield-spread premium (some call it more simply a kickback), this creates a "reverse competition" dynamic, where the intermediary has an incentive to steer the consumer to a higher rate option.

While dealerships argue that these yield spreads are compensation for arranging the financing, that argument does not justify the practice nor the cost. There is simply no legitimate reason for a dealer to receive more compensation for putting a consumer into a 10% loan than for putting her into a 9% loan. The only purpose the yield-spread premium serves is to incent dealers to squeeze extra interest payments out of their unknowing consumers. The abusive nature of the practice is intensified because consumers don't know about it or about how much it costs. Yet it is not a practice that can be cured by disclosure, as testing by the Federal Reserve Board and other agencies has demonstrated with YSPs in the mortgage market. Indeed, the FRB originally proposed to address the issue through disclosure, then withdrew the proposal because testing showed disclosure does not work well.[90] Moreover, the hidden cost is too substantial for that argument to be justified.

CRL research estimates that dealer yield-spread premiums cost consumers an estimated $20.8 billion in 2008.[91] The dealer YSPs add an average $647 to the cost of each vehicle – the rate bumped up an extra .6% for new cars, and 1.8% for used cars. Other data, looking at five major captive auto lenders, reported an average mark up of $989 per vehicle.[92] If evaluated as compensation for a "service", that is a hefty price. Particularly so for a service that, after all, benefits the dealer as much as the consumer: the dealer wants to make the sale, and financing is what lets that happen.

It is not unreasonable for car buyers to assume that the rate they are offered is what they qualify for based on their creditworthiness and the collateral. This is particularly true when the retail installment sales contract actually lists the seller/dealer as the creditor on the deal.[93] Our survey indicated that close to half of buyer-borrowers did not negotiate the *credit* price because they trusted the dealer to give them a good rate.[94] These buyer-borrowers paid a steep price for that trust: it works out to a 2% "trust tax" on the price of credit.

But not all borrowers pay the YSP, so in fact, those consumers who do pay a mark-up pay more than that average. And in yet another parallel to the mortgage market, there is evidence from other studies indicating that minorities were both more likely than whites to be charged a kickback, and that the amount of the kickbacks were larger than the kickbacks whites were charged. Some 54.6% of African American's were charged a kick-back, compared to 30.6% of whites, and the amount of kickbacks charged to African-Americans is about $427 greater.[95] As a result of fair lending litigation over the discriminatory aspect of these mark-ups, some third party lenders capped the amount of the mark-up they permit dealers to around 2-3%.[96] However, that still is a considerable additional cost, and even assuming it eliminates the racially differential impact, it just puts the practice into the category of being an equal opportunity abuse.

DEALER KICKBACK VOLUME BY STATE 2007[97]

Rank	State	New Vehicle Market Share	New Vehicle Kickback Volume	Used Vehicle Market Share	Used Vehicle Kickback Volume	Total Dealer Kickback Volume
26	Alabama	1 26%	$110,476,064	1 65%	$199,560,418	$310,036,482
50	Alaska	0.11%	$9,914,978	0.21%	$26,035,577	$35,950,555
13	Arizona	2.61%	$228,410,644	2.11%	$256,264,673	$484,675,317
35	Arkansas	0.85%	$74,402,532	0.90%	$109,059,142	$183,461,674
1	California	12.11%	$1,057,992,630	11.95%	$1,448,752,786	$2,506,745,416
22	Colorado	1.61%	$140,493,995	1.47%	$178,025,775	$318,519,771
30	Connecticut	1.17%	$102,079,879	1.10%	$132,847,890	$234,927,769
49	DC	0.26%	$22,468,182	0.15%	$18,663,357	$41,131,539
46	Delaware	0.31%	$26,820,950	0.21%	$25,634,228	$52,455,178
4	Florida	5.77%	$504,151,195	5.56%	$674,680,597	$1,178,831,792
8	Georgia	3.70%	$323,065,213	3.36%	$407,671,641	$730,736,855
42	Hawaii	0.33%	$28,538,113	0.30%	$36,936,277	$65,474,390
39	Idaho	0.55%	$48,427,492	0.49%	$58,969,272	$107,396,765
6	Illinois	4.52%	$394,937,006	4.02%	$487,602,027	$882,539,032
16	Indiana	2.18%	$190,226,706	2.02%	$245,349,422	$435,576,129
27	Iowa	1.35%	$118,358,410	1.20%	$145,118,756	$263,477,166
32	Kansas	0.99%	$86,458,502	0.96%	$116,945,478	$203,403,980
20	Kentucky	1.59%	$138,588,600	1.62%	$197,001,967	$335,590,567
25	Louisiana	1.31%	$114,836,696	1.63%	$197,071,081	$311,907,778
41	Maine	0.31%	$27,066,509	0.34%	$41,375,372	$68,441,881
18	Maryland	1.99%	$173,845,933	1.93%	$233,483,543	$407,329,476
17	Massachusetts	2.16%	$189,055,715	1.80%	$218,817,918	$407,873,633
10	Michigan	3.42%	$298,616,832	2.79%	$337,914,435	$636,531,267
24	Minnesota	1.43%	$124,807,602	1.56%	$189,653,997	$314,461,600
33	Mississippi	0.94%	$82,106,608	0.91%	$110,868,246	$192,974,854
19	Missouri	1.67%	$145,547,261	1.88%	$228,497,594	$374,044,855
43	Montana	0.29%	$25,054,850	0.27%	$33,335,045	$58,389,895
38	Nebraska	0.46%	$40,522,425	0.55%	$67,216,943	$107,739,369
31	Nevada	1.12%	$98,264,544	0.91%	$109,960,057	$208,224,601

40	New Hampshire	0.38%	$33,358,404	0.41%	$50,043,793	$83,402,197
11	New Jersey	3.01%	$263,222,301	3.05%	$370,352,203	$633,574,504
36	New Mexico	0.73%	$63,723,788	0.86%	$104,451,505	$168,175,293
3	New York	6.23%	$544,292,611	6.61%	$801,815,017	$1,346,107,627
9	North Carolina	2.97%	$259,900,705	3.34%	$405,176,242	$665,076,947
48	North Dakota	0.20%	$17,265,135	0.21%	$26,004,051	$43,269,186
7	Ohio	3.48%	$303,940,474	3.86%	$467,821,924	$771,762,398
29	Oklahoma	1.09%	$95,642,921	1.20%	$145,106,631	$240,749,552
28	Oregon	1.09%	$94,914,110	1.23%	$149,702,143	$244,616,253
5	Pennsylvania	4.11%	$358,910,664	4.47%	$541,872,721	$900,783,385
45	Rhode Island	0.27%	$23,919,687	0.28%	$33,479,337	$57,399,024
23	South Carolina	1.34%	$117,471,427	1.62%	$197,001,967	$314,473,394
47	South Dakota	0.21%	$18,698,289	0.27%	$32,424,430	$51,122,719
15	Tennessee	2.07%	$180,501,359	2.33%	$282,904,093	$463,405,452
2	Texas	7.85%	$685,630,944	7.90%	$957,842,960	$1,643,473,904
34	Utah	0.87%	$76,438,659	0.88%	$107,201,537	$183,640,196
44	Vermont	0.26%	$22,817,732	0.29%	$34,694,298	$57,512,030
12	Virginia	2.85%	$248,819,979	2.84%	$343,969,840	$592,789,819
14	Washington	2.31%	$202,267,821	2.24%	$271,233,432	$473,501,253
37	West Virginia	0.67%	$58,205,272	0.51%	$62,381,349	$120,586,621
21	Wisconsin	1.52%	$133,240,489	1.57%	$190,286,941	$323,527,431
51	Wyoming	0.11%	$10,024,212	0.13%	$16,281,936	$26,306,148
	Total U.S.	**100.00%**	**$8,738,743,050**	**100.00%**	**$12,125,361,864**	**$20,864,104,914**

[1] See, e.g., testimony of Patricia McCoy before the U.S. Senate Banking Committee, "Consumer Protections in Financial Services: Past Problems, Future Solutions, " available at http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Testimony&Hearing_ID=11be680d-04db-42cc-89bf-7fe4ffe4d9cd&Witness_ID=b6ba604a-d441-43e3-9951-1fbab4b11e57.

[2] Studies show that the subprime foreclosure crisis was driven more by the kinds of loan terms that came to prevail in too large a segment of the market rather than by the characteristics of the borrowers. *See, e.g.* Lei Ding, Roberta G. Quercia, Wei Li, and Janneke Ratcliffe, *Risky Borrowers or Risky Mortgages: Disaggregating Effects Using Propensity Score Models*, Center for Community Capital, Univ. of North Carolina & Center for Responsible Lending (Working Paper, Sept. 13, 2008).

[3] Non-prime includes subprime and "Alt-A", but excludes FHA. Alt-A has vague and inconsistent definitions. It can mean prime-worthy borrowers by FICO scores but with non-standard loan terms, or it can mean FICO scores between prime and subprime.

[4] 2008 Mortgage Market Statistical Annual; Inside B&C Lending.

[5] *The Wall Street Journal, Subprime Debacle Traps Even Very Credit-Worthy, December 2007 at* http://online.wsj.com/article/SB119662974358911035.html?mod=hps_us_whats_news.

[6] Leslie Parrish, *Overdraft Explosion: Bank fees for overdrafts increase 35% in two years*, Center for Responsible Lending, forthcoming October 2009.

[7] See Joshua M. Frank, *What's Draining Your Wallet? The Real Cost of Credit Card Advances,* p. 8, (December 16, 2008).

[8] Federal Trade Commission Act, 15 U.S.C. 45(a)(1).

[9] 15 U.S.C. Sec 57a.

[10] This was the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act of 1975, Pub. L. No. 93-637, 88 Stat. 2183 (1975) (codified as amended in various sections inserted throughout 15 U.S.C.). The provision giving rule-writing authority to the FRB, OTS and NCUA can be found at 15 U.S.C. 15 USC 57a(f).

[11] For an overview of the federal banking agencies' long-standing (but long ignored) authority to enforce the Federal Trade Commission Act's ban on unfair and deceptive acts and practices, from the perspective of a senior official of the OCC, *see* Julie L. Williams & Michael S. Bylsma, "On the Same Page: Federal Banking Agency Enforcement of the FTC Act to Address Unfair and Deceptive Practices by Banks," 58 Bus. Law. 1243 (May, 2003) (hereafter "Williams & Bylsma").

[12] 12 U.S.C. § 1639(l).

[13] H.R. Conf. Rep. No. 1142, 63d Cong., 2d Sess. 19 (1914), *quoted in* American Financial Serv. Ass'n v. FTC, 767 F.2d 957, 966 (D.C. C.A. 1985).

[14] See, e.g., Jess Bravin & Paul Beckett, *Friendly Watchdog: Federal Regulator Often Helps Banks Fighting Consumers*, Wall St. J., Jan. 28, 2002.

[15] See Julie L. Williams & Michael L. Bylsma, *On the Same Page: Federal Banking Agency Enforcement of the FTC Act to Address Unfair and Deceptive Practices by Banks*, 58 Bus. Law. 1243, 1244, 1246 & n.25, 1253 (2003) (conceding that "[a]n obvious question is why it took the federal banking agencies more than twenty-five years to reach consensus on their authority to enforce the FTC Act").

[16] Duncan A. MacDonald (former General Counsel, Citigroup Inc.'s Europe and North American card business), Letter to the Editor, *Comptroller Has Duty to Clean Up Card Pricing Mess*, Am. Banker, Nov. 21, 2003, at 17; *see also* Frontline, *Secret History of the Credit Card*, Transcript at 16-17, http://www.pbs.org/wgbh/pages/frontline/shows/credit/etc/script.html.

[17] Information on OCC's enforcement actions is contained in annual reports that the U.S. Attorney General provide to Congress. See U.S. Attorney General, Annual Report to Congress Pursuant to the Equal Credit Opportunity Act, *available at* http://www.usdoj.gov/crt/housing/housing_special. php.

[18] In 2005, the OCC required that Laredo National Bank set aside $14 million to cover refunds to borrowers who'd been harmed by the bank's home loan practices. In 2003, it required Clear Lake National Bank to provide $100,000 in restitution to borrowers who'd received tax-lien mortgage loans and to review a portfolio of mortgage loans to determine if similar violations existed. See *Improving Federal Consumer Protection in Financial Services: Hearing Before the H. Comm. on Fin. Servs.*, 110th Cong. 18 (2007) (statement of John C. Dugan, Comptroller of the Currency).); cf. *Credit Card Practices: Current Consumer and Regulatory Issues: Hearing Before the Subcomm. on Fin. Insts. and Consumer Credit of the H. Comm. on Fin. Servs.*, 110th Cong. 14-15, 18 (2007).

[19] See http://www.bloomberg.com/apps/news?pid=20601068&sid=aVgZgMsNYrzo&refer=economy.

[20] See, e.g. http://www.nytimes.com/2007/12/18/business/18subprime.html.

[21] Office of the Comptroller of the Currency, National Credit Committee, *Survey of Credit Underwriting Practices 2005*; see also Fitch Ratings, 2007 Global Structured Finance Outlook: Economic and Sector-by-Sector Analysis (December 11, 2006).

[22] Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision, National Credit Union Administration, "Interagency Guidance on Nontraditional Mortgage Product Risks," 71 Fed. Reg. 58609 (Oct. 4, 2006) http://www.federalreserve.gov/boarddocs/srletters/2006/SR0615a2.pdf4, 2006), *available at* http://www.federalreserve.gov/boarddocs/srletters/2006/SR0615a2.pdf.

[23] See *In Re Washington Mutual, Inc. Securities Litigation*, No. 2:08-MD-1919 MJP (W.D. Wash) (Former employees allege in the court documents that, well into 2007, WaMu underwrote pay option ARM loans based on the borrowers' ability to afford the low "teaser" payment—and not the full payment that inevitably would cause borrowers' monthly obligations to skyrocket).

[24] Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision, National Credit Union Administration, "Statement on Subprime Mortgage Lending," 72 Fed. Reg. 37569 (July 10, 2007).

[25] Interagency Guidance on Subprime Lending (Mar. 1, 1999), *available at* http://www.fdic.gov/news/news/financial/1999/FIL9920a.html.

[26] 2001 Interagency Expanded Guidance for Subprime Lending Programs (Feb. 2, 2001), *available at* http://files.ots.treas.gov/25137.pdfhttp://files.ots.treas.gov/25137.pdf.

[27] See *Consumer Protections in Financial Services: Past Problems, Future Solutions: Hearing Before the S. Comm. on Banking, Housing and Urban Affairs*, 111th Cong. (2009) (statement of Patricia A. McCoy, Professor of Law, Univ. of Conn.), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=40666635-bc76-4d59-9c25-76daf0784239.

[28] Id.

[29] Id.

[30] Cal. Reinvestment Coal., *Who Really Gets Higher-Cost Home Loans?* 3, 18 (2005).

[31] Affidavits by Elizabeth M. Jacobson and Tony Paschal in *Mayor and City Council of Baltimore v. Wells Fargo Bank*, No. 1:08-cv -00062-BEL (D. Md.), Documents 74-16 and 74-17.

[32] See Board of Governors of the Federal Reserve System, Annual Report, *available at* http://www.federalreserve.gov/ boarddocs/rptcongress/ (containing information on the OCC's enforcement actions); Arthur E. Wilmarth, Jr., *The OCC's Preemption Rules Exceed the Agency's Authority and Present a Serious Threat to the Dual Banking System and Consumer Protection*, 23 Ann. Rev. Banking & Fin. L. 225, 237-52 (2004) (finding that the OCC's consumer protection enforcement actions targeted small national banks); *Improving Federal Consumer Protection in Financial Services: Hearing Before the H. Comm. on Fin. Servs.*, 110th Cong. 18 (2007) (statement of John C. Dugan, Comptroller of the Currency) (describing number of consumer complaints received by the OCC); OCC, Consumer Protection News: Unfair and Deceptive Practices, http://www.occ.gov/Consumer/Unfair.htm (describing the number of enforcement actions taken by the OCC).

[33] We have reported that consumers paid $17.5 billion in overdraft fees in 2006 in exchange for only $15.8 billion in credit. We are currently updating our estimates based on 2008 data, which will show overdraft fees paid annually have increased to well over $20 billion in just two years.

[34] Statistics indicate that from 1997 to 2007, the average overdraft fee charged increased from $16.50 to $29. The FRB's research indicates that the average was $16.50 in 1997 (*see* Federal Reserve Bulletin, *Retail Fees of Depository Institutions, 1997-2001*, 405, 409, *available at* http://www.federalreserve.gov/pubs/bulletin/2002/0902lead.pdf) and $21.82 in 2002 (*see* Board of Governors of the Federal Reserve System, *Annual Report to the Congress on Retail Fees and Services of Depository Institutions* at 5 (June 2003), *available at* http://www.federalreserve.gov/boarddocs/rptcongress/2003fees.pdf). Bankrate's survey on overdrafts found that the average charged was $29 in 2007. Bankrate, *2007 Courtesy Overdraft Study*, *available at* http://www.bankrate.com/brm/news/chk/20071219_overdraft_survey_main_a1.asp.

[35] Eric Halperin, Lisa James, and Peter Smith, *Debit Card Danger. Banks offer little warning and few choices as customers pay a high price for debit card overdrafts*, Center for Responsible Lending, at 25 (Jan. 25, 2007), *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/Debit-Card-Danger-report.pdf.

[36] OCC Interpretive Letter # 914 (August 3, 2001), *available at* http://www.occ.treas.gov/interp/sep01/int914.pdf. The OCC raised compliance issues with respect to TILA, TISA, EFTA, ECOA, and Regulation O (extensions of credit to bank insiders).

[37] 67 Fed. Reg. 72620 (2002).

[38] Joint Guidance on Overdraft Protection Programs, 70 Fed. Reg. 9127 (Feb. 24, 2005).

[39] *Id* at 9128.

[40] *Id.*

[41] http://www.helpwithmybank.gov/faqs/banking_overdraft.html#drop08. Additionally, Consumer Federations of America's 2009 survey of overdraft fees at the 16 largest banks finds that their average fee is $35, compared to $27 at FDIC-regulated institutions. CFA Survey: Sixteen Largest Banks Overdraft Fees and Terms (updated July 31, 2009), available at http://www.consumerfed.org/pdfs/overdraft_fee_report_09.pdf; Eleven of the 16 largest banks are OCC-supervised.

[42] Mark Fusaro, *Are "Bounced Check Loans" Really Loans?*, note 4, at 6 (noting 20% of institutions in June 2004 were applying "bounce protection" to debit cards or ATM) (Feb. 2007), *available at* http://personal.ecu.edu/fusarom/fusarobpintentional.pdf.

[43] FDIC Study of Bank Overdraft Programs at iv (Nov. 2008).

[44] 70 Fed. Reg. 29582 (May 2005).

[45] 74 Fed. Reg. 5212 (Jan. 29, 2009).

[46] Comptroller John Dugan released a statement on September 25, urging national preemptive standards.

[47] Dean Baker, Dangerous Trends: The Growth of Debt in the U.S. Economy, at 4, Fig 1 (2004); Stephen Roach, Comment: America's Inflated Asset Prices Must Fall, Financial Times, January 8, 2008.

[48] Sam Roberts, *Census Data Shows Recession Brings Changes*, New York Times, p. A14 (Sept. 21, 2009). For data regarding the net drain on homeownership by subprime lending, see *Subprime Lending: A Net Drain on Homeownership* (Center for Responsible Lending), March 27, 2007 http://www.responsiblelending.org/mortgage-lending/policy-legislation/congress/Net-Drain-in-Home-Ownership.pdf.

[49] Michael McKinstry, *Big Trouble*, CardTrak (July 25, 2008), http://cardtrack.com/news/2008/07/25/big_trouble.

[50] Calculated from Nilson Report, *Top Credit Card Issuers*, 1, 9 (Issue 896 February, 2008); Nilson Report, *General Purpose Cards – U.S. 2007*, 1, 9 (Issue 902, May 2008). *See also* Adam J. Levitin, *All But Accurate: A Critique of the American Bankers Association Study of Credit Card Regulation*, p. 20 (2007), (hereafter Levitin (2007) *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1029191.

[51] Testimony of Edmund Mierzwinski, *Hearing on Credit Card Interchange Fees* Before the Antitrust Task Force of the House Judiciary Committee, p. 6 (July 19, 2007).

[52] 2008 Mortgage Market Statistical Annual; Inside B&C Lending).

[53] *Option ARMs: It's Later Than It Seems*, Fitch Ratings (September 2, 2008), at 5.

[54] Inside Mortgage Finance (Countrywide, IndyMac, WaMu and Wells.)

[55] Testimony of Prof. Patricia A. McCoy, Hearing on "Consumer Protections in Financial Services; Past Problems, Future Solutions" before the U.S. Senate Committee on Banking, Housing and Urban Affairs, p. 21, *see also* pg. 18-22 (March 3, 2009)

[56] 1 INSIDE MORTGAGE FINANCE, THE 2006 MORTGAGE MARKET STATISTICAL ANNUAL 187 (2006); OCC, NATIONAL BANK OPERATING SUBSIDIARIES DOING BUSINESS WITH CONSUMERS AS OF 12/31/2005 TO BE UPDATED ANNUALLY (2005), http://www.occ.treas.gov/consumer/Report%20-%202006%20for%20Op%20Sub%20pdf.pdf. Because National City Bank sold First Franklin Financial to Merrill Lynch in December 2006, First Franklin Financial is no longer a national bank operating subsidiary. *In Brief: Nat City Sells First Franklin*, AM. BANKER, Jan. 3, 2007, at 20. National City Bank was forced into a "shotgun marriage" with PNC in October, 2008.

[57] Letter from Comptroller of the Currency to Elizabeth Warren , Chair Congressional Oversight Panel, (February 12, 2009).

[58] Michael McKinstry, *Big Trouble*, CardTrak (July 25, 2008), http://cardtrack.com/news/2008/07/25/big_trouble.

[59] 3 N.Y.C.R.R. 6.8.

[60] Wells Fargo's Direct Deposit Advance (*see* https://www.wellsfargo.com/checking/dda/); U.S. Bank's Checking Account Advance (*see* http://www.usbank.com/cgi_w/cfm/personal/products_and_services/checking/caa.cfm); Fifth Third Bank's "Early Access" product (*see* https://www.53.com/wps/portal/pv?New_WCM_Context=/wps/wcm/connect/FifthThirdSite/Personal/Checking+Accounts/Fifth+Third+Early+Access/).

[61] **Massachusetts** (Mass. Gen. Laws ch. 940, § 8.06(17)(Where the financial interest of a mortgage broker conflicts with the interests of the borrower—*e.g.* the broker's compensation will increase directly or indirectly if the borrower obtains a loan with higher interest rates—the broker shall disclose the conflict and shall not proceed with the loan so long as such a conflict exists.); **North Carolina** (N.C. Gen. Stat. § 53-243.11)(No lender shall provide nor shall any broker receive any compensation that changes based on the terms of the loan, other than principal.)

[62] Section 158 of HOEPA mandated periodic hearings on the state of the market and the adequacy of the law. Information from these hearings led the FRB to use its authority under 15 USC 1602(aa) to add abusive single premium credit insurance charges to the HOEPA "trigger fees."

[63] *See, e.g.* Jean Ann Fox and Anna Petrini, *Internet Payday Lending; How High-Priced Lenders Use The Internet to Mire Borrowers in Debt and Evade State Consumer Protections* (Consumer Federation of America, Mov. 30, 2004). Other schemes have involved payday lending disguised as catalogue sales.

[64] Section 124(a)(2) preserves the authority of the FTC or any other agency, (presumably excluding the "Agency" – the CFPA) to act.

[65] Most branded cards are actually issued by banks, to take advantage of federal preemption laws and regulations. Target, for example, has a national bank.

[66] One of the most notorious cases of equity-skimming predatory mortgage lending began with a retail seller-financed "freezer-meat sale" assigned by the seller to Associates. The case was profiled on both the front page of the Wall Street Journal and a network prime-time news program.

[67] Pope, Justin. "For-Profit Colleges' Increased Lending Prompts Concerns." The Associated Press. August 15, 2009. Available online at http://www.usatoday.com/news/education/2009-08-15-profit-college-lending_N.htm. Also see "Corinthian Colleges, Inc. F4Q09 (Qtr End 06/30/09) Earnings Call Transcript" at http://seekingalpha.com/article/158257-corinthian-colleges-inc-f4q09-qtr-end-06-30-09-earnings-call-transcript?source=bnet.

[68] From Corinthian College's website. Available online at http://www.cci.edu/brands/everest.

[69] Pope, Justin. Ibid

[70] Center for Responsible Lending calculations based on data from CNW Marketing, NCM Associates, and CRL survey data.

[71] *See* Federal Reserve Board Statistical Release G.19 (July, 2009): the average amount financed for 2007 was over $28,000.

[72] Roland Arnall headed the Long Beach Mortgage Company when the Department of Justice brought its first reverse redlining case for discriminatory pricing, ending with a $5 million settlement in 1996. **Cite.** Arnall went on to head Ameriquest. Its practices put it in the sights of a state multi-state investigation resulting in a injunction and a multimillion dollar settlement in 2005.]

[73] The run-up to the recent crisis has provided considerable evidence as to what practices increase risk. The CFPA's mission to engage in reality-based research and evidence-based oversight are key components to preventing yet another market collapse.

[74] See McCoy testimony, *supra.*

[75] See, e.g., *The People of the State of California v. Countrywide Financial Corp.*, Los Angeles Superior Court, June 24, 2008 Available, *available at* http://ag.ca.gov/cms_attachments/press/pdfs/n1588_firstamendedcomplaint.pdf#xml=http://search.doj.ca.gov:8004/AGSearch/isysquery/d9682d50-f6f7-4c18-9b74-dd03bca6cf28/2/hilite/ .
Seehttp //ag.ca.gov/cms_attachments/press/pdfs/n1588_firstamendedcomplaint.pdf#xml=http://search.doj.ca.gov:8004/AGSearch/isysquery/d9682d50-f6f7-4c18-9b74-dd03bca6cf28/2/hilite/; see also *Unfair and Unsafe: How Countrywide's irresponsible practices have harmed borrowers and shareholders*, CRL Issue Paper (Feb. 7, 2008). Available at http://www.responsiblelending.org/mortgage-lending/research-analysis/unfair-and-unsafe-countrywide-white-paper.pdf .), *available at* http://www.responsiblelending.org/mortgage-lending/research-analysis/unfair-and-unsafe-countrywide-white-paper.pdf .

[76] Countrywide Financial Corporation, Q3 2007 Earnings Call, Oct. 26, 2007. See; see also Gretchen Morgenson, *Inside the Countrywide Spending Spree,* N.YY. Times (August. 26, 2008)); Gretchen Morgenson & Geraldine Fabrikant, *Countrywide's Chief Salesman and Defender,* N.Y. Times (Nov. 11, 2007).

[77] Office of Inspector General, Department of the Treasury, *Material Loss Review of ANB Financial, National Association* (Nov. 25, 2008) OIG-09-013.

[78] Office of Inspector General, Department of the Treasury, *Material Loss Review of First National Bank of Nevada and First Heritage Bank, National Association* (February 27, 2009) OIG-09-033.

[79] In 2004, as warning signs of dangerous practices in the mortgage market grew, then-OTS director James Gilleran made it clear his agency was determined to keep a pliable attitude toward policing the home lenders: "Our goal is to allow thrifts to operate with a wide breadth of freedom from regulatory intrusion." Between 2001 and 2004, the OTS slashed its staff by 25% and changed its examination structure to emphasize having lenders do "self-evaluations" of their compliance with consumer protection laws. By 2005, the OTS had a new director, John Reich, but the message was similar. When concerns were raised about lenders' lack of concern for borrowers' ability to repay their loans, Reich cautioned that regulators should not interfere with thrifts that "have demonstrated that they have the knowhow to manage these products through all kinds of economic cycles." See Binyamin Appelbaum & Ellen Nakashima, *Banking Regulator Played Advocate Over Enforcer*, Wash. Post (Nov. 23, 2008).

[80] For more details on OTS's regulatory failures, see Michael Hudson and Jim Overton, *The Second S&L Scandal: How OTS allowed reckless and unfair lending to fleece homeowners and cripple the nation's savings and loan industry*, Center for Responsible Lending (Jan 2009) Available at http://www.responsiblelending.org/mortgage-lending policy-legislation regulators the-second-s-l-scandal pdf .), *available at* http://www responsiblelending org/mortgage-lending/policy-legislation regulators/the-second-s-l-scandal.pdf.

[81] Office of Inspector General, Department of the Treasury, *Material Loss Review of Superior Bank, FSB* (Feb. 6, 2002); OIG-02-040; and Office of Inspector General, Federal Deposit Insurance Corporation, *Issues Related to the Failure of Superior Bank, FSB, Hinsdale, Illinois* (Feb. 6, 2002) Audit Report No. 02-005.

[82] Office of Inspector General, Department of the Treasury, *Material Loss Review of NetBank, FSB* (Apr. 23, 2008) OIG-08-032.

[83] Office of Inspector General, Department of the Treasury, *Material Loss Review of IndyMac Bank, FSB* (Feb. 26, 2009) OIG-09-032.

[84] Office of Inspector General, Department of the Treasury, *Material Loss Review of Downey Savings and Loan FA* (June 15, 2009) OIG-09-039.

[85] The inspector general discovered, for example, that OTS's western regional director had allowed IndyMac to count money it received from its bank holding company in May 2008 in a quarterly report outlining its financial condition as of March 31, 2008 See Binyamin Appelbaum and Ellen Nakashima, *Regulator Let IndyMac Falsify Report*, Washington Post (December 23, 2008) and Cheyenne Hopkins, *Treasury IG Faults OTS For Allowing Backdating*, American Banker (May 22, 2009)

[86] Appelbaum & Nakashima, *supra* note 77.

[87] Appendix A includes a summary of the findings and an explanation of the methodology.

[88] Online interview with Brent Carmichael (Moderator, NCM Associates, Inc), *Time is Now for Buy-Here, Pay-Here*, AIN Media (Automotivedigest.com), Aug. 2008 (Emphasis added).

[89] Rosland Briggs Gammon, *Buy-here, pay-here plans may attract more dealers; Growing customer base, higher standards may outweigh risks*, Automotive News, Vol. 82, No 6294, Feb 11, 2008.

[90] 73 Fed. Reg. 44522, 44563-65 (July 30, 2008).

[91] See Testimony of Kathleen Keest, *Hearing on H.R. 2309: The Consumer Credit and Debt Protection Act*, before the Subcommittee on Commerce, Trade and Consumer Protection Committee on Energy and Commerce (May 12, 2009).

[92] Mark A. Cohen, Imperfect Competition in Auto Lending: Subjective Markup, Racial Disparity, and Class Action Litigation, Vanderbilt University (Dec 2006) [hereinafter Imperfect Competition].

[93] ThoughAs explained in note 26, though the seller-dealer is listed as the creditor on the contract, in fact it typically sends the credit application to one or more potential third- party lenders for approval or disapproval. The outside lender tells the dealer the terms upon which it would approve the deal, including the "par rate" or "buy rate" – that is the rate that the buyer qualifies for based on its credit qualifications and the collateral. The dealer mark-up, or yield spread premium is an upward bump to that "buy rate" from which the dealer receives extra compensation.

[94] *See* Appendix A. This too, is parallel to the mortgage market, where many borrowers believe that lenders are required to give them the best rate they qualify for.

[95] Imperfect Competition. Figures are weighted averages using data from five major auto finance companies compiling 12.6 million records between 1993 and 2004.

[96] For example, the settlement agreement sets limits in this range for GMAC in *Coleman v. GMAC*, Para. 8.3, No. 3-98-0211 (M.D. Tenn, settlement agreement filed Feb. 10, 2004), *available at* http://www.consumerlaw.org/issues/cocounseling/content/GMACSettlementAgrmt.pdf.

[97] Figures derived from kickback data in the 2008 Consumer Bankers Association Automotive Finance Study (2007 full-year data), and 2007 sales data for dealer-financed vehicles from CNW Market Research (excluding leases). State market shares also from 2007 CNW Market Research data.

American Financial Services Association

HOUSE COMMITTEE ON FINANCIAL SERVICES

Hearing on:

Perspectives on the Consumer Financial Protection Agency

Wednesday, September 30, 2009

WRITTEN TESTIMONY OF BILL HIMPLER

EXECUTIVE VICE PRESIDENT

THE AMERICAN FINANCIAL SERVICES ASSOCIATION

HOUSE COMMITTEE ON FINANCIAL SERVICES

Hearing on:

Perspectives on the Consumer Financial Protection Agency

Wednesday, September 30, 2009

WRITTEN TESTIMONY OF BILL HIMPLER

Mr. Chairman, Ranking Member Bachus, and Members of the Committee, my name is Bill Himpler and I am the Executive Vice President of the American Financial Services Association (AFSA). AFSA's 350 member companies include consumer and commercial finance companies, "captive" auto finance companies, credit card issuers, mortgage lenders, industrial banks and other financial service firms that lend to consumers and small businesses. I appreciate the opportunity to give our member companies' perspective on the proposal to create a Consumer Financial Protection Agency (CFPA).

Chairman Frank, in light of the revisions for the CFPA that you put forth last week, I'd like to thank you for your willingness to listen and consider different perspectives on this very important proposal. At the same time, we noted that many of the revisions focus on nonbanks.

In addition, some committee members may have seen *The Washington Post's* front-page article on September 27th that defined consumer finance companies more narrowly than we do. Before I present our views on the CFPA, I'd like to take a minute to set the record straight regarding consumer finance companies and how they're currently regulated.

Finance companies come in many shapes and sizes – some are independently owned lenders that specialize in providing personal loans to consumers and small business owners; others are "captives" that provide financing for vehicles or other products manufactured by their parent companies. While I cannot speak for other institutions that may fall under the proposal's definition of nonbanks, I can assure this committee that finance companies are already heavily regulated.

In addition to being subjected to federal consumer protection laws, such as the Truth in Lending Act (TILA), Fair Credit Reporting Act (FCRA) and the Equal Credit Opportunity Act (ECOA), finance companies are licensed and regulated by the states and abide by consumer protection statutes in all of the states in which they do business.

Like banks, finance companies undergo regular and vigorous examination by state regulators. These companies have been successful at meeting the credit needs of communities in part because they are subject to oversight by state regulators who have a familiarity with local and regional situations and issues faced by lenders. This knowledge, along with their proximity, means state regulators frequently are among the first to identify emerging issues, practices or products that may need further investigation. Though the state system has not been perfect, no one can argue that states have not aggressively fought abusive lending. In 2008 alone, state regulators took more than 7,000 mortgage enforcement actions.

After a careful review of the proposed revisions, AFSA remains opposed to the CFPA proposal. While some critics have equated our stance as being opposed to <u>any</u> changes to consumer protection regulations, this is not the case. To the contrary, AFSA strongly supports efforts by the Obama Administration and others to improve consumer protections for financial services customers – but we do have philosophical differences as to how to go about achieving this goal. We also have concerns that the revised language for the proposal could reduce – and perhaps eliminate – a critical source of consumer credit. I'll discuss this in more detail later.

To begin, let me outline four fundamental reasons for our position on the CFPA.

First, because it's based on the premise that the entire financial services industry is broken, the CFPA would try to "fix" what's still working.

Second, the CFPA is still likely to mean higher prices and reduced product choice for financial services customers even if the "plain vanilla" requirement was eliminated.

Third, we believe that more government intervention in the form of a vast, new regulator won't necessarily result in better consumer protection.

And fourth, the creation of another separate regulator would bifurcate the consumer protection and safety and soundness functions of financial regulation.

<u>If Isn't Broke, Don't Fix It</u>

The CFPA is based upon the notion that the entire financial services system is broken based upon what occurred in the housing market. In addition, the bill's intent is to use a "one-size-fits-all approach" and treat all financial services products the same. For instance, it makes no sense to compare terms, such as APR, for a 30-year fixed mortgage with those of a short-term installment loan used to buy a new washer and dryer.

It's important to recognize that mortgages are just one of many products within the expansive consumer lending marketplace. Many of the companies that would be subject to intensified requirements, greater restrictions and higher compliance costs under the CFPA would be those that didn't contribute to the mortgage crisis – i.e., those offering auto financing, personal loans and other types of products that enable consumers and small businesses to meet their everyday needs.

To put it another way, the lenders that weren't part of the problem will be left holding the bag. The financial crisis took a toll on many of these institutions, such as the auto finance companies that are now struggling to obtain access to capital. Some of them may decide the compliance costs and risks associated with the CFPA are untenable, causing them to exit the market and leaving borrowers with fewer credit options.

More Government Doesn't Mean Better Consumer Protection

Supporters of the CFPA have attempted to portray it as a government watchdog that would be better able to weed out bad practices in the financial services sector than the existing federal agencies. Yet there's no guarantee this will happen – and policymakers should not be "tricked and trapped" into thinking that more bureaucracy is what's needed to improve consumer protection.

Even if it were scaled back in accordance to last week's revisions, the proposed agency still would require an immense amount of resources - as well as a restructuring of existing regulatory personnel - before it could become operational. Such an approach seems ill-advised when we already have several federal regulators with the expertise and experience to do the job.

What's more, putting an untested, inexperienced agency in charge of consumer protection for the entire financial marketplace could exacerbate existing problems, rather than reduce them. A public opinion survey conducted this summer found that 79% of Americans believe that "before creating a new agency, we should make sure we understand how it will impact the economy. Rushing to create it may cause more harm in the long run."

Consumers and Small Businesses Will Have Fewer, More Expensive Borrowing Options

If the CFPA were to become a reality, financial services customers are likely to have less borrowing flexibility even with the elimination of the "plain vanilla" requirement. The new regulator would still retain expansive rulemaking authority and the ability to determine allowable products and services, which will greatly influence the options that will be available to consumers. Financial institutions falling underneath the CFPA's jurisdiction will face considerable compliance costs that will get passed on to borrowers. In essence, this would impose a new tax on consumers at a time when they are least able to afford it.

Splitting the Prudential and Consumer Protection Functions Won't Yield Better Results

AFSA supports, and believes consumers will be better served by, a regulatory structure where prudential and consumer protection oversight is housed within a single regulator. Congress tried to separate these two intertwined functions with the Government Sponsored Enterprises (GSEs). Federal Housing Finance Agency Director James Lockhart recently cited this separation of functions as one of the primary reasons for the failure of Fannie Mae and Freddie Mac. Today, no evidence shows that a separation of prudential and consumer protection regulation will offer better results in the financial services arena – in fact, indications are to the contrary. We urge Congress to support a regulatory structure that does not separate financial products and services from the viability of the companies that offer them.

Indeed, given that the agency would be required only to "consult" with prudential regulators, it is all too likely that the agency would embark on a mission to severely restrict sound business and financial practices it perceives as not "consumer friendly."

CFPA – ECONOMIC RAMIFCATIONS

For the reasons I've just explained, AFSA believes the creation of a CFPA will not fulfill the goal of improving consumer protection for financial services customers. It most certainly is not in the consumer's best interest to add layers of bureaucracy, reduce credit choices and raise prices for financial services.

In addition, I'd also like to point out that, if the proposal were to focus on nonbanks, it could reduce – and perhaps eliminate – many finance companies, which are a critical source of credit for consumers and small businesses.

While banks play a vital role in the economy and the consumer credit market, Federal Reserve Board statistics show that the majority of non-mortgage consumer credit is provided by finance companies and others who raise funds through securitization. Finance companies have a long history of meeting the credit needs of consumers – from buying a car to get to work, to paying college costs for a son or daughter.

Today's installment lenders are a key element in supporting the country's economic health. People turn to installment lenders for a multitude of reasons. Key among these, however, is the need to access small sums to deal with unforeseen circumstances.

Take for example, an unanticipated car repair. Keeping one's vehicle in good repair is essential to allow transportation to work. Absent access to small sums over and above a wage, the repairs necessary for such transportation may not be possible, resulting in job loss. Many less-advantaged citizens in our country do not have access to the kinds of credit cards and financial offerings available to the more fortunate, and have long relied on access to small-sum installment loans to meet their credit needs. And they have proven that they can and do make good use of borrowed money, even if they sometimes struggle to demonstrate their creditworthiness to lenders.

In addition to installment lenders, auto finance companies are vitally important, especially in an economy where preserving or finding employment is foremost on the minds of many Americans. Vehicles play a critical role in sustaining employment because the majority of Americans still use them to get to work. A 2007 U.S. Census Bureau American Community Survey found that close to nine out of 10 workers drove to work in 2005, with 75% of the commuters driving alone.

It's worth noting that, while the proposed revisions to the CFPA legislation would exempt car dealers, this will be of little consequence to them. These dealers, after all, will need finance companies to provide their customers with a means to acquire cars.

Consumers are not the only ones who will feel the effects – millions of small businesses will as well. According to a September 2009 report from the U.S. Chamber of Commerce's Center for Capital Markets Competitiveness, most of the 26.7 million businesses in the United States, including the self employed, rely on credit cards, home equity loans and other sources of consumer lending to finance their business. Among the report's conclusions is that "the CFPA credit squeeze would like result in business closures, fewer startups and slower growth."

If installment, auto and other finance companies were required to shoulder much of the compliance burden resulting from a CFPA, it undoubtedly would affect their ability to provide safe, convenient and affordable loans – just as the economy is starting to show signs of recovery.

A More Effective Approach

AFSA does not oppose consumer protections – it embraces them. We support rational consumer protection that is regulated and enforced in a manner that allows financial services providers to plan and price for risk, to operate their businesses efficiently and safely, and promote access to a full range of credit products for Americans.

To that end, we offer the following suggestions:

1. Improve Consumer Disclosures

   We agree with Elizabeth Warren and others who have cited the need for clear, easy-to-understand disclosures for consumer credit products – but it makes no sense to create another agency when we already have an alphabet soup of regulators that can do the job.

2. Consider alternatives to the CFPA

   The CFPA is not the only option we have for changing consumer protection. Representative Minnick, for example, is working on an alternative proposal that would have existing federal and state regulators work together on a "consumer financial protection council." Given the importance of this issue, we urge this committee to avoid rushing into solutions that, in the end, could create more harm than good.

3. Pursue a regulatory structure that does not separate financial products and services from the viability of the companies that offer them.

   All prudential agencies should work together to coordinate on consumer protection regulation for financial products and services with the goal that the regulations be consistent and uniform.

4. Step up enforcement of existing consumer protection laws.

   This is not to say we advocate the status quo. While the current financial regulators already have many enforcement tools at their disposal, changes are needed to enable these regulators to fully utilize these tools. This includes allocating sufficient resources and other support.

5. Continue efforts to improve financial education.

   The President's Advisory Council on Financial Literacy and the U.S. Treasury's Office of Financial Education play important roles in working with the financial services industry and others in the private sector on financial literacy initiatives. Ultimately, an educated consumer is the best defense against fraud and unscrupulous practices.

As I said at the outset, we fully support the goal of the administration and this committee to improve the quality and effectiveness of consumer protection for all Americans. I appreciate the opportunity to testify here today and am happy to answer any questions Members may have.

The Heritage Foundation
LEADERSHIP FOR AMERICA
214 Massachusetts Avenue, NE • Washington DC 20002 • (202) 546-4400 • heritage.org

CONGRESSIONAL TESTIMONY

How to Protect Consumers in the Financial Marketplace: An Alternate Approach

Testimony before
Committee on Financial Services
United States House of Representatives

September 30, 2009

David C. John
Senior Research Fellow
The Heritage Foundation

My name is David C. John. I am a Senior Research Fellow in Retirement Security and Financial Institutions at The Heritage Foundation. The views I express in this testimony are my own, and should not be construed as representing any official position of The Heritage Foundation.

The Treasury Department has proposed consolidating the existing consumer protection divisions of the various federal financial regulatory agencies into a new and powerful Consumer Financial Protection Agency (CFPA). The CFPA would be responsible for creating and enforcing the regulation of consumer financial products.[1] On July 9, House Financial Services Committee Chairman Barney Frank introduced a slightly revised version of the Treasury proposal as H.R. 3126[2] and announced his intention to pass the bill as rapidly as possible. Just last week, Chairman Frank issued a revised version of this proposal.

Even with the most recent changes, creating a new agency would be a huge mistake that would hurt consumers far more than it helps them. A CFPA would raise costs for consumers, reduce the number and kind of products available to them, increase the micro-management of financial-services firms, and greatly increase the confusion caused by differing and conflicting consumer laws in the different states.

A far better approach would be to coordinate the consumer activities of existing state and federal financial regulators by creating a coordinating council designed to promote equal standards of consumer protection using agencies' existing powers. Critics of the current regulatory system justify the need for a CFPA by citing instances where different agencies applied different regulatory standards to similar products, and pointing to unregulated entities or products that took advantage of consumers. But these problems could just as easily be solved by a coordinating council as by creating a massive new

---

[1]A Treasury Department fact sheet, "Strengthening Consumer Protection," on the proposed new agency is available at *http://www.financialstability.gov/docs/regulatoryreform/strengthening_consumer_protection.pdf* (September 1, 2009).
[2]H.R. 3126, at *http://www.house.gov/apps/list/press/financialsvcs_dem/21frank_011_xml.pdf* (September 1, 2009).

regulator. The council would be managed and staffed by the agencies with an oversight panel of outside experts to monitor its activities and ensure that coverage is universal.

Consumer protections need to be both more effective and to apply to all consumers, regardless of the presence of unregulated products or segments of the industry, but there is no need for a massive new agency. Given the right instructions and oversight, the existing state and federal regulators could effectively deal with abuses and gaps between different types of financial institutions. As discussed below, the proposed CFPA could actually make matters worse for consumers by causing chaos while it re-arranges the existing regulators into a cumbersome, unresponsive bureaucracy.

A Better Approach to Consumer Protection

A better way to improve consumer financial regulation would be to create a council of regulators similar to the one charged with creating uniform standards for the examination of financial institutions, the Federal Financial Institutions Examination Council (FFIEC).[3] The council of consumer financial regulators would be charged with ensuring that existing state and federal regulators have uniform regulatory standards that apply to all types of financial institutions and can meet the challenges posed by complex new financial products. But it leaves the day-to-day enforcement to regulators that understand that type of financial institution and its operational necessities. Such a council has the advantage of neither creating a vast new all-powerful bureaucracy nor completely disrupting current regulatory efforts by merging parts of different agencies.

The council would consist of one representative from each federal agency[4] and elected representatives from councils of the various types of state regulators[5]. In addition,

---

[3]The FFIEC "is a formal interagency body empowered to prescribe uniform principles, standards, and report forms for the federal examination of financial institutions by the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS), and to make recommendations to promote uniformity in the supervision of financial institutions. In 2006, the State Liaison Committee (SLC) was added to the Council as a voting member. The SLC includes representatives from the Conference of State Bank Supervisors (CSBS), the American Council of State Savings Supervisors (ACSSS), and the National Association of State Credit Union Supervisors (NASCUS)." See *http://www.ffiec.gov/* (September 1, 2009).
[4]If existing federal financial regulatory agencies are merged, or new ones are created, the membership of the council would change, but not its purpose or ongoing efforts.
[5] Thus, there would be one individual representing state credit union administrators, another representing state banking regulators and so forth.

it would have a fully participating chairman[6] appointed by the president and a board of outside expert advisors, who would monitor consumer regulatory activities. Staffing would come from within the agencies except for a very small support staff for the chairman and advisors.

The inclusion of state regulators in the council would make coverage even more universal than it would be under the proposed CFPA. Standards agreed to by the council would apply to insurance companies (exempted under the CFPA approach) and as states move to license them, the unregulated mortgage brokers and others who were often responsible for abuses in mortgage lending. Instead of a one-size-fits-all policy dictated by Washington, states would continue to have flexibility in implementing regulations, subject to the oversight of the council and its expert advisors, who could issue public statements and studies to make sure that consumers are aware of states with poor coverage or enforcement. Failure to act could make loans issued in those states ineligible for securitization or sale to investors in other states. This approach would preserve state regulation of those entities that are currently state-regulated rather than attempting to federalize all aspects of consumer financial relationships.[7] The council would also include both the Securities and Exchange Commission and Commodity Futures Trading Commission, thus closing other gaps in the CFPA as proposed, including the regulation of retirement savings accounts.

The council would be responsible for developing broad standards for consumer regulation while leaving the writing and enforcement of specific regulations to those agencies with responsibilities for that area. This ensures that the regulations take into consideration the operational realities of the regulated institutions as well as any special characteristics of regional markets.[8]

[6]Council guidelines would be developed by consensus. The outside advisors would submit reports and provide advice to the council, but would not participate in its deliberations.
[7]Currently the Uniform Commercial Code, recommended language created by the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute (ALI) and passed by the individual states, sometimes with changes to reflect the circumstances of specific states, ensures that businesses with interstate operations face roughly the same legal climate in all states. Should it be necessary, a similar mechanism could recommend model financial regulatory standards to state legislatures.
[8]Since decisions of the council would not have the force of law, implementation of decisions may require the individual agencies to alter their regulations, or even to seek a change to statutes from the relevant state or federal legislative body. Agencies that failed to implement council guidelines would be identified

Another key advantage of the council is that by using existing regulators and their current authority, the regulators' individual efforts can be better monitored than the results of the proposed vast new bureaucracy's vague and almost unlimited powers. Through proper congressional oversight and the reports from the new council's expert advisors, Congress can better pinpoint successes and failures than it could by attempting to keep track of the efforts of one massive agency.

New Federal Agency Is Not the Best Way to Help Consumers

While some Members of Congress and the Obama Administration seem to believe that only the creation of a new agency will prove their commitment to ensuring that customers receive both the information and financial product choice that they need, this is not the case. Financial products can be confusing, and consumers can be manipulated into making poor choices. However, improved disclosures and requiring financial institutions to offer basic products to all of their customers with the appropriate credit history, does not mean a whole new federal agency needs to be created. The draft credit card regulations issued by the Federal Reserve last year,[9] for instance, were an effective response to problems in that industry. Although Congress chose to go beyond the Fed's regulations, the quality of the draft regulations demonstrate the ability of the current financial regulators to effectively handle consumer issues[10].

The CFPA proposal is filled with poorly considered departures from existing law and practice that are as likely to damage consumers' interests as improve them. Giving any agency such wide powers makes little sense, and encouraging the individual states to create their own higher standards will damage the national market in financial services. Congress should avoid the bad policies contained in the proposed CFPA. The same goals supported by those who propose the creation of a new agency can be better achieved through a coordinating council of existing regulatory agencies instead. There is no need

---

through its reports, and in some cases those reports could recommend that the relevant legislative body impose those decisions through changes in the law.

[9]For a summary of the credit card rules approved by the Federal Reserve Board of Governors on December 18, 2008, see "Highlights of Rules Regarding Credit Card Accounts," at *http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20081218a1.pdf* (September 1, 2009).

[10]David C. John, "Senate Credit Card Bill Would Restrict Credit for Those Who Need It Most," Heritage Foundation *WebMemo* No. 2435, May 12, 2009 at *http://www.heritage.org/Research/Regulation/wm2435.cfm*

for a massive new agency when existing agencies could work better, faster, and at little additional cost.

****

The Heritage Foundation is a public policy, research, and educational organization operating under Section 501(C)(3). It is privately supported and receives no funds from any government at any level, nor does it perform any government or other contract work.

The Heritage Foundation is the most broadly supported think tank in the United States. During 2008, it had nearly 400,000 individual, foundation, and corporate supporters representing every state in the U.S. Its 2008 income came from the following sources:

Individuals	67%
Foundations	27%
Corporations	5%

The top five corporate givers provided The Heritage Foundation with 1.8% of its 2008 income. The Heritage Foundation's books are audited annually by the national accounting firm of McGladrey & Pullen. A list of major donors is available from The Heritage Foundation upon request.

Members of The Heritage Foundation staff testify as individuals discussing their own independent research. The views expressed are their own and do not reflect an institutional position for The Heritage Foundation or its board of trustees.

INDEPENDENT COMMUNITY
BANKERS *of* AMERICA

Testimony of

R. Michael S. Menzies, Sr.
President and CEO, Easton Bank and Trust Company
Easton, Maryland

On behalf of the
Independent Community Bankers of America

Before the

Congress of the United States
House of Representatives
Committee on Financial Services

Hearing on

"Perspectives on the Consumer Financial Protection Agency"

September 30, 2009
Washington, D.C.

Chairman Frank, Ranking Member Bachus, Members of the Committee, my name is Michael Menzies. I am the President and CEO of Easton Bank and Trust Company in Easton, Maryland and the Chairman of the Independent Community Bankers of America[1]. Easton Bank is a state-chartered community bank with $150 million in assets. I am pleased to represent community bankers and ICBA's 5,000 members at this important hearing on the proposed Consumer Financial Protection Agency (CFPA).

ICBA believes that consumer protection is the cornerstone of our financial system. It is the virtue that defines community banking and allows institutions like mine to stand out in a very crowded field of competitors. The 8,000 community banks in this country operate in the shadow of a relative handful of megabanks, and cannot compete on margins or economies of scale. Were all things equal, it would not be possible for many of ICBA's member banks to have existed for well over a century, as they have. It is consumer protection – manifested as special attention paid to the individualized needs of each customer, better rates and terms for lending products, and the knowledge that with local decision-making comes local accountability – that has made the community banking sector resilient for generations.

During this economic downturn, increasing numbers of consumers have recognized this distinction and have moved their assets to local banks with proven track records of conservative and sensible financial stewardship. Customers are attracted to do business with community banks because they are responsible lenders, with local decision-

---

[1] The Independent Community Bankers of America, the nation's voice for community banks, represents 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve.
With nearly 5,000 members, representing more than 20,000 locations nationwide and employing nearly 300,000 Americans, ICBA members hold $1 trillion in assets, $800 billion in deposits, and $700 billion in loans to consumers, small businesses and the agricultural community.

making and a vested interest in their local economies. This is why community banks have not gotten into trouble through the use of exotic lending products that led other large firms into bankruptcy or partial government ownership. This relationship is symbiotic: Instilling confidence in our customers that they will be treated honestly means a community banker is not going to take excessive risks, and will certainly not engage in an abusive practice to drive customers away. It also explains why community bankers never relaxed their lending standards simply to compete with the megabanks and non-bank lenders.

Target the source of the problem

However, where virtues exist, so must vice. As we now know, two distinct classes of firms operate in a way that proved abusive to consumers – one above and one below the radar, yet both managing to avoid adequate regulation: above was the group of over-leveraged, too-big-to-fail firms whose concentration risks have cost American taxpayers over $7 trillion in economic worth. These firms are, undeniably, under the jurisdiction of myriad federal regulators. However, these regulators have neither the means to resolve a systemically risky financial firm, or the mandate to scrutinize these firms to match the level of danger they and all their disparate parts represent to the broader economy. Below the radar exist far too many non-bank financial institutions, peddling their wares, unencumbered by most forms of government regulation, accountability, or care for the future well-being of those to whom they lent indiscriminately. It is these firms that should be the focus of the CFPA.

Furthermore, to protect consumers, Congress needs to make passing legislation to identify institutions that may pose a systemic risk a first priority this fall. They must subject these mammoth firms to stronger supervision, capital and liquidity requirements, and better protect the taxpayers by establishing a systemic risk fund paid for by those firms. An important part of the solution to the too-big-to-fail problem is contained in H.R. 2897, the Bank Accountability and Risk Assessment Act, introduced by Representative Luis V. Gutierrez, and ICBA urges the Committee to incorporate this measure into any broader financial regulatory reform proposal it considers in the future.

H.R. 3126, the CFPA Act of 2009, as introduced

As currently drafted, ICBA is very concerned that H.R. 3126 would do more harm than good by unduly burdening our nation's community bankers who did not engage in the deceptive practices targeted by the proposal, yet would be hardest hit by the added regulatory burden imposed by this new agency.

First, we appreciate that the legislation does not transfer enforcement authority over the Community Reinvestment Act (CRA) to the new agency. This is a common-sense step that allows current prudential regulators to maintain their authority over this law. CRA is intended to ensure that banks are providing services to all segments of the community. Similarly, other fair lending statutes, such as the Equal Credit Opportunity Act (ECOA) and Home Mortgage Disclosure Act, should also remain with the current financial regulatory agencies that will be conducting safety and soundness examinations.

For community banks, safety and soundness and consumer protection are not mutually exclusive functions. The legislation creating the CFPA regrettably splits the safety and soundness and consumer protection functions, going so far as to place this new agency as the ultimate arbiter of any dispute between a prudential regulator and itself. While community banks go above and beyond to protect their customers, allowing consumer protection to trump safety and soundness is a dangerous precedent. Bank regulators have expertise in balancing safe and sound operation with the need to provide consumers information they need to make informed financial decisions and protect them from unfair and harmful practices.

In addition, and contrary to conventional wisdom, the concept of prescribing a "plain vanilla" list of financial products will harm, not help, community banks. That is why we are pleased that the Chairman's proposed revisions to the bill eliminate this requirement. To be sure, community banks are able to offer consumers simpler products when it is appropriate; but "simpleness" as a doctrine should not be promoted at the expense of all other products or, more importantly, a customer's needs. The "plain vanilla" mandate contained in the introduced version of H.R. 3126 would create a structure for certain financial products, where some must meet a lesser threshold of acceptance while others must face more scrutiny and require more paperwork. Community banks do not have robust legal and compliance departments to handle this sort of product approval regime: it is, on average, no more than three people. As a consequence, any incentive a CFPA creates – intentionally or otherwise – to offer "plain vanilla" products will amount to a disincentive for community bankers to offer anything *but* those products. In this regard, a level playing field will put small, local bankers at a tremendous competitive disadvantage relative to their larger competitors.

Improvements in discussion draft, but further changes needed

ICBA appreciates that Chairman Frank has begun to address other community bank concerns in the recently released discussion draft. Removal of a "plain vanilla" product mandate or authority is very significant; this deletion must be maintained as this legislation advances. We are also pleased that the CFPA may no longer apply a "reasonableness" standard in assessing whether an act or practice is unfair. Such vague standards, while not unknown to the banking sector, create uncertainty and invite litigation – two things anathema to community bankers.

That said, there remain significant areas of the proposal to which we object:

- The task of examining a bank for consumer protection compliance should remain with the banking agencies. As discussed previously, ICBA believes the regulatory, enforcement and examination powers shifted to the CFPA would unwisely separate consumer protection from safety and soundness enforcement, when both types of enforcement must co-exist under one agency for efficient financial services regulation. Separating this enforcement among two different agencies would only give each agency half the information it would need to conduct thorough examinations. We believe the CFPA should focus its resources on the not-insubstantial task of setting up an exam system for non-banks, rather than stripping the existing agencies of their consumer compliance examiners. Lax supervision of non-bank lenders was a key contributor to our financial crisis, not the carefully supervised activities of community banks.
- Rulewriting for banks cannot be the sole responsibility of the CFPA, and should be shared jointly between CFPA and the federal banking agencies. If the CFPA is not equally interested in the safety and soundness of the lender, it is likely to promulgate unnecessarily burdensome or contrary rules to those issued by the prudential regulator.

- The Chairman's discussion draft modifies the leadership structure of the proposed CFPA, creating an autonomous director, while establishing an advisory board with virtually no authority. ICBA is strongly concerned with this approach, which lacks any form of substantive checks and balances, and provides no meaningful voice for community bank viewpoints in the decision-making process of the Agency. The advisory board should be vested with real authority over this powerful agency.
- Regarding funding of the CFPA, if the agency is not funded by appropriations, ICBA strongly supports assessments on non-bank financial firms under the CFPA's jurisdiction as a main source of Agency funding. However, we are strongly opposed to the CFPA's authority to assess fees on federally insured depository institutions. Since the Chairman's new draft also draws funds from the Federal Reserve System, it is unnecessary to assess further fees on the community banking sector.
- The numerous reporting requirements in this bill place a disproportionately high burden on community banks without a commensurate benefit to consumers. The cost of these mandates is very high for small institutions that simply do not have the extra resources available to comply. The committee should review the cost and utility of these reporting requirements for community banks and eliminate those that do not appropriately balance costs and benefits.

Conclusion

It was just over a year ago that the collapse of Lehman Brothers helped trigger a credit crisis that crippled the economy. Congress owes it to the American people to modernize our financial consumer protection regulations of the many non-bank financial firms, and to address the challenges posed by systemically risky and too-big-to-fail institutions.

However, the proposed CFPA highlights a long-standing challenge facing community banks, namely encouraging policymakers to distinguish between large and small financial institutions and not to assume that a one-size-fits-all approach is an appropriate way to legislate or regulate the financial sector. If the current economic crisis has proven anything, it is that there are significant disparities between the way large firms and smaller firms do business, a fact that should be considered before applying a "broad-brush" legislative approach toward protecting consumers.

In recent Congressional testimony, administration officials pointed out the disparity between the existing regulatory regimes for federally insured banks and those for non-bank financial firms. ICBA agrees that the lack of sufficient regulatory oversight of many unregulated firms, particularly those in the mortgage industry, contributed significantly to our financial crisis. However we disagree with a response that, instead of focusing on regulatory gaps and augmenting existing systems, places community banks into an entirely new regime with only vague limits and checks on its powers.

We must end too-big-to-fail and reduce systemic risk in order to protect consumers, local communities, our financial system and the economy from the destabilizing effects that occur when a giant institution runs into trouble. Community banks fund growth, drive new business development, help families buy homes, and finance education. We are not responsible for the current state of our economy but are the victim of others' bad practices. Yet, we continue to help the people and businesses in our communities recover from this crisis and find a way back to prosperity. ICBA looks forward to working with this Committee to create a financial system that better protects consumers while not overburdening or restricting the ability of thousands of community bankers from serving their customers' legitimate credit and investment needs.

Thank you, and I look forward to your questions.

Statement
of the
U.S. Chamber
of Commerce

ON: PERSPECTIVES ON THE CONSUMER FINANCIAL PROTECTION AGENCY

TO: U.S. HOUSE OF REPRESENTATIVES COMMITTEE ON FINAINCAIL SERVICES

BY: ANDREW J. PINCUS, PARTNER, MAYER BROWN LLP

DATE: SEPTEMBER 30, 2009

The Chamber's mission is to advance human progress through an economic, political and social system based on individual freedom, incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation, representing more than three million businesses and organizations of every size, sector, and region.

More than 96 percent of the Chamber's members are small businesses with 100 or fewer employees, 70 percent of which have 10 or fewer employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business manufacturing, retailing, services, construction, wholesaling, and finance – is represented. Also, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the U.S. Chamber of Commerce's 112 American Chambers of Commerce abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross section of Chamber members serving on committees, subcommittees, and task forces. More than 1,000 business people participate in this process.

Chairman Frank, Ranking Member Baucus, and Members of the House Financial Services Committee, thank you for the opportunity to appear before you today on behalf of the U.S. Chamber of Commerce to address the Consumer Financial Protection Agency Act ("the Act").

The Chamber strongly supports the Administration's goal of enhancing consumer protection. Even before the financial crisis hit, the Chamber's Center for Capital Markets Competitiveness called for regulatory reform, including strengthening consumer protections. The crisis has clearly illuminated the shortcomings of our outdated regulatory system. Millions of consumers and investors were harmed, in part because of regulatory gaps but just as much or even more because of regulators' failure to exercise the authority – especially the enforcement authority – that they already possess.

The Chamber believes that consumers need:

- Clearer disclosure and better information;
- More vigorous, effective enforcement against predatory practices and other abuses; and
- Elimination of regulatory gaps that allowed some financial services entities to escape regulation applicable to their competitors.

We need smarter, more effective regulation. Adding new regulatory layers and enacting expansive, and duplicative, regulatory authority will not produce that result. Rather, it is likely to lead to confusion, uncertainty, and a regulatory system that imposes heavy burdens on business without providing the protections that consumers need.

On September 23rd, the Chamber released a study conducted by Thomas Durkin, an economist who spent more than 20 years at the Federal Reserve. Durkin concluded that regulatory burdens associated with a lack of preemption and legal uncertainties created by new, vague, and undefined statutory terms would reduce the ability of financial institutions to extend consumer credit, and would likely increase the cost of credit that is available.

Moreover, this reduction in credit would impact small businesses as well, because it would affect the very consumer financial products that small businesses use to supplement business credit, which often is not available to small and new enterprises. At the very time when we need these job-creators the most in order to restore growth to our economy, we will be hobbling their efforts by reducing their access to the credit that is essential to fuel that growth. I have submitted a copy of Mr. Durkin's study with my testimony.

The Chamber opposes the CFPA legislation in its current form because it believes the current bill is the wrong way to enhance consumer protection, and it will have significant and harmful unintended consequences for consumers, for the business community and for the overall economy.

Chairman Frank's September 22 memorandum identified a number of the specific concerns that we have expressed. However, illustrating the complexity of these issues and the need for careful assessment of the impact of proposed provisions, the changes made in the bill do not address the concerns discussed in the memorandum.

I will focus my remarks on six areas:

- The scope of the current draft legislation;
- the vague regulatory burdens that it would impose;
- the requirement that covered businesses offer particular products;
- the lack of coordination among federal regulators;
- the creation of new state regulatory authority; and
- the lack of preemption.

Scope

The scope of H.R. 3126 as introduced is sweeping, giving the CFPA authority to regulate businesses and professionals far beyond traditional consumer finance.

The bill does not focus on entities that are solely, or even principally, engaged in financial services activities. Rather, it casts an extremely broad net that would encompass a vast segment of the entire economy.

We appreciate the recognition of this overbreadth in Chairman Frank's September 22 memorandum. Unfortunately, the revised bill does not solve the problems created by the underlying bill's expansive approach. Here are just a few examples of the many I can cite:

- Merchants and Retailers

Although Section 124(a) provides that the CFPA does not have authority "regarding credit or other financial activity issued **directly** by a merchant, retailer or seller of nonfinancial services to a consumer" (emphasis added), the definitions of "extending credit" and "covered person" remain unchanged, leaving open the possibility that a merchant could be found by the CFPA to "indirectly" engage in financial activity or to be a "material service" provider to a covered person. For example, a business that merely accepts credit cards could meet either of those qualifications – either indirectly engaging in a financial activity (the provision of credit by the credit card network) or providing a material service to the credit card network.

In addition, although businesses that *sell* stored value cards are now exempt, businesses that *issue* stored value cards – or that merely allow their names or trademarks to be used on stored value cards – remain subject to regulation as a "covered person."

- Accountants, Lawyers, and Tax Preparers

Section 124(e) exempts accountants, lawyers, and tax preparers, but provides that the exemption "shall not apply....to the extent such person is" engaged in a "financial activity" or is otherwise subject to the existing federal consumer laws. That means that any activity by an accountant or lawyer that falls within the broad "financial activity" definition – provision of tax planning advice in connection with estate planning, for example – or any activity that the Agency classifies as a financial activity under its rulemaking authority would trigger the applicability of the statute.

Moreover, although tax preparation services are no longer expressly included in the definition of "[a]cting as a financial advisor" (Section 101(18)(H)), such services are not expressly excluded from that definition. Accordingly, there is a risk the Agency could simply interpret the broad language of the definition ("providing financial and other related advisory services") to include tax preparation.

- Real Estate Brokers and Auto Dealer

The exemptions for real estate brokers and auto dealers suffer from the same flaw as the one for accountants, lawyers, and tax preparers: they do not apply if the person is engaged in a financial activity or otherwise subject to the existing federal consumer laws.

In addition, even the limited protection provided by the exemptions fails to encompass activities in which these individuals routinely engage. Thus, the "real estate broker" exemption does not include negotiations relating to financing and the auto dealer exemption does not apply to lease transactions and excludes activities relating to the arranging of financing. That means that auto dealers likely will be covered by the statute for *all activities other than all-cash vehicle sales*.

- New "Related Person" Provision

The bill includes a new provision, defining the term "related person" (Section 101(30)), which is applicable to all entities other than bank holding companies, credit unions, and depository institutions. It includes:

  - "any director, officer, employee charged with managerial responsibility, or controlling stockholder of, or agent for, such covered person" and "any shareholder, consultant, joint venture partner, and any other person as determined by the Director who materially participates in the conduct of the affairs of such covered person."

- Also included is "any independent contractor (including any attorney, appraiser, or accountant), with respect to such covered person, who knowingly or recklessly participates in any" violation of "any" law or regulation or breach of fiduciary duty.

Any person who is a related person "shall be deemed to be a covered person for all purposes of" the new law and the existing federal laws.

This provision has extremely broad implications. It allows the Agency to impose fees on, and require reports from, employees, shareholders, directors and others. And it broadly subjects shareholders and directors to the Agency's authority, even with respect to activities unrelated to the covered person with which they are associated.

The portion of the definition relating to independent contractors casts the net even farther: independent contractors are transformed into "covered persons" – and become subject to regulations that didn't previously apply – if they "recklessly" have "participated" in a violation of any law. How can these entities protect themselves? Any association with a covered person that engages in wrongful conduct could trigger regulatory obligations that the contractor previously ignored, based on a very vague and uncertain standard. More importantly, that standard can be invoked in an action seeking damages by the Agency, a State Attorney General, or a plaintiffs' lawyer to whom a State Attorney General has outsourced the case. This is a huge expansion of potential liability.

We recognize that there is a similar concept, institution-related party, in the banking law. But the proposed use of the concept here is much broader – including imposing all of the Agency's regulations on a previously-unregulated party and subjecting that party to liability for class-action type damages.

- Agency Authority to Expand its Own Jurisdiction

Another troubling aspect of H.R. 3126 is that it gives the Agency the authority to expand its own jurisdiction, including within the scope of "financial activity" "any other activity that the Agency defines, by regulation as financial activity for the purposes of this title." That opens the door to ever-expanding jurisdiction through regulatory fiat and without congressional review.

The revised draft includes standards that the Agency must meet to expand its authority, but those standards impose no real limitations. The Agency need only find that:

- "the activity has, or there is likelihood that the activity will have, a material adverse impact on the creditworthiness or financial well-being of consumers," or
- "the activity is incidental or complementary to any other financial activity regulated by the Agency," or
- "the activity is entered into or conducted as subterfuge or with a purpose to evade" the provisions of the bill or existing consumer protection laws.

These new standards for expanding the Agency's authority are vague and vulnerable to varying interpretations – the "substantial likelihood" test gives the Agency the ability to hypothesize adverse consequences and then extend its regulatory reach based on its own suspicions. And given the broad-based authority of the Agency, there could be a relatively low threshold for defining activities as "incidental" or "complementary" (a term that appears to be drawn from banking law, where it did receive a broad interpretation).

Vague Statutory Standards

Another aspect of H.R. 3126 that provoked considerable concern is the provision that, without any action by the Agency, would have imposed vague regulatory standards upon covered persons—standards that would have required businesses to determine the extent to which consumers comprehended particular information.

Although this provision (Section 132(b)) has been removed from the revised bill, new language has been added to Section 138(1) making it "unlawful for any person" to engage in any unfair, deceptive or abusive act or practice. This provision imposes broad liability on anyone – not just a covered person – any time the Agency later determines that person's conduct is "unfair", "deceptive" or "abusive," even if there was no regulation requiring a particular disclosure or prohibiting the particular practice. It thus subjects businesses to broader and vaguer standards than the language deleted from the bill.

Requirement of "Plain Vanilla" Products

The revised bill does not include the provision of H.R. 3126 that imposed the "plain vanilla" product requirement (Section 136). But nothing in the revised bill prevents the Agency from imposing that very same requirement, or otherwise pushing consumer products toward standardization, by using its broad authority to prevent "abusive" acts and practices (Section 131), which includes the imposition of "requirements for the purpose of preventing such acts or practices" or by invoking its "fair dealing" authority (Section 137). Furthermore, the elimination of preemption of state law means that States would be free to impose a "plain vanilla" requirement even if the Agency did not do so, and 50 different such requirements at that.

Regulatory Coordination

Separating the regulation of financial products from regulatory expertise regarding the safety and soundness of financial institutions threatens consumers as well as the stability of the entire financial system. The vast majority of consumer protection issues also implicate safety and soundness concerns. Frequently, the issues are two sides of the same coin: pricing a product to reflect its cost and risk may promote safety and soundness but also may implicate consumer protection concerns.

The revised bill attempts to address this issue by creating a dispute resolution process. It is not clear whether that process could be effective – even the bill recognizes that it could take 60 days for an issue to be resolved, and experience with statutory deadlines indicates that they are rarely met.

More importantly, Section 123(c)'s resolution procedure applies only to conflicting "material supervisory determinations" between the CFPA and a federal banking agency. It *does not* apply to "any regulation or guidance, or order of general applicability" -- and therefore would not apply to the significant risk that the CFPA would adopt regulations that conflict with safety and soundness principles.

Lack of Preemption

At a time when harmonization has been identified by all stakeholders as a goal of regulatory reform, the proposed CFPA will do exactly the opposite. Rather than adopting a new national standard and eliminating multiple and conflicting state laws, the new agency would set the floor, creating inconsistencies, duplications, and conflicting mandates between the federal and state agencies.

Thus, the bill rolls back 150 years of banking law by subjecting national banks for the first time to a labyrinth of state consumer protection mandates. And if that were not problematic enough, the bill gives States independent power to interpret and enforce the federal standards – even if they adopt an interpretation different from the Agency's.

Again, thank you for the opportunity to testify, and I look forward to answering the Committee's questions.

WASHINGTON BUREAU · NATIONAL ASSOCIATION FOR THE ADVANCEMENT OF COLORED PEOPLE
1156 15TH STREET, NW SUITE 915 · WASHINGTON, DC 20005 · P (202) 463-2940 · F (202) 463-2953
E-MAIL: WASHINGTONBUREAU@NAACPNET.ORG · WEB ADDRESS WWW.NAACP.ORG

TESTIMONY OF HILARY O. SHELTON,

DIRECTOR, NAACP WASHINGTON BUREAU &

SENIOR VICE PRESIDENT FOR ADVOCACY AND POLICY

BEFORE THE HOUSE FINANCIAL SERVICES COMMITTEE

on

"PERSPECTIVES ON THE CONSUMER FINANCIAL PROTECTION AGENCY"

September 30, 2009

Thank you, Mr. Chairman, Ranking Member Bachus and members of the Committee on Financial Services for inviting me here today. I appreciate the opportunity to share with you the views of the NAACP on the creation of a Consumer Financial Protection Agency, or CFPA. I would also like to begin by thanking you, Chairman Frank, for all you have done and continue to do to help low- and middle-income Americans, as well as racial and ethnic minority Americans attain financial security. In fact, NAACP members from across the Nation who were fortunate enough to hear your presentation at our annual convention in New York earlier this year are still talking about the new agency and its promise for our communities.

More than one hundred years old, the NAACP today is our Nation's oldest, largest and most widely recognized grassroots civil rights organization. We currently have more than 2,200 units in every state in the country, as well as in Italy, Germany, Korea and Japan.

The NAACP is very supportive of the creation of a strong and effective Consumer Financial Protection Agency with the protection of civil rights and a directive that it seek out and work to eliminate discrimination as a core part of its mandate. We need clear and concise rules, clearly and vigorously enforced, if we are to promote economic security and growth throughout our Nation. For too long, racial and ethnic minorities, the elderly and others have been targeted by unscrupulous lenders and underserved by traditional financial institutions. The result of this lack of standard rules and strict enforcement of the rules that we do have has been the financial stagnation, and in too many cases, the economic ruin, of entire communities.

Our current system of consumer protection fails to protect Americans of all races and backgrounds from the most basic exploitation and abuses that can cost individuals and families hundreds of thousands of dollars, and even their homes. Current laws and enforcement allow a range of institutions to escape supervision because responsibility for consumer protection is fragmented across too many regulators. Too many finance companies are not regulated at all at the Federal level.

When they have been engaged, too many regulators have spent too much time in recent years asking "What's the effect on the financial firm?" without asking "What's the effect on consumers?" As a result, among other problems, regulators permitted inappropriate mortgages and abusive credit card practices. And the result of these misplaced priorities, as we have seen, has been an almost complete collapse of not only our Nation's economy, but the near ruination of the global financial system as well.

In the recent crisis, many of the people who were targeted by unscrupulous lenders lost their savings, their financial security, and in too many cases their homes. Sadly, many of the worst abusers consistently targeted low-income families, racial and ethnic minorities, women and the elderly.

Examples of the financial abusers targeting racial and ethnic minorities abound, and can be found throughout the mortgage arena, where predatory lenders consistently targeted African Americans and others. This was also done in credit card abuses and in payday lending, just to name a few.

For example, in the American mortgage market predatory lenders have, for decades, targeted African American borrowers and other racial and ethnic minorities as well as the elderly with their nefarious products. A study by the Center for Responsible Lending demonstrated that for most types of subprime home loans, African American and Latino borrowers are more than 30% more likely to have higher fees and interest rate loans than Caucasian borrowers, even after accounting for differences in risk[1]. In fact, United for a Fair Economy estimates that people of color are 2 to 5 times more likely to receive a predatory loan than white borrowers.[2] Put in other terms, sub-prime mortgage originators have flooded minority communities with high-cost, unsustainable loans that were made to consumers without regard to their ability to repay or the value of the property. From 2000 to 2007, communities of color lost between $164 and $213 billion,[3] and the numbers keep rising as the foreclosure crisis worsens. Fannie Mae and Freddie Mac estimate that up to half of the borrowers who received subprime loans should have qualified for "prime-rate" conventional loans, had mortgage lenders exercised proper business sense.[4]

This is not a new trend. As far back as 2000, a study by the U.S. Department of Housing and Urban Development clearly demonstrated that many people of color could qualify for more affordable loans than they were receiving[5]. In 1996, a study by Fannie

[1] Center for Responsible Lending. May 31, 2006. "*Unfair Lending: The effect of Race and Ethnicity on the Price of Subprime Mortgages*" Debbie Gruenstein Bocian, Keith Ernst and Wei Li.
[2] "The Silent Depression: State of the Dream 2009," United for a Fair Economy, 2009.
[3] "Foreclosed: State of the Dream 2008," United for a Fair Economy, 2008.
[4] See the Center for Responsible Lending's *Fact Sheet on Predatory Mortgage Lending* at http://www.responsiblelending.org/pdfs/2b003-mortgage2005.pdf, and *The Impending Rate Shock: A Study of Home Mortgages in 130 American Cities*, ACORN, August 15, 2006, available at www.acorn.org.
[5] *Unequal Burden: Income and Racial Disparities in Subprime Lending in America* (Washington, DC: HUD, 2000).

Mae and Freddie Mac reported that as many as a third of the families who receive subprime loans actually qualify for prime loans[6].

Sadly, mortgage lenders are not the only ones who target racial and ethnic minority communities with their wealth-stripping products. In the credit card market, one report showed that 15% of African-American and 13% of Latino card users have cards with interest rates over 20%, compared to only 7% of White card users – many of whom are responding to credit card solicitations with preset terms and conditions. Our communities were also hard hit by the exploitative ploys of some credit card companies which would hike interest rates and charge excessive fees, often without any advance notice and sometimes without the knowledge of the credit cardholder.

And payday lenders are notorious for setting up their shops, and charging incredibly exploitative rates, in abundance in African American communities. To paraphrase Julian Bond, the Chairman of our National Board of Directors, payday lenders are as common in African American communities as Starbucks Stores are in middle class communities that are predominantly White.

It is because of these targeted abuses that the NAACP strongly supports the creation of a strong Consumer Financial Protection Agency. As envisioned, the CFPA would provide the government with the tools necessary to help consumers navigate and be treated fairly by what is often a confusing and potentially ruinous environment; it would support if not require regulators to become more protective of consumers; and it would make civil rights protections more of a key element in the regulation and oversight of financial services.

It is also because of the systemic discriminatory and abusive lending practices and the resulting wealth-stripping, ruinous effects, that we feel very strongly that the newly created Consumer Financial Protection Agency must be given the mandate as well as the power to seek to prevent and remedy illegal discrimination. We were pleased to see and are supportive of the provisions in the latest draft of the CFPA legislation that creates an Office of Fair Lending and Equal Opportunity, and makes the fight against discrimination based on race or ethnic background part of the mandate of the new agency. These provisions will go a long way toward putting some teeth into the laws that are already on the books and to protecting consumers, all consumers, as they attempt to navigate our Nation's financial services.

One area that the NAACP would like to see the current CFPA proposal strengthened is that we would like to see regulation of the Community Reinvestment Act, the CRA, fall under the CFPA's jurisdiction. We need to renew, reinvigorate, modernize and expand CRA, and I appreciate the comments of the Chairman last week when he said that he, too, is serious about updating this important law. I would suggest that perhaps in the

---

[6] Freddie Mac. September 1996. *Automated Underwriting: Making Mortgages Lending Simpler and Fairer for America's Families. Washington DC*

course of reauthorizing CRA, this committee consider putting authority for this important law under a newly created and robust CFPA. In order to fully address the needs of local communities, many of which are represented by the NAACP, the CFPA should be able to review and enforce lending laws at that level.

Mr. Chairman, members, as I have said all along, the NAACP strongly supports the creation of a robust CFPA and appreciates all the work that has gone into including civil rights protections in the draft that we are currently discussing. It is our belief that a strong CFPA will go a long way toward addressing the very real needs of enforcement and regulation in the financial services arena. However, let me make it clear that we have no illusions that this new agency will fully address all of the needs and shortcomings that continue to plague our communities, and indeed our Nation.

We still need strong laws to address many of the problems that allow unscrupulous lenders to target low- and moderate-income Americans, as well as racial and ethnic minority Americans and the elderly at all levels of the economic scale. Specifically, the NAACP will continue to fight for aggressive anti-predatory lending laws, as well as curbs on abusive payday loans and real assistance for homeowners facing foreclosure.

In that vein, I look forward to continuing to work with you, Mr. Chairman, as well as all of the other members of this committee to enact strong legislation to help all Americans gain the American dream of economic security.

Thank you again for inviting me here today and I stand ready to take any or your questions.

Testimony of

Edward L. Yingling

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Committee on Financial Services

United States House of Representatives

Testimony of

Edward L. Yingling

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Committee on Financial Services

United States House of Representatives

Chairman Frank, Ranking Member Bachus, members of the Committee, thank you for inviting me to testify today on the proposed Consumer Financial Protection Agency (CFPA) and the September 25 Discussion Draft. I am Edward L. Yingling, President and CEO of the American Bankers Association.

The American Bankers Association brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $13.3 trillion in assets and employ over two million men and women.

Since I testified before this Committee in July on the CFPA, I will not repeat all the points I raised at that time about our industry's great concern with the CFPA proposed by the Administration. Since the Administration first proposed the CFPA, there has been a constructive debate about the merits of the overall concept and about many of its specifics. ABA wishes to thank the members of this Committee and their staffs for the attention they are giving to this important topic and to the issues ABA and others have raised.

When I testified in July, I asked the Committee to look at this issue not only from the point of view of consumers, whose concerns should be paramount, but also from the point of view of community bankers – the great, great majority of whom had nothing to do with the causes of the financial crisis, but who are struggling with the economic implications of the crisis and with a growing mountain of regulatory burdens which will almost certainly increase dramatically over the next year.

Since I last testified, I asked ABA's staff to determine the total amount of consumer regulations and guidelines to which banks are currently subject. The answer is 1700 pages of fine print, and that is just in the consumer area. Since the median size bank has 34 employees, that means the median size bank today has 50 pages of fine print in the consumer area for each employee. That also means half the banks in the country have more than 50 pages for each employee.

I want to express the appreciation of the ABA for the consideration many members of this Committee have given to the situation of traditional banks, and to the unnecessary burden the Administration's CFPA proposal would place on these banks. There is simply no justification for imposing significant new burdens on heavily regulated banks that never made one subprime loan, nor contributed to the causes of the financial crisis.

Our country has seen a terrible financial crisis and a deep recession, which has hurt many people. Many have lost their jobs; many have lost their homes; and many have seen their savings drastically reduced. Reform is needed. For the last year, ABA has supported broad reform, including in testimony several times before this Committee. We have supported, among other reforms: the creation of a systemic risk oversight agency; the creation of a strong resolution system, one that aggressively addresses the problems caused by the too-big-to-fail concept; the filling of regulatory gaps for derivatives, hedge funds, mortgage brokers and others; reform of the accounting standard setting process; additional authority for the Fed to regulate the payments system; improved international cooperation; and improved consumer protections.

While there were many causes of the financial crisis, failures of consumer protection in the mortgage arena certainly contributed. Some consumers were given mortgages that should never have been made and, in many cases, consumers did not understand the financial risks and future obligations they were taking on. As Congress moves to strengthen consumer regulation, however, it is important to focus on what the problem areas were. The debate on the CFPA has served the valuable purpose of more clearly identifying the problems.

Those lobbying for the CFPA almost uniformly point to two main examples to support the creation of the CFPA: first, the failure of the Fed to use HOEPA to fully address abusive mortgage practices and, second, the failure of the Fed to move earlier on its credit card rule. More recently, proponents have criticized the Fed for not moving sooner on overdraft protection plans. In addition, there has been strong criticism from many parties, including the ABA, of the failure to adequately regulate the non-bank providers of financial services, particularly in the mortgage area. In fact, the fundamental weakness in HOEPA was that there was no provision for adequate enforcement on non-banks.

Thus, the two areas that have been identified in this debate as needing reform are the need for a more direct focus by federal regulators on consumer issues and the need for more enforcement on non-banks[1]. The ABA agrees that reforms are needed in these two areas.

On the other hand, in our opinion, no real case has been made for major changes in two other areas: first, requiring additional enforcement on banks and credit unions; and, second, a large increase in consumer regulatory powers. On the first point, while the argument is made that federal regulators should have developed stronger regulations and done so sooner, there is little indication that, once regulations are issued, they are not generally enforced on banks and credit unions. Certainly there does not appear to be sufficient reason to impose heavy new regulatory requirements and costs on banks and credit unions for regulatory oversight and exams. On the second point, the Fed had the HOEPA authority and has the clear authority to address credit card issues (already done) and overdraft protection (in process). In fact, the expanded use of the UDAP (Unfair and Deceptive Acts and Practices) by the Fed creates a powerful general tool in addition to all the specific consumer laws.

The CFPA, as proposed by the Administration, unfortunately, goes well beyond addressing the two weaknesses identified – the need for more direct focus on consumer issues and stronger regulation and enforcement on non-banks. The Administration proposal unnecessarily imposes new burdens on banks and credit unions and creates an agency with vast and unprecedented new powers.

Discussion Draft

Last week, Chairman Frank released a new discussion draft with a number of changes to the Administration's CFPA proposal. We are pleased to note that the discussion draft addresses several issues ABA has raised and takes into account some of the potential additional burdens on traditional banks.

The discussion draft addresses the following issues:

➢it removes the requirement that banks offer government designed "plain vanilla" products;

[1] As used in this testimony, the term "non-banks" refers to entities engaged in financial services that are not FDIC-insured banks or credit unions As the Congress moves to expand regulation and enforcement on non-banks, a grey area that needs further attention is the consumer regulatory regime that should apply to bank holding companies and their non-bank subsidiaries. The ABA is currently developing recommendations in this area, and it may be that consumer regulatory oversight of such entities should be more explicitly given to the holding company regulator This would be in keeping with recent Federal Reserve determinations.

- it removes the unworkable requirement that communications with consumers be "reasonable";
- it requires coordinated exams of banks by the CFPA and safety and soundness regulators;
- it provides a stronger dispute resolution mechanism when a bank is caught in a dispute between the consumer and prudential regulators;
- it provides a more explicit and stronger mandate to focus on the non-banks that were the primary cause of the financial crisis;
- it provides a more equitable funding structure for the CFPA; and
- the structure of the CFPA is modified to provide stronger input from the bank regulators.

These are significant improvements, and we are also pleased that Secretary Geithner expressed general agreement with these changes when he testified before this Committee last week. We also appreciate the fact that Chairman Frank had previously removed the Administration provision that would have moved CRA authority to the CFPA, a provision that would have undermined the balance we have achieved in designing CRA lending while maintaining safety and soundness principles.

The additional focus in the discussion draft on non-bank providers of financial services is particularly important. As Chairman Frank is quoted as saying in Sunday's Washington Post: "If we only had community banks and credit unions, we wouldn't be in this problem." One of our major concerns with the CFPA as proposed by the Administration is that it would not adequately focus on the non-bank sector, where the subprime mortgage crisis really began. The actions in the non-bank sector not only instigated the subprime crisis, but they skewed the markets in ways that badly affected some banks. The discussion draft rightly focuses the regulatory and enforcement authority more on non-banks than the original proposal did.

The discussion draft also provides exemptions for a number of entities. In general, we agree that it makes no sense to have the CFPA regulate normal commercial activities or incidental financial transactions. Our concern is that the exemptions be crafted in a manner that does not exempt entities by their "label" if, in reality, they are engaged in true financial activities that raise significant consumer protection issues – for example, a realtor engaged in the subprime mortgage process. We recognize the language in the draft attempts to address this issue, and we may suggest further language to strengthen the discussion draft in this regard.

Problems with the Discussion Draft

The ABA still has major concerns in the following principal areas:

- the draft removes preemption of state and local laws; without preemption, we will have a patchwork of laws that will result in increased costs and less credit availability;
- the CFPA has extensive new powers to "legislate" its own rules, rather than applying the existing rules created by Congress;
- the draft creates a new agency that, while improved in design, will conflict with the safety and soundness regulators.

Preemption

The ABA strongly supports the preemption of state laws under the National Bank Act, a preemption that has existed since the Civil War. We believe that without such preemption we will have a patchwork of state, and even local, laws that will confuse consumers, greatly increase the cost of financial services, and serve as a strong disincentive to create new products of value to consumers. A simple visual helps to show the problem: proponents of the CFPA promise it will create simple, one-page disclosures (a goal we share), but the removal of preemption will result in page after page of disclaimers and disclosures about all the differing state and local laws applicable. We clearly have national markets for consumer financial products and services, and we need to be able to apply national standards. There can, however, be a better balance and coordination between the federal and state efforts. Too often, in recent years, issues have been addressed in litigation rather than by cooperation.

CFPA Powers

As stated above, there has been little justification given for the broad new powers given to the CFPA under the Administration's proposal. The discussion draft removes two of those explicit powers – designing plain vanilla products and requiring communications to be "reasonable." However, even with those changes, the proposed CFPA would be given unprecedented power. Consider for example:

- Section 131, which changes the UDAP standard by adding the word "abusive", throwing away all the developed legal standards on UDAP and giving the agency a vague, unknown, and very broad ability to declare practices "abusive."

- Section 133, which gives the CFPA open-ended authority to regulate the manner in which consumer products and services are provided.
- Section 136 (a)(1), which mandates that the CFPA create regulations "to ensure fair dealing with consumers." "Fair dealing" is a standard so vague and broad that the CFPA could justify almost any regulatory action.
- Section 136 (a)(3), which gives the CFPA broad authority to regulate the compensation of those providing products and services to consumers, with the only limitation being that the CFPA cannot provide an overall cap.

Another provision of great concern is Section 137, which provides broad authority to obtain information from providers of financial institutions. While there are some safeguards in the provision, it could impose significant hardships on providers, particularly small firms, and could easily be abused by law firms and other groups for fishing expeditions or to threaten providers with significant compliance costs. At a minimum, providers should be allowed to recoup their costs for complying with non-routine information requests.

The broad powers and the vague legal terms used (such as "abusive" and "fair dealing") will create great uncertainty in the markets, as no one will know what the new rules of the road are for many years. This will undoubtedly cause firms to cut back on the extension of credit and to avoid testing new products and services in the marketplace for fear they will run afoul of future legal standards.

From a broader perspective, as I testified in July, the proposed delegation of authority to the CFPA is so vast that it renders all previous consumer laws enacted by Congress – including the recently enacted credit card law – mere floors. Several members of this Committee have raised concerns about this delegation, which basically gives the CFPA authority to legislate, and we believe they are correct in their concerns.

CFPA

As the debate has proceeded on the CFPA, a number of different approaches to the fundamental structure of the consumer regulator have been suggested, including:

- the CFPA as proposed by the Administration;

- the CFPA in the discussion draft, which has a single head, with an advisory board of other regulators and more coordination of exams of banks;
- the proposal from FDIC Chairman Sheila Bair to create a CFPA, but leave enforcement with respect to, and examination of, banks and credit unions to the prudential regulator;
- providing a stronger role and mandate to an enhanced, and possibly expanded, FFIEC;
- adjusting the current structure by imposing requirements for greater focus and reporting to Congress on consumer issues.

As we have previously testified at length, the ABA opposes the creation of a new agency focused on consumer protection on the fundamental principles that, first, you cannot separate the regulation of products from the regulation of the entity providing the products, and that, second, safety and soundness and consumer protection are too intertwined to separate. However, as discussed above, ABA agrees there is a need to improve the focus on consumer issues and to strengthen the regulation of non-banks. We have previously provided the Committee with suggestions to achieve these objectives, and we will continue to provide further suggestions.

Conclusion

There is a demonstrated need to strengthen consumer protection in the financial arena. ABA is committed to working with Congress to strengthen the structure of consumer protection, while avoiding undermining the availability of credit and imposing new, unnecessary costs on both consumers and financial services providers.

CUNA
Credit Union National Association
601 Pennsylvania Ave., NW | South Building, Suite 600 | Washington, DC 20004-2601 | PHONE: 202-638-5777 | FAX: 202-638-7734
cuna.org

September 30, 2009

The Honorable Barney Frank
Chairman
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

The Honorable Spencer Bachus
Ranking Member
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

Dear Chairman Frank and Ranking Member Bachus:

On behalf of the Credit Union National Association (CUNA), I am writing regarding today's hearing entitled, "Perspectives on the Consumer Financial Protection Agency." CUNA represents approximately 90 percent of America's 8,000 credit unions and their 92 million members.

Consumers of financial products—especially consumers of products and services provided by currently unregulated entities—need greater protections. An agency with the primary mission of consumer protection could be an effective way to achieve that protection, provided it does not impose duplicative or unnecessary regulatory burdens on credit unions. Credit unions did not in any way contribute to the current financial debacle and their current regulatory regime, coupled with their cooperative structure, militates against credit unions ever contributing to a financial crisis.

We have been carefully following the development of legislation to create a Consumer Financial Protection Agency (CFPA) because its enactment could significantly affect credit unions. Following up on our letter to you of July 14, 2009, we would like to discuss our views on the latest draft of CFPA legislation.

In our view, the discussion draft takes several steps in the right direction, including clarifying that credit unions will not be required to offer a plain vanilla financial product before offering a product that better meets the needs of the member, providing the Chairman of the National Credit Union Administration a seat on the CFPA Oversight Board, and directing the CFPA Director to take into account disclosure requirements under other laws in order to enhance consumer compliance and reduce regulatory burden. The discussion draft also includes several provisions designed to ensure that the CFPA does not result in an increase in fees and assessments on depository institutions.

Nevertheless, we remain concerned that the language in the discussion draft does not go far enough to ensure that the agency seek ways to reduce regulatory burden on credit unions and eliminate duplicative and redundant regulation. Additionally, there are several other areas that remain of great concern to credit unions, including the examination and enforcement authorities conveyed to the CFPA, the treatment of credit insurance products, the collection of depositor data, and the treatment of state consumer protection law. As the Committee proceeds to mark-up the Consumer Financial Protection Agency Act, we hope these concerns will be given serious consideration.

Examination, Supervision and Enforcement
Credit unions remain concerned that the legislation will result in additional, annual examination requirements they will have to prepare for and fund, and that those examinations will be conducted by examiners who are not familiar with credit unions and do not understand or appreciate what makes them unique.

As we indicated in our July letter, we believe that CFPA should have full authority to write the rules for consumer protection, but for regulated entities such as credit unions, the examination, supervision and enforcement of these regulations should be retained by the prudential regulator, with all consumer protection exam reports and actions shared with the CFPA. The currently unregulated entities should certainly be examined by the CFPA. We would also support giving the CFPA back-up examination powers over regulated depository institutions, such as when material complaints repeatedly arise about the implementation of a particular regulation. We would also support the ability of CPFA examiners to examine regulated depository institutions on a random, backup basis.

Most policymakers with whom we speak, both in Congress as well as within the administration, tell us that credit unions ought not to worry about the examinations because of how credit unions offer products to their members. We agree completely. Credit unions are not concerned about the results of a separate consumer protection examination; credit unions question the necessity for a separate examination given the fact that credit unions are largely viewed as offering consumer-friendly financial products, and the abuses that precipitated the crisis did not emanate from the credit union system.

The concern credit unions have is how this new examination authority will affect service to credit union members. Most credit unions are extremely small institutions relative to the largest banks and non-bank entities; some have just a handful of employees. A separate consumer protection examiner will distract credit unions from their mission and divert resources away from serving their members. We appreciate the language in the current discussion draft that would require the CFPA to coordinate examinations with an institution's prudential regulator, but we have concerns about how this coordination would work.

Moreover, the discussion draft appears to envision scenarios in which credit unions could receive conflicting guidance from their safety and soundness examiner and the CFPA examiner. The creation of an administrative proceeding to resolve these disputes may be well-intentioned and necessary, but it also helps illustrate the structural problem that the legislation creates by subjecting credit unions to examinations by entities with different core interests. Additionally, the dispute resolution process will increase costs for credit unions that may become involved in the process. We feel strongly that credit union members will ultimately be better served if the prudential regulator has primary responsibility for the examination, supervision and enforcement of consumer protection laws.

Regulatory Consolidation and Modernization

The CFPA legislation represents an important opportunity to begin the long process of consolidating and modernizing the various consumer protection statutes and regulations. Over the course of the last several decades, the current consumer protection laws have been layered on top of each other producing duplicative mandates and disclosures.

These duplicative and overlapping rules are draining the resources of many credit unions and must be eliminated. We have been heartened by the comments of proponents of this legislation who tout the potential for the reduction of regulatory burden. As Harvard University Professor Elizabeth Warren testified, "a single regulatory agency watching out for families and individuals can reduce the overall regulatory burden."[1] Assistant Treasury Secretary Michael Barr has made similar statements: "The CFPA is not a new layer of regulation; it will consolidate existing regulators and authorities. This will bring efficiencies for industry."[2]

The potential for compliance to be streamlined, consumer understanding increased, and duplicative requirements eliminated is one of the attractive features of a single agency responsible for writing the regulations for all consumer regulation. For instance, the reconciliation of the *Truth in Lending Act* (TILA) and the *Real Estate Settlement Procedures Act* (RESPA) mortgage lending disclosures is strongly supported by credit unions. We continue to urge Congress to ensure that this vision becomes a reality.

In July, we asked you to consider changes to H.R. 3126 that would require the CFPA to streamline and modernize consumer protection regulation to minimize unnecessary regulatory burden. We appreciate that Section 132 of the discussion draft states, "the Director shall take into account disclosure requirements under other laws in order to enhance consumer compliance and reduce regulatory burden." However, we hope the Committee will consider additional language to ensure that going forward the agency seek ways to minimize the burden its regulations will have on credit unions.

Credit unions are also understandably concerned that an agency with the sole mandate of developing and amending consumer law regulations will continually modify them to respond to new issues and complaints. A new CFPA must have procedures to assure that credit unions are not overwhelmed with regulatory revisions. We encourage the Committee to ensure that regulations adopted by the CFPA have reasonable compliance effective dates and are amended in an orderly fashion so that regulations are not continually being revised. The Federal Reserve Board's April-October schedule for TILA changes provides one model for how changes could be considered and adopted.

---

[1] Testimony of Elizabeth Warren before the House Financial Services Committee. June 24, 2009. 5.

[2] Testimony of Michael Barr before the House Energy and Commerce Committee. July 8, 2009. 9.

Treatment of Credit Insurance
CUNA is concerned that credit life and credit disability insurance products have been included as a covered product in this legislation, while all other forms of life insurance are specifically excluded from the purview of the proposed CFPA. We believe that CFPA regulation of credit life and disability insurance would be duplicative and would also add an additional compliance burden on credit unions that offer these financial products to their members. That is because the proposed CFPA would have indirect regulatory authority over these products by virtue of its authorities under the TILA and the *Home Owners Equity Protection Act* (HOEPA).

TILA, implemented by the Federal Reserve Board's Regulation Z, requires that borrowers be informed of loan costs, including the cost of credit insurance. Further, Regulation Z requires a written disclosure informing the borrower that "*the purchase of credit insurance is optional and not a condition of credit and will not be provided unless the borrower agrees to pay for the coverage*." The borrower must indicate the election of coverage in writing. In addition, the 2002 amendments to HOEPA already have had the effect of significantly reducing the use of single-premium credit insurance on real estate secured lending.

If the underlying concern with respect to these products relates to the merits of single-premium credit insurance, we suggest that an alternative approach would be to prohibit single-premium credit insurance products in connection with residential mortgage loans. Earlier this year, the House of Representatives passed a bill, H.R. 1728, which included this type of language, and CUNA could support this approach as an alternative to the credit insurance language presently under consideration.

Collection of Depositor Information
As we stated in July, we believe that collection of depositor data by census tract should only be required of institutions for which similar data is not already collected by a federal or state regulator. There should be significant limits to the use of this data by the CFPA.

We are concerned with the provisions of the proposed legislation that require the CFPA to collect depositor data by census tract because these data collection requirements could increase credit unions' regulatory and reporting burdens. We urge Congress not to permit the CFPA to collect data on entities from which similar data is already being collected by their prudential regulator.

In January, the National Credit Union Administration (NCUA) inaugurated a data collection program for Federal credit unions under which membership profile data is obtained during each regulator examination. The data is uploaded to NCUA's central office and a membership income profile is generated using geo-coding software. NCUA also uses the 5300 report to obtain information on the financial services that credit unions offer their members. Credit unions believe this data collection program provides sufficient information on members' income levels and services provided and that additional data collection from credit unions in these areas would be redundant and burdensome.

Treatment of State Law
In order to achieve the regulatory simplicity that is a key objective for consumers and financial institutions alike under the new agency, there needs to be one rule of the road on consumer

protection issues. We are well aware of the sensitivities of proposing federal preemption of state laws. However, if Congress creates a CFPA, and its rules merely become the floor in terms of consumer protection, many state laws will remain or be passed, and the size and complexity of consumer disclosures will be unmanageable for institutions and incomprehensible for consumers.

We urge Congress to preempt state consumer protection law when establishing the CFPA, and we are confident that by charging a single federal agency with the responsibility to regulate consumer protection law, as well as with rigorous Congressional oversight, more thorough consumer protection regulation will be achieved. We also believe that state concerns can be addressed through participation on the CFPA Oversight Board, as the legislation envisions.

Simply put: if the CFPA is sufficiently empowered to be a credible regulator ensuring nationwide consumer protection, why should any additional state rules be necessary? Conversely, if the proposed CFPA is not expected to be adequate to the task, why establish such a new agency in the first place?

Closing
On behalf of America's credit unions and their 92 million members, thank you very much for the opportunity to share our perspective on the CFPA legislation. As the Committee proceeds to mark-up, we look forward to working with you and would be happy to discuss these issues further.

Sincerely,

Daniel A. Mica
President and CEO

Statement of

Mortgage Bankers Association

For the

Committee on Financial Services

United States House of Representatives

Hearing on

Perspectives on the Consumer Financial Protection Agency

September 30, 2009

The Mortgage Bankers Association [1] appreciates the opportunity to provide this statement for the record for the Financial Services Committee's hearing titled "Perspectives on the Consumer Financial Protection Agency" (CFPA).

MBA shares this committee's dedication to developing more effective protections for consumers and providing needed reforms to the housing finance system. Just as this committee has worked toward this objective, MBA has dedicated its own resources to developing what we regard as ground-breaking proposals for reform of our industry. Our proposals would establish new, rigorous national mortgage lending standards and new regulation of nondepository mortgage bankers and mortgage brokers that would fit well within an improved federal regulatory structure.

While we believe the introduction of the administration's proposals and H.R. 3126, the Consumer Financial Protection Agency Act of 2009, as well as the recent revisions to that proposal, are important steps on the path to regulatory reform, we also believe that before this committee takes action, much more work needs to be done. Changes to the financial regulatory structure will have profound effects on the availability and affordability of mortgage financing and other financial products and services for years to come. These proposals must not be rushed through. They must be judiciously considered so reform is done right.

Since H.R. 3126 was introduced this summer, MBA has had an opportunity to consult with our members concerning some of the key details of the legislation and we are now prepared to provide more extensive views than we did in our testimony on July 15, 2009, before this committee. We will continue to seek our members' views as we work with this committee and the entire Congress to further develop these important reform initiatives.

An Unparalleled Time for Regulatory Reform and Improved Consumer Protection

As MBA has stated before, the nation faces a once-in-a-generation opportunity to improve the mortgage lending process. The current dual federal-state regulatory framework has demonstrated that it is badly in need of an overhaul if it is to provide effective oversight of all aspects of the financial services industry and better serve consumers. The scope and powers of financial services regulators have not kept pace

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: Hwww mortgagebankers orgH.

with advances in the type, sophistication and delivery mechanisms of the financial products, services and providers they are tasked with regulating. This has resulted in broad supervisory gaps in some areas of the industry and costly redundancies in others.

We believe carefully crafted regulatory improvements would help restore investor and consumer confidence in the nation's lending and financial markets and assure the availability and affordability of sustainable mortgage credit for years to come. At the same time, if regulatory solutions are not well-conceived, they risk exacerbating a credit crisis that trillions of public dollars have still not fully resolved. In this regard, we must emphasize that consumer protection regulation must be carefully constructed to have its intended effects and best serve all consumers – those who have benefitted greatly from the mortgage market as well as those who have been confused or even harmed.

In our view, the Mortgage Improvement and Regulation Act (MIRA), attached to this statement (Attachment 1), which MBA developed and is described below, is the right combination of improvements to serve consumers. We urge the committee to consider it as an alternative, or as a complement, to H.R. 3126.

Consumer Financial Protection Agency

MBA appreciates the recent effort to revise H.R. 3126 and supports key changes that would narrow the focus of the CFPA. The proposed CFPA would, however, still be charged with regulating a wide array of broadly defined "financial activities" that would include, among other things: deposit-taking activities; extending credit and servicing loans; check cashing and check-guaranty services; collection of consumer debts; real estate settlement services; certain leasing activities; acting as an investment adviser if not subject to CFTC or SEC regulation; acting as a financial adviser; financial data processing; money transmitting; issuance of stored value; acting as a money services business or as a custodian of money or any financial instrument; and any other activity that the Director defines, by regulation, as a financial activity.

The CFPA would be just as broadly empowered to:

- Ensure the appropriate and effective disclosure or communication to consumers of costs;
- Restrict unfair, deceptive, or abusive acts or practices in connection with any transaction with a consumer for a consumer financial product or service;
- Prescribe rules and issue orders regarding the manner, settings and circumstances for the provision of any consumer products or financial services;
- Establish new duties of care for covered persons;
- Establish duties regarding compensation practices including yield spread premiums (YSPs);
- Ban mandatory arbitration;
- Establish operating requirements like bonding, recordkeeping, and the like;
- Enforce the law through orders and penalties; and
- Perform a variety of other functions including research.

Under H.R. 3126, the CFPA also would be reassigned all of the consumer financial protection functions of the Board of Governors of the Federal Reserve (Board), the Comptroller of the Currency (OCC), the Office of Thrift Supervision (OTS), the Federal Deposit Insurance Corporation (FDIC), and the Federal Trade Commission (FTC). These regulators would have secondary, or back-up, enforcement authority.

A top concern for MBA is that while the CFPA's powers would be broad, its rules and accompanying law would only serve as a "floor," not a "ceiling" for future state legislation. States would be empowered to enact or issue additional statutes, regulations, orders, or interpretations in the area of consumer financial protection as long as they offered greater protection to consumers. H.R. 3126, therefore, would exacerbate the patchwork of laws that provide uneven protection and increased costs to consumers. H.R. 3126 also would make national banks subject to additional state laws. MBA believes that more, not less, preemption is called for to establish uniform national standards and that federal and state cooperation to develop and assure enforcement of uniform standards would be far more responsive to current needs than what is proposed under H.R. 3126.

MBA's Mortgage Improvement and Regulation Act (MIRA)

In contrast to H.R. 3126, MBA's MIRA proposal would establish uniform national mortgage lending standards that include a comprehensive set of substantive requirements and consumer protections. These uniform national standards would apply to all mortgage lenders and mortgage lending institutions, regardless of their size, charter type, or which regulator has responsibility for them.

In arriving at these standards, MIRA builds on the Federal Reserve Board's new rules under the Home Ownership and Equity Protection Act (HOEPA). These rules include greater protections for subprime borrowers, with new requirements for ability to repay determinations, documentation, escrows and prepayment penalties. The standards also include requirements for all mortgage loans to stem appraiser coercion, servicing and advertising abuses.

Additionally, MIRA includes other standards that were developed by this committee as part of H.R. 1728, the Mortgage Reform and Anti-Predatory Lending Act of 2009, which was approved by the House of Representatives. It also includes new transparency provisions to conform Real Estate Settlement Procedures Act (RESPA) and Truth in Lending Act (TILA) disclosures and MBA's own initiatives, such as proposals for a duty of care for loan originators – all with an eye to assuring greater transparency, consumer protection and returning liquidity to the market.

MIRA's changes to the regulatory structure would include establishment of a new federal regulatory authority that should be nested within an existing federal prudential regulator to implement the new lending standards and, for the first time, regulate independent nondepository mortgage bankers and mortgage brokers at the federal level. The new regulator would also be charged with operation of the nation's mortgage counseling and financial literacy programs, resulting in greater focus on these important efforts. The proposal even requires that lenders and brokers pay the costs of their own regulation.

While MIRA's new standards would be truly uniform and preemptive of state lending laws, they also would be dynamic. To achieve this, MIRA would establish a council of state and federal regulators to revisit and update the standards regularly and to address any new abuses and concerns. Federal banking agencies would enforce the uniform standards against national banks. At the same time, state and federal regulators would be required to work together in reviewing and examining nondepository mortgage bankers and brokers and other state regulated lenders in enforcing the new standards.

Overall, the proposal is both comprehensive and workable and would be complementary to other regulatory reform proposals. We would note that as a result of our recent consultations with MBA members, we will soon be updating the MIRA proposal to include new provisions, including consolidating regulatory authorities in a federal prudential regulator.

MBA's Recommended Changes to H.R. 3126

While MBA and its members support robust improvements to consumer protection regulation, MBA has very strong concerns about the establishment of a separate consumer protection regulator along the lines proposed. MBA strongly urges that Congress should revise the legislation to:

1. **Establish preemptive uniform national mortgage lending standards and a meaningful partnership between state and federal regulators to keep the standards up-to-date and to enforce them consistently across the nation.**

   To achieve uniform national mortgage lending standards, MBA would urge that the committee delete provisions that: (1) establish the new CFPA's regulations as a floor, not a ceiling, for consumer protection requirements; (2) undermine the preemption available to national banks under current law; and (3) encourage states to enact their own additional laws, which will unnecessarily increase costs to consumers. In their place, the committee should add provisions that establish robust but preemptive uniform national mortgage lending standards for all lenders that will offer consumers sound, consistent protection nationwide.

   Also, in order to ensure that the protections are up to date, H.R. 3126 should: establish a Council of State and Federal Regulators to consult at least quarterly with the new federal financial regulator assigned responsibility for mortgage lending; report to Congress annually on needed additions to the uniform national mortgage standards to address abuses; consult on regulations before they are publicly proposed; advise on the regulation of independent mortgage bankers and brokers, including licensing standards and registration; promote consistent examinations and regulatory actions; and consult on the development and operation of national financial literacy, counseling and consumer information.

These changes would establish rigorous, dynamic uniform national lending standards that would be enforced through a partnership of state and federal regulators. Because the standards would apply to all lenders, they would maximize competition to lower costs, while providing consumers nationwide the highest level of consumer protection. Such an approach would be superior to one that would perpetuate and, in fact, worsen the patchwork of federal and state laws that have lessened competition, resulted in unnecessary costs, and failed to adequately protect consumers consistently throughout the nation. (A map illustrating the current patchwork of state lending laws is appended to this statement as Attachment 2).

2. **Assign responsibility for implementation of the uniform lending standards to a federal prudential regulator in order to strengthen consumer protection in the most effective manner possible.**

MBA believes this change would strengthen consumer protection in the most effective manner possible by assigning responsibility for the new lending standards to a federal prudential regulator, already responsible for regulation of financial institutions. Such a regulator would also be required to have an office specifically dedicated to regulation of mortgage lending functions. This change also would assure that all regulatory imperatives, including important protections and safety and soundness are well considered and carried out. To accomplish this objective, the committee should delete provisions in H.R. 3126 that would establish the CFPA as a separate agency within government.[2] It also should substitute provisions that assign regulatory functions for mortgage lending to a mortgage lending regulator within a prudential federal financial regulator.

Separating mortgage lending regulation from prudential financial regulation, as proposed in H.R. 3126, will fail to achieve an appropriate balance of the competing considerations of prudential financial supervision and consumer protection. Financial regulators have a critical role, balancing different objectives such as supporting and maintaining the integrity of competitive markets, guarding against systemic risk, and protecting depositors, borrowers, and investors. A wise regulator, armed with appropriate statutory guidance, subject to appropriate oversight, and seeking input from all interested parties, will achieve a balance among competing objectives. On the other hand, a regulator singularly focused on any one of these objectives risks being myopic to other important concerns.

It is particularly notable that separate bureaucracies in government, each assigned a portion of regulatory responsibility, have a poor track record of effective regulation. The split of programmatic and financial regulatory responsibilities for Fannie Mae and Freddie Mac, between the Department of Housing and Urban Development

[2] H.R. 3126, Section 111.

(HUD) and the Office of Federal Housing Enterprise Oversight (OFHEO), is a troubling example, recently corrected by Congress. So, too, is the split of regulatory authority for mortgage transactions between HUD and the Federal Reserve that continues to result in piecemeal, uncoordinated RESPA and TILA reform.

While MBA recognizes that there are profound concerns among some in Congress about past failures of federal financial regulators, it also believes that these matters can be addressed by strengthening accountability to Congress through reporting, hearings and, if necessary, other means such as budgetary restrictions to ensure performance. To abandon the concept of a fully empowered financial regulator assuming mortgage lending and other consumer protection functions based upon recent shortcomings is to ignore the clear benefits of robust consumer protection and financial regulation operating in tandem.

3. **Close the existing gaps in regulation of lenders and mortgage brokers, and assign their regulation to a federal prudential regulator.**

   Clearly, there are gaps in the regulation of independent mortgage bankers and mortgage brokers from state to state. While the MBA appreciates that H.R. 3126 attempts to address this problem, the bill does not, in MBA's view, do so in an optimal manner. The bill assigns regulation of mortgage brokers and nondepository mortgage bankers solely to the CFPA. Yet prudential regulators are experienced in supervision and examination and would be far better equipped to immediately establish processes for examination and supervision of these entities in conjunction with the states. They would also be better equipped to establish consistent nationwide qualifications – including net worth, bonding and other qualifications – as well as implementing uniform national mortgage lending standards. For these reasons, MBA believes the committee should add provisions to the bill assigning regulation of nondepository mortgage bankers and mortgage brokers to a federal prudential regulator.

4. **Truly improve and simplify disclosures now rather than permitting successive efforts by HUD, the Federal Reserve and the CFPA.**

   While H.R. 3126 suggests that HUD and the Federal Reserve should work together to achieve a single combined RESPA/TILA disclosure, or have the effort become the responsibility of CFPA, the bill does not require immediate HUD-Fed collaboration as did H.R. 1728, passed by the House of Representatives earlier in this session. Absent action under this bill to require HUD and the Federal Reserve to cooperate now, the industry and consumers face years of piecemeal reform under RESPA, then TILA, and potentially under a new consumer regulator. Accordingly, the bill should be revised to require HUD to at least temporarily suspend implementation of its impending RESPA rule and require it and the Federal Reserve to work together to simplify RESPA and TILA disclosures on a coordinated and comprehensive basis. A change to the bill to require these two agencies to work together now would avoid unnecessary costs and bring comprehensive mortgage disclosure reform to consumers considerably more quickly.

5. **Maintain the provisions consolidating federal regulatory authorities, not in the CFPA but in a federal prudential regulator.**

   MBA applauds the fact that H.R. 3126 would transfer and consolidate the array of current federal consumer financial protection functions. MBA regards this effort as another important step in assuring consistent consumer protection regulation of lenders at the federal level. It believes, however, that rather than assigning federal functions to the CFPA, they should be assigned to a federal prudential regulator.

   Consumers today bear the burden and costs of diverse and uncoordinated regulation from a wide array of federal regulators. The failure of HUD and the Federal Reserve to adequately coordinate on RESPA and TILA is the latest example of how federal agencies operating independently can increase regulatory burden without providing optimal benefits for consumers. A far better model would assign consumer protection functions to a federal prudential regulator and make it fully accountable to Congress for its performance in carrying out its charge.

Conclusion

MBA believes a combination of the committee's proposals and MBA's MIRA proposal is the best avenue to improve consumer protection.

Rather than dispersing regulatory authority, MBA's proposal would close existing regulatory gaps by assigning regulation of nondepository mortgage lenders and mortgage brokers to a federal prudential regulator. It would also assure far greater consumer protection by implementing rigorous, uniform, national lending standards.

Uniform national standards would be far more effective than the patchwork of inconsistent laws which add unnecessary costs and confusion to the process. A new uniform model would not only arm consumers with new protections, but it would sharpen the focus of those who are charged with protecting them.

The federal mortgage regulator would work in partnership with state officials to update and enforce the standards, protecting consumers in every state from abuse. The underlying law also would assure funding from regulated entities so both federal and state regulators would have the resources they need to carry out their important work.

In sum, we are grateful for the administration and the committee's important steps in this area. We look forward to working together to improve these proposals to provide consumers the protections they deserve and to ensure the vitality of the nation's mortgage financing system for years to come.

Attachments

Attachment 1 – MBA's Mortgage Improvement and Regulation Act (March 2009)

Attachment 2 – MBA's Map of the Patchwork of State Laws

MORTGAGE BANKERS ASSOCIATION
Investing in communities

Outline of Draft Proposed Legislation
"Mortgage Improvement and Regulation Act of 2009 (MIRA)"
As of March 19, 2009

Executive Summary

Overview: This legislation, entitled the "Mortgage Improvement and Regulation Act of 2009," or "MIRA" would establish a tough new, federal regulatory scheme for mortgage lending. Specifically, it would establish new uniform national standards and a new national regulator, assisted by state officials, to replace the current patchwork of state and federal mortgage lending laws. The key sections of MIRA are as follows:

I. **Purposes** – Describes MIRA's purposes as: establishing a new, comprehensive framework for national regulation of mortgage lending to protect borrowers nationwide; to ensure consistent regulation of independent mortgage bankers and mortgage brokers; to invigorate a fairer and more competitive primary mortgage market and increase transparency; to facilitate greater secondary market investment; and to otherwise foster a return to stability of the nation's financial system.

   MIRA achieves these purposes by: establishing a new federal regulator responsible for mortgage lending standards; requiring the regulator to implement rigorous uniform national mortgage lending standards enacted under MIRA, as well as servicing standards, that are to be supplemented as necessary by the Director in consultation with state and federal regulators; assigning the regulator responsibility for regulating independent mortgage bankers and mortgage brokers including establishing uniform licensing and registration standards with increased net worth and bonding requirements; assigning disclosure, counseling and financial literacy responsibilities to the new regulator; and preempting state and local lending laws, as necessary;

II. **Definitions** – Defines all necessary terms including the standards (or "triggers") for higher priced or subprime loans which are subject to special requirements under the Act;

III. **New Regulator** – Establishes a new Federal Mortgage Regulatory Agency (FMRA), within the Treasury Department, headed by a Director of Federal Mortgage Regulation (Director) to be responsible for regulating mortgage lending including implementing and establishing Uniform National Mortgage Standards (UNMS) by regulation; regulating independent mortgage bankers and mortgage brokers in partnership with state financial regulators who also shall review for compliance with and examine and enforce the UNMS for such entities; consulting with federal and state financial regulators which shall examine, review and enforce the UNMS for federal and state depository institutions which they regulate respectively and operating national financial literacy, counseling and consumer information programs;

IV. **New Advisory Council** – Establishes a Council of State and Federal Regulators (CSFR) to consult at least quarterly with the Director and report to Congress annually on needed additions to UNMS to address abuses; to consult with the Director on regulations before they are publicly proposed; to advise on the regulation of independent mortgage bankers and brokers, including licensing standards and registration; and to consult on the development and operation of national financial literacy, counseling and consumer information;

V. **New Oversight Board** – Establishes a Mortgage Lending Oversight Board, comprised of the Secretaries of Treasury and Housing and Urban Development (HUD) and the Chairman of the Federal Reserve Board, to oversee operations of FMRA;

VI. **Uniform National Standards** – Establishes Uniform National Mortgage Standards (UNMS) which include substantive requirements and consumer protections. UNMS include all of the restrictions that the Federal Reserve recently promulgated by regulation under the Home Ownership and Equity Protection Act (HOEPA) for higher priced (nonprime) loans and for all closed-end loans and restrictions against unfair mortgage advertising. These include requirements that lenders determine a borrower's ability to repay, require documentation verifying income and/or assets, limit prepayment penalties, and establish escrow accounts for taxes and insurance. UNMS also includes key prohibitions from H.R. 3915 (passed by the House of Representatives in November 2007) including, but not limited to, additional provisions to improve mortgage servicing and the appraisal process to protect consumers as well as provisions developed by the Mortgage Bankers Association. For example, a revised duty of care would require that all loan originators including loan officers for mortgage lenders (lender loan officers) and loan officers for mortgage brokers (mortgage broker loan officers): (1) comply with all licensing and registration requirements; (2) present the consumer with a choice of loan products for which the consumer likely qualifies which is available from that lender, and which may be appropriate to the consumer's existing circumstances, based on information obtained by the originator; and (3) make full and timely disclosures to each consumer of (a) comparative costs and benefits of each loan product offered or discussed and (b) whether the originator is or is not acting as an agent for the consumer. The duty of care would also require that (4) the mortgage broker loan officer provide the borrower a disclosure of the mortgage broker's total compensation including any amounts that the broker may receive from the lender based on a higher rate or the terms of the loan; and (*5*) a consumer must affirmatively, opt-in, in writing *prior to closing*, to a nontraditional mortgage product[1] after the lender's loan officer or mortgage broker discloses the costs and benefits of the loan to the borrower, also in writing;

VII. **Additions to Standards** – Requires the Director to meet at least quarterly in consultation with CSFR to supplement the UNMS as necessary, to promulgate such changes by regulation and to report to Congress annually on the need for additional changes and their disposition;

VIII. **Regulatory Responsibilities** – Requires the Director to implement the UNMS to regulate mortgage lending activities nationally; to supplement the UNMS as necessary in conjunction with the CSFR; to regulate activities of non-depository mortgage bankers and mortgage brokers including establishing uniform licensing and registry requirements for such entities in conjunction with the CSFR (including net worth and bonding requirements) with licensing and registration requirements to be applied by state officials; to work in partnership with state regulators to examine, review and enforce the UNMS for non-depository mortgage bankers and brokers; and to consult with federal and state financial regulators which shall examine, review and enforce the UNMS for federal and state depository institutions which they regulate respectively;

IX. **Penalties/Remedies** – Clarifies existing penalties for noncompliance such as the right of rescission, and also establishes alternative remedies for borrowers and a right to cure for lenders;

X. **Enforcement/Examination Authorities** – Authorizes the Director, federal agencies and state agencies to review, examine and enforce the UNMS concerning all mortgage lending operations and also confers rights on private parties to enforce provisions of MIRA;

XI. **Financial Literacy and Counseling** – Assigns the Director responsibility of operating a national financial literacy and counseling program including requiring mandatory counseling for reverse mortgages, HOEPA highest cost mortgages and interest-only mortgages for first-time homebuyers under certain conditions including the availability of sufficient counseling resources to avoid denying or unreasonably delaying the availability of mortgage credit;

XII. **Mortgage Fraud** – Provides increased resources for investigating and prosecuting mortgage fraud;

---

[1] A nontraditional mortgage product is a mortgage product that allows a borrower to defer principal or interest, such as a payment option ARM or an interest-only loan.

XIII. **Initial Funding** – Authorizes start-up funds for establishment of the FMRA and its first two years of operations including the costs of consumer testing, financial literacy, counseling and anti-fraud activities;

XIV. **Resources for Regulation Going Forward/Sharing Funds With States** – Beyond the start-up period, authorizes FMRA to charge a reasonable assessment of each entity regulated by the FMRA to defray the costs of regulation. States would receive licensure and registry fees and would share in assessments on regulated entities for examination and enforcement to extent appropriate to avoid duplicate charges on regulated entities;

XV. **Improving Transparency** – Requires HUD and the Federal Reserve to work in consultation with FMRA to develop simplified, uniform and national disclosure forms and consumer information. This would include combined and coordinated RESPA and TILA Good Faith Estimate (GFE) disclosures, HUD-1 and final TILA disclosures as well as accompanying consumer information. Also, MIRA requires these agencies to develop forms to facilitate borrower understanding of the mortgage process and lender, broker and their loan officers' duty of care for consumers: (1) to provide information regarding their circumstances, including the consumer's risk appetite, to assist the loan officer or mortgage broker in deciding which loan products should be presented to the consumer; (2) to affirmatively opt-in to a nontraditional mortgage product following a disclosure explaining the option, including the risks and benefits of an adjustable loan; and (3) to disclose the amount of a mortgage broker's compensation;

XVI. **Preemption** – Amends federal and state laws as necessary including preempting contrary state laws.

More Detailed Outline of MBA's MIRA Proposal

Specifically, MIRA:

I. **Purposes -** Describes its purposes as: establishing a new, comprehensive framework for national regulation of mortgage lending to protect borrowers nationwide; to ensure consistent regulation of independent mortgage bankers and mortgage brokers; to invigorate a fairer and more competitive primary mortgage market and increase transparency; to facilitate greater secondary market investment and to otherwise foster a return to stability of the nation's financial system. The short-term responses to the mortgage crisis have been national in scope and so too should be the long-term solutions.

The Act indicates that it seeks to achieve this purpose by:

A. Establishing a new federal regulator responsible for mortgage lending standards;

B. Requiring the regulator to implement rigorous uniform national mortgage lending standards enacted under MIRA, including substantive requirements for originations, servicing standards and means of making the market much more transparent, that are to be supplemented by the federal regulator in consultation with state and federal regulators, as necessary, with greater requirements applicable to subprime lending;

C. Assigning state and federal regulators concurrent responsibility for reviewing, examining and enforcing the uniform national standards while conferring new, more effective enforcement means;

D. Assigning the new regulator responsibility for regulating, and establishing uniform licensing and registration standards, with increased net worth and bonding requirements, for independent mortgage bankers and mortgage brokers;

E. Assigning disclosure, counseling and financial literacy responsibilities to the new regulator; and

F. Preempting state and local lending laws as necessary.

II. **Definitions -** Defines all necessary terms including:

A. "Council of State and Federal Regulators (CSFR)" means an advisory body of mortgage regulators representing each of the 50 states, the District of Columbia and United States territories as well as representatives of the Federal Reserve, Comptroller of Currency, Office of Thrift Supervision, the Federal Deposit Insurance Corporation, the National Credit Union Administration and the Federal Trade Commission;

B. "Federal Mortgage Regulatory Agency (FMRA)" means an independent office within the U.S. Treasury Department established under this Act;

C. "Federal Mortgage Regulatory Agency Oversight Board" or "Oversight Board" shall be composed of the Secretary of Treasury, Chairman of the Federal Reserve Board and the Secretary of HUD;

D. "Higher Priced Loans" for first lien residential mortgage loans are 1.5 percentage points above the average prime offer rate issued by Freddie Mac, and for second-lien loans are 3.5 percentage points over the same index. The Director may adjust these limits as necessary through rulemaking to more precisely define higher cost or subprime loans;

E. HOEPA Covered Loans are Highest Cost or Section 32 residential mortgage loans that meet the following tests:
   1. For a first-lien loan, the annual percentage rate (APR) exceeds by more than eight percentage points the rates on Treasury securities of comparable maturity;
   2. For a second-lien loan, the APR exceeds by more than 10 percentage points the rates on Treasury securities of comparable maturity; or
   3. The total fees and points payable by the consumer at or before closing exceed the larger of $561 or eight percent of the total loan amount. (The $561 figure is for 2008. This amount is adjusted annually by the Federal Reserve Board, based on changes in the Consumer Price Index.) Credit insurance premiums for insurance written in connection with the credit transaction are counted as fees.

F. "Nontraditional mortgages" are residential mortgage loans that allow borrowers to defer principal or interest;

G. "Qualified mortgages" are residential mortgage loans that have APRs that are do not exceed the Federal Reserve higher cost triggers;

H. "Regulated entity" – Non-depository residential mortgage lenders and residential mortgage brokers;

I. "Residential mortgage loans" are any extensions of credit to purchase, finance construction, or refinance secured by a 1-4 unit dwelling;

J. "Uniform National Mortgage Standards (UNMS)" includes standards promulgated under this Act and amended by the FMRA in consultation with the CSFR.

III. **New Regulator -** Establishes a Federal Mortgage Regulatory Agency (FMRA) as an independent office within the federal government or within an agency of government:

A. Headed by a Director, confirmed by the Senate, for a five-year term responsible for implementing and establishing UNMS, regulating independent mortgage bankers and brokers and operating national financial literacy programs and establishing national mortgage transparency and disclosure requirements in consultation with the Council of State and Federal Regulators (CSFR);

B. Assigns powers to the FMRA and the Director on par with the general powers of the Federal Housing Finance Agency (FHFA) and its Director including, but not limited to, the power to appoint employees and examiners, to contract and to remain outside the appropriations process;

C. Also assigns sufficient powers to the FMRA and the Director to assure consumer protection and prudential operations by mortgage bankers and mortgage brokers to provide financing needs to consumers. Such regulation should be principles-based to the greatest extent feasible to assure market innovation and lower borrower costs while assuring much better consumer protection;

D. Stipulates that FMRA should have deputy directors, including:

1. Deputy Director for Mortgage Standards
2. Deputy Director for Regulation
3. Deputy Director for Financial Literacy and Information.

IV. **New Advisory Council -** Establish a Council of State and Federal Regulators (CSFR) that shall include representatives of all members of the Federal Financial Institutions Examination Council (FFIEC), and representatives of the District of Columbia and all 50 state's financial regulators. The CSFR shall:

1. Advise the FMRA on an ongoing basis of abuses occurring which are not addressed by the UNMS;
2. Make recommendations for additions to the UNMS;

3. Provide advice and guidance on regulating regulated entities, operation of the financial literacy counseling program and other matters at the request of the Director;
4. Be headed by an executive committee of nine members which shall be elected by the members and meet monthly with the Director, in person or by phone;
5. Meet quarterly with at least one annual in-person meeting; and
6. Report to the Congress annually on recommendations by the CSFR and their disposition.

V. Oversight Board - Establishes a Mortgage Lending Oversight Board.

The Oversight Board shall:

1. Meet regularly and oversee the operations of the FMRA;
2. Provide any necessary advice to the FMRA; and
3. Establish a strategic plan for the FMRA to carry out its mission.

VI. Uniform Mortgage Standards - Establish Uniform National Mortgage Standards (UNMS) that include standards for nontraditional and subprime loans and standards for all loans that include:

A. *Note - This section includes Federal Reserve HOEPA restrictions largely verbatim.* Enacting into legislation the requirements for higher cost or subprime loans (called "not qualified mortgages" pursuant to H.R. 3915) promulgated by the Federal Reserve in regulations under the Home Ownership and Equity Protection Act (HOEPA) that shall also apply to nontraditional loans and become effective October 1, 2009 that:

1. Prohibition Against Failing to Consider Borrower's Ability to Repay - Prohibit creditors from extending a higher-priced mortgage or a HOEPA-covered loan without considering borrowers' ability to repay the loan based on the consumer's income or assets. Establishes a presumption of compliance with requirement where a creditor satisfies three requirements: (1) verifies and documents repayment ability of borrower; (2) determines repayment ability using the fully indexed rate and fully amortizing payment, except in certain circumstances, and considering other mortgage-related obligations such as property taxes and homeowners insurance; and (3) assesses the consumer's repayment ability using either ratio of the consumer's total debt obligation to income (DTI) or income the consumer will have after paying debt obligations. Does not

prescribe particular thresholds for the DTI or the residual income ratio.

2. Prohibition Against Failing to Verify Income - Prohibits creditor from relying on amounts of income (except for expected income) or assets to assess repayment ability for higher-priced loan or HOEPA-covered loan secured by consumer's principal dwelling unless the creditor verifies the amounts. Authorizes creditor to rely on W-2 forms, tax returns, payroll receipts, financial records or any other document providing reasonably reliable evidence of income, except a statement only from the consumer.

3. Prohibition Against Certain Prepayment Penalties - Prohibits prepayment penalties for any higher-priced loan or HOEPA-covered loan where payments can change during the four-year period following loan consummation. For other higher-priced loans, where payments do not change for four years, prohibits prepayment penalties exceeding two years from loan consummation or applicable to refinancing by creditor or its affiliate.

4. Requirement for Escrow Accounts - Requires creditors to establish escrow account for property taxes and homeowners insurance for at least one year. Servicer maintains the authority to continue or discontinue escrowing after required time. MIRA also provides FMRA authority to eliminate the requirement on servicer in case of emergency, such as loss of credit lines to advance taxes and insurance (T&I) payments.

B. Enacting into legislation the requirements for <u>all</u> closed-end loans promulgated in regulation by the Federal Reserve under HOEPA, with additions from H.R. 3915, as well as the mortgage broker contract provisions that were proposed by the Federal Reserve Board but not finalized, as follows:

   1. Appraisals – In order to regularize and protect against misconduct in the appraisal process, MIRA shall contain the following:

      a. Prohibition Against Coercing or Otherwise Pressuring Appraisers – Prohibits creditors, mortgage brokers, real estate brokers, or anyone else interested in the transaction and their agents and affiliates from coercing, extorting, colluding, inducing, bribing, intimidating, pressuring, or otherwise encouraging an appraiser to misstate or misrepresent a dwelling's value, for all closed-end residential loans. MIRA also prohibits a creditor from extending credit if the creditor knew of a violation, e.g., that an appraiser has been encouraged by creditor, mortgage broker or affiliate of either (including any of their employees) to misstate or misrepresent the principal dwelling's value, unless the creditor acts with reasonable diligence to determine that the appraisal was accurate or extends credit based on a separate appraisal untainted by coercion.

b. Prohibition Against Appraiser Misconduct – No appraiser conducting an appraisal may have a direct or indirect interest, financial or otherwise, in the property or transaction involving the appraisal.

c. Require FMRA to prescribe regulations and guidelines to:

    i. Implement the foregoing prohibitions in "a." and "b." above, including detailing conduct which is permissible and impermissible under each section, combining the guidance in the Board's final HOEPA rule and H.R. 3915;

    ii. Prohibit other practices which are unfair or deceptive in the appraisal process, including establishing reasonable safeguards against flipping and to otherwise ensure adequate and independent appraisals; and

    iii. Permit mortgage lenders to establish procedures including appropriate organizational structures to allow them to order appraisals or to engage the services of in-house appraisal staff for the purpose of attaining an independent and accurate appraisal, provided adequate safeguards, to be set by the Appraisal Standards Board to ensure that the ordering and operations of the lender are consistent with and do not violate the prohibitions of this section.

d. Establish penalties for violations of appraisal requirements.

e. Establish an Appraisal Oversight Board of federal and state regulatory officials to monitor appraisal practices and abuses and advise FMRA on the development of rules and guidance.

2. Assigns the Government Accountability Office (GAO) responsibility to study the appraisal process and standards for appraisers in each of the states and the District of Columbia, to recommend whether uniform national standards and a national mortgage fraud database are warranted for appraisers similar to the standards for loan originators, and to report to the Congress and FMRA on this subject and other improvements to the appraisal process within one year.

3. Prohibitions Against Certain Servicing Practices – Prohibits certain practices by servicers of closed-end consumer credit transactions secured by consumer's principal dwelling, including: (i) failing to credit a consumer's full periodic payment as of the date received, but creditors are not required to credit partial payments, and whether a payment is a full or partial payment is governed by the loan agreement or promissory note; (ii) imposing a late fee or delinquency charge where the only basis is consumer's failure to include in a current payment delinquency charge imposed on earlier payments; and (iii) failing to provide an accurate payoff statement within reasonable time after request.

   In addition, MIRA includes several provisions to facilitate servicing which are to be implemented by FMRA, including:

   a. Amend RESPA to allow FMRA to establish standards for forced placed hazard and flood insurance including proper notice and refunds when duplicative insurance is in place; and

   b. Amend RESPA to decrease the time to respond to valid qualified written requests but also provide 30-day extension upon notification to the borrower that more time is needed to research the request.

4. MIRA includes a safe harbor to facilitate improved servicing, which is to be implemented by FMRA. The safe harbor would:

   a. Help servicers implement strong streamlined modification programs using either a FDIC-style program, their own variants or the standards issued by the government pursuant to the Making Home Affordable Plan;

b. Provide an official mechanism for a review of alternatives to or variations of the FDIC program, and allows them to be deemed within the safe harbor;

c. Standardize the net present value (NPV) test and allows servicers to modify a loan if the NPV of a loan modification is greater than the NPV of foreclosure (i.e., there is no requirement to maximize the investor return on each individual loan modification);

d. Provide a specific indemnification for losses to a securitization vehicle or investor regarding loan modifications authorized by this Section as long as the servicer acts in good faith in accordance with this Section;

e. Mitigate the risk of constitutional challenges by creating a right of recovery through the Troubled Assets Relief Program (TARP) for securitization vehicles and investors if they can show that a servicer's streamlined modification program has injured them and the safe harbor has resulted in a taking;

f. Set a workable standard of proof for the investor to prove that a streamlined modification program has damaged them; and

g. Allow removal of actions to federal court.

5. *The following provision, as indicated, was proposed but not finalized by Federal Reserve Board.* Prohibits YSPs Unless Written Agreement – Prohibits creditor from directly or indirectly paying the mortgage broker unless the broker enters into a written agreement with the consumer that includes a disclosure to the consumer of the broker's total compensation that the broker will receive and retain from all sources, that the consumer will pay the entire compensation even if all or part is paid directly by the creditor, and that a creditor's payment to a broker can influence the broker to offer loan terms or products that are not in the consumer's interest or are not the most favorable the consumer could obtain. Also, prohibits broker from exceeding the compensation in the agreement.

6. *Amends advertising rules for both open-end home equity plans and closed-end mortgages including applying "clear and*

conspicuous" standard as was provided under the Board's HOEPA rules. Requires:

a. Whenever rate or payment is included in advertisement for closed-end or open-end credit secured by dwelling, all rates or payments that will apply over term of loan must be disclosed with equal prominence and in close proximity to advertised rate or payment; and

b. For closed-end mortgages, no longer allows advertisement of any interest rate lower than rate at which interest is accruing on annual basis. Also, for closed-end mortgage loans, prohibits: (a) advertising fixed-rate or payments when rate or payments are fixed only for limited period of time rather than full loan term; (b) comparing an actual or hypothetical consumer's current rate or payment to advertised loan unless the advertisement states rate or payments over the full term of the advertised loan; (c) advertising loan products as "government" or "government-sponsored" or otherwise government endorsed loan programs when they are not; (d) prominently displaying the name of a consumer's current lender unless the advertisement also discloses that the advertising lender is not affiliated with current lender; (e) advertising claims of debt elimination if product advertised merely replaces one debt obligation with another; (f) advertising that creates false impression that mortgage broker or lender has fiduciary relationship with consumer; and (g) foreign language advertisements in which certain information such as teaser rate is provided in foreign language and other disclosures only in English.

7. Additional Standards from H.R. 3915 are to be included in the UNMS, with some revisions, as follows:

   a. Duty of Care – Requires all loan originators including loan officers for mortgage lenders (lender loan officers) and loan officers for mortgage brokers (mortgage broker loan officers): (1) comply with all licensing and registration requirements; (2) present the consumer with a choice of loan products for which the consumer likely qualifies available from that lender, and which may be appropriate to the consumer's existing circumstances, based on information known by or obtained by the originator; and (3) make full and timely disclosures to each consumer of (a) comparative costs and benefits of each loan product offered or discussed and (b) whether the originator is or is not acting as an agent for the consumer. The duty of care would also require that: (4) the mortgage broker loan officer provide the borrower a disclosure of the mortgage broker's total compensation including any amounts that the broker may receive from the lender based on a higher rate or the terms of the loan; and (5) a consumer must affirmatively, opt-in, in writing *prior to closing*, to a nontraditional mortgage product after the lender's loan officer or mortgage broker discloses the costs and benefits of the loan to the borrower, also in writing.

b. Anti-Steering – All mortgage brokers, for all transactions are prohibited from receiving any incentive compensation (including yield spread premiums or equivalent compensation) that is based on or varies with the terms other than the amount of principal of any loan unless they enter into an agreement with the consumer that they are receiving such compensation and the amount of such compensation in accordance with the provisions of this Act. This restriction does not limit or affect the ability of a mortgage originator to sell residential mortgage loans to subsequent purchasers.

c. Effect of Foreclosure on Preexisting Lease – A successor to a foreclosed property shall take the property subject to the rights of a bona fide tenant (not the mortgagor) under a lease entered into before the date of the notice of foreclosure for 30 days after the date of a foreclosure, as long as the tenant receives notice from the servicer at the time the foreclosure is instituted stating that the property has entered the foreclosure process and that the tenant must vacate the property no later than 30 days after the foreclosure is complete, unless the successor waives the requirement.

d. Negative Amortization – Prohibited unless the creditor provides a complete disclosure to the consumer.

8. HOEPA High Cost Mortgages – Note: *MIRA does not include a third trigger for High Cost Mortgages in H.R. 3915 of a prepayment penalty for more than 36 months. The Federal Reserve Board rules are more restrictive for higher priced loans limiting prepayment penalties to two years or prohibiting them*

entirely for some adjustable loans. Would amend HOEPA in several ways, including expanding its coverage to purchase loans.

9. Servicing – Requires the Director in consultation with CSFR to promulgate rules governing mortgage servicers that ensure that servicing companies are competent and qualified and that servicers institute training, procedures and standards to assure borrowers are treated fairly and competently, including the Board's servicing requirements at VI, b, 3 above and procedures for quick response and appropriate action when borrowers are delinquent and facing foreclosure. Also requires the Director to establish a new centralized servicing database, in lieu of existing inconsistent state and federal systems, which includes data on borrower requests for workouts and their disposition.

10. Miranda Warning – To improve mortgage servicing interactions with borrowers, amends the Fair Debt Collection Practices Act (FDCPA) which requires a debt collector to provide a debtor with a "Miranda" warning upon initial contact with debtor, and a shorter "mini-Miranda" in all subsequent contacts (written and oral) for the life of the loan.

    a. Unfortunately, mortgage servicers are considered "debt collectors" in the vast majority of cases and must state that they are attempting to collect a debt and that any information will be used for that purpose. This statement is misleading when applied to loss mitigation activity and serves to chill a borrower's willingness to work with the servicer to provide information required to execute loss mitigation.

    b. MIRA amends the FDCPA to exclude mortgage servicers of first lien residential mortgages from the Miranda notice requirement. All of the other consumer protection under FDCPA would continue to apply. Thus, a mortgage servicer who, whether by assignment, sale or transfer, becomes the person responsible for servicing mortgage loans secured by first liens, including loans that were in default at the time such person became responsible for the servicing, shall be exempt from the FDCPA Miranda requirements in connection with the collection of any debt arising from such a defaulted related mortgage loan.

VII. Additions to Standards - Requires the Director in consultation with CSFR to meet at least quarterly to supplement the UNMS as necessary, to promulgate such changes by regulation and report to Congress on the state of mortgage lending, the need for additional changes and their disposition by the Director, annually.

VIII. **Regulatory Responsibilities -** Requires the Director to apply the UNMS to regulate the mortgage lending activities of all federally and state regulated lending institutions in cooperation with their regulators, to regulate all activities of independent lenders and mortgage brokers including establishing uniform licensing and registry requirements for such entities, in consultation with CSFR, consistent with the requirements of the S.A.F.E. Act; and to work in partnership with federal and state regulatory and enforcement officials to examine, review and enforce the UNMS. Specifically, the Act:

A. Establishes a new uniform federal regulatory structure for mortgage lending under which the FMRA would:

1. Regulate all mortgage lending activities of all state and federally regulated lenders through the UNMS; such regulators would retain responsibility to regulate all other activities of such institutions and examine, review and enforce the UNMS; and

2. Promulgate rules in consultation with CSFR governing mortgage servicers that ensure that servicing companies are competent and qualified and that servicers institute training, procedures and standards to assure borrowers are treated fairly and competently, including the Federal Reserve Board's servicing requirements at VI, b, 3 above and procedures for quick response and appropriate action when borrowers are delinquent and facing foreclosure.

B. Requires FMRA to directly regulate all non-depository mortgage lenders and mortgage brokers and mortgage bankers and work cooperatively with current federal and state regulators to review, examine and enforce the UNMS established under this Act for those entities.

1. In carrying out this function, FMRA is required, within one year of enactment, to establish uniform nationwide licensing and registry requirements to apply to all independent mortgage bankers and mortgage brokers which are not federally regulated. Such rules should provide rigorous requirements to ensure competent and qualified lenders and brokers and maximum competition across state lines to lower costs to consumers. *Note: The Act (below) would amend the S.A.F.E. Act which sets minimum requirements for licensing of mortgage originators and requires the states to enact laws specifying licensing and registry requirements for non-federally regulated originators within one year. The Act would*

transfer responsibility for establishing licensing and registry requirements from the states to the FMRA;

2. Also in carrying out this function, such rules should appropriately differentiate between the two types of entities where necessary considering their differing functions and the differing policy concerns which the respective industries present. The rules should require that bankers and brokers at the time of first licensure and on a continuing basis shall:

   a. Meet appropriate educational, testing and character requirements;

      1. Meet net worth and bonding requirements-

         i. For mortgage bankers – the corporate net worth requirement shall be at least $500,000, plus $50,000 for each branch office with a maximum limit of $1 million, as evaluated by audited statements and the bonding requirement shall be a suitable amount to protect borrowers; and

         ii. For mortgage brokers the corporate net worth requirements shall be at least $150,000, plus $25,000 for each branch office up to the requirement for a full eagle from FHA, and the bonding requirement shall be at least $75,000.

IX. Penalties/Remedies - Clarifies Penalties and Establishes New Penalties

A. Consumers who bring action against creditors for violations may seek:

1. Actual damages;

2. Statutory damages in an individual action of up to $2,000 or, in a class action, total statutory damages for the class of up to $500,000 or one percent of the creditor's net worth, whichever is less;

3. Special statutory damages equal to the sum of all finance charges and fees paid by the consumer; and court costs and attorney fees;

4. Refinance mortgages subject to the right of rescission. An action for rescission, costs and attorney's fees may be brought against a lender for violation of the Ability to Repay requirements for a higher priced mortgage;

5. In all cases where a claim for rescission and a claim for damages is made, a creditor has a right to cure non-compliance in lieu of rescission if no later than 90 days after receipt of notification of the consumer's claim, the creditor provides a cure at no cost to the consumer;

6. Definition of Cure – Cure for a violation of the ability to repay requirement means modification or refinancing of the loan at no cost to the consumer to provide terms that would have satisfied the ability to repay requirement.

B. Limited Assignee Liability – An action for rescission and costs may be brought against an assignee or securitizer. Assignees and securitizers are protected from liability if no later than 90 days after notice from a consumer the assignee or securitizer provides a cure or the assignee or securitizer satisfies the following conditions:

1. Has a policy against buying loans other than qualified mortgages or higher cost mortgages meeting the requirements of the Act;

2. Has a policy intended to verify assignor or seller compliance with representations and warranties that the seller is not selling any loan that is not a qualified mortgage or a higher cost mortgage meeting the requirements of the Act;

3. Satisfies 2 above, by exercising due diligence per regulations issued by the Securities and Exchange Commission and banking regulators including through adequate sampling procedures; and has a contract with the assignee which represents and warrants that the seller or assignor is not selling loans which are not higher cost loans meeting the requirements of this Act.

C. New penalties for disclosure violations. Amends Section 4 and 5, of RESPA, 12 USC 2603 and 12 USC 2604, to provide penalties for:

1. Failing to provide a consumer the disclosures under 4 and 5 as applicable;
2. Failing to disclose the costs that the borrower is estimated to receive or is charged at closing on the HUD-1;
3. Charging the consumer at closing an amount 10 percent greater than the total cost of lender, mortgage broker, title and other third party fees that was estimated at the time of application, provided the borrower qualifies for the loan in final underwriting and does not request a different loan;

4. Charging a consumer more than the maximum amount of mortgage broker compensation disclosed; and
5. Wrongfully advising the consumer of the broker's function in the transaction; i.e., that he will shop for a borrower when he is not in fact an agent of the borrower. This provision may include a criminal penalty.

D. MBA supports civil money penalties and private remedies instead of rescission or refund of finance charges for minor infractions and infractions that trigger from on-going or periodic servicing or lending responsibilities.

X. **Enforcement/Examination Authorities -** Authorizes FMRA, other federal agencies, state agencies and private parties to enforce the UNMS and to interact with federal and state banking regulators to review, examine and enforce UNMS concerning all mortgage lending operations.

XI. **Financial Literacy and Counseling -** Assigns the Director national responsibility of operating a national financial literacy and counseling program targeted at understanding credit and mortgages, including requiring mandatory counseling for certain mortgage products. The Director shall, with the advice of the CSFR and interested stakeholders:

1. Develop a curriculum for a national financial literacy program in conjunction with the CSFR for use by educational institutions at the elementary, middle school and secondary school levels;

2. Develop a comprehensive Web site to inform the public about the mortgage process and to compare the mortgage products available;

3. Establish and administer an assistance program to eligible recipients to develop counseling capacity;

4. Require, through rulemaking, mandatory counseling for mortgage products that present an increased risk of default, in the judgment of the Director. These products should include all reverse mortgages, and, as long as adequate counseling resources are available such that loan closings are not delayed, HOEPA highest priced and higher priced loans which could result in negative amortization made to first-time homebuyers.

XII. **Mortgage Fraud -** Authorizes $31,250,000 from 2009 through 2013 for new employees at the Department of Justice dedicated to combat mortgage fraud, and $750,000 for the same period for additional funding for a mortgage fraud interagency task force.

XIII. Initial Funding - Authorizes start-up funds of $____ for establishment of the FMRA and its first two years of operations including the costs of consumer testing, financial literacy, counseling and anti-fraud activities.

XIV. Resources for Regulation/Sharing Funds With States – Beyond start up period, authorizes FMRA to charge a reasonable assessment on each entity regulated by the FMRA to defray the costs of regulation. States would receive licensure and registry fees and would share in assessments on regulated entities for examination and enforcement to extent appropriate to avoid duplicate charges on regulated entities.

XV. Improving Transparency – Requires HUD and the Federal Reserve to work together in consultation with the Director and CSFR to develop a simplified, combined RESPA/TILA disclosure that shall be uniform and used nationally. HUD would be directed to withdraw the pending RESPA rule prescribing a new GFE and HUD-1 and coordinate its efforts with the TILA reform efforts of the Federal Reserve Board. These joint efforts of the Federal Reserve Board and HUD should be placed on an aggressive timetable established by Congress which would implement the new disclosures in a coordinated manner that would avoid confusion and reduce consumer costs. Specifically, MIRA requires:

A. Combined, coordinated and simplified RESPA and TILA Good Faith Estimate (GFE) disclosures, combined, coordinated and simplified HUD-1 and final TILA disclosures as well as accompanying consumer information meeting the requirements of TILA and RESPA that would require that disclosures be given at the same time and in accordance with the Mortgage Disclosure Improvement Act (enacted July 2008).

B. The combined RESPA and TILA GFE would include:

1. A uniform one-page, box-type summary of the estimated costs and terms of each individual mortgage loan offer that would include:

   i. the estimated loan amount; note rate and Annual Percentage Rate (APR); the total settlement costs;
   ii. whether the loan is adjustable and, if so, how frequently;
   iii. the note rate and APR for the loan;
   iv. the estimated mortgage payment of principal and interest and estimated amounts for taxes and insurance (Estimated PITI);
   v. whether the loan does or does not have a prepayment penalty with its duration and amount;
   vi. whether the loan has a balloon payment with its timing and amount;

vii. whether the lender automatically escrows taxes and insurance;
viii. whether private mortgage insurance or a second mortgage is needed with its cost(s); and
ix. which, if any, costs are or are not guaranteed to come within 10 percent of the final settlement costs subject to approval of the borrower and property securing the mortgage.

2. Group key settlement costs into major categories based on which service provider receives them, discloses the total cost for each category and then totals them as a total estimated cost. These categories would include: fees paid to the mortgage originator, lender or broker, fees paid for title insurance and closing services, fees paid to other third parties and government charges and not detail the sums for sub-costs within cost categories, except government charges, on the GFE or the HUD-1;

3. Include the maximum amount of compensation the mortgage broker will receive in the transaction;

4. Arrive at total estimated settlement costs: and monthly payment(s);

5. Advise the borrower of possible payment shock, balloon payments, prepayment penalties, the cost of a no-doc or low-doc loan and the borrower's responsibility for taxes and insurance and mandatory homeowners' association dues or condominium fees, where applicable; and such other information regarding the transaction as the Director deems necessary for borrowers.

C. A new standard, combined, brief plain language home purchase and mortgage financing handbook drawing from the current Special Information Booklet and the Consumer Handbook on Adjustable Rate Mortgages (CHARM) and other materials, to provide consumers generic information for both home purchase and mortgage refinance transactions that, among other things:

1. Clearly describes the key terms and costs of homeownership including the down payment, monthly payments, settlement costs, taxes and insurance and other monthly charges;

2. Advises consumers of the importance of credit history, down payment and adequate reserves in obtaining a lower cost mortgage and maintaining homeownership;

3. Advises consumers of the risks and benefits of various mortgage products including providing information on payment adjustments, balloon payments, prepayment penalties, the need to pay taxes and insurance and the costs of no-documentation and low-documentation loans;

4. Advises consumers of the roles and responsibilities of different players in the mortgage process including the differences between mortgage lenders and mortgage brokers, that only those mortgage brokers which identify themselves as such are borrowers' agents and the fact that all mortgage originators will receive additional income if a borrower agrees on a higher mortgage rate.

D. A standard agreement intended to replace disparate state disclosures, regarding the cost and function of the mortgage broker in the transaction that: notifies a consumer of the maximum amount the mortgage broker will receive in the transaction; whether a broker is or is not acting as an agent for the borrower; and whether the mortgage broker may increase its commission based on the borrower's agreement to an increased interest rate. This form will be provided by mortgage brokers in addition to the GFE disclosure.

E. A new combined HUD-1 and final TILA disclosure, for each mortgage loan covered by RESPA and TILA that easily corresponds to a new standardized GFE/TILA form so that a borrower can readily compare both documents including both the estimated and final settlement costs. Note: The current HUD-1, and even the one recently promulgated by HUD, is still not comparable to the GFE. The consumer, therefore, is not able to make an apples-to-apples comparison of the fees and terms at application and at settlement.

F. New forms to facilitate borrower understanding of the mortgage process and lender, broker and their loan officers' duty of care for consumers: (1) to provide information regarding their circumstances including the consumer's risk appetite to assist the loan officer or mortgage broker in deciding which loan products should be presented to the consumer; (2) to affirmatively opt-in to a nontraditional mortgage product following a disclosure explaining the option, including the risks and benefits of an adjustable loan; and (3) to disclose the amount of a mortgage broker's compensation.

G. New forms to provide reasonable notice to a borrower prior to reset of an adjustable rate mortgage

XVI. Preemption and Revisions to Federal Laws - Preempts contrary state laws and amends several federal laws as follows:

A. Amends the S.A.F.E. Act to transfer responsibilities for establishing uniform national mortgage licensing and registry standards for originators of regulated entities from the states to FMRA;

B. Amends TILA and RESPA to:

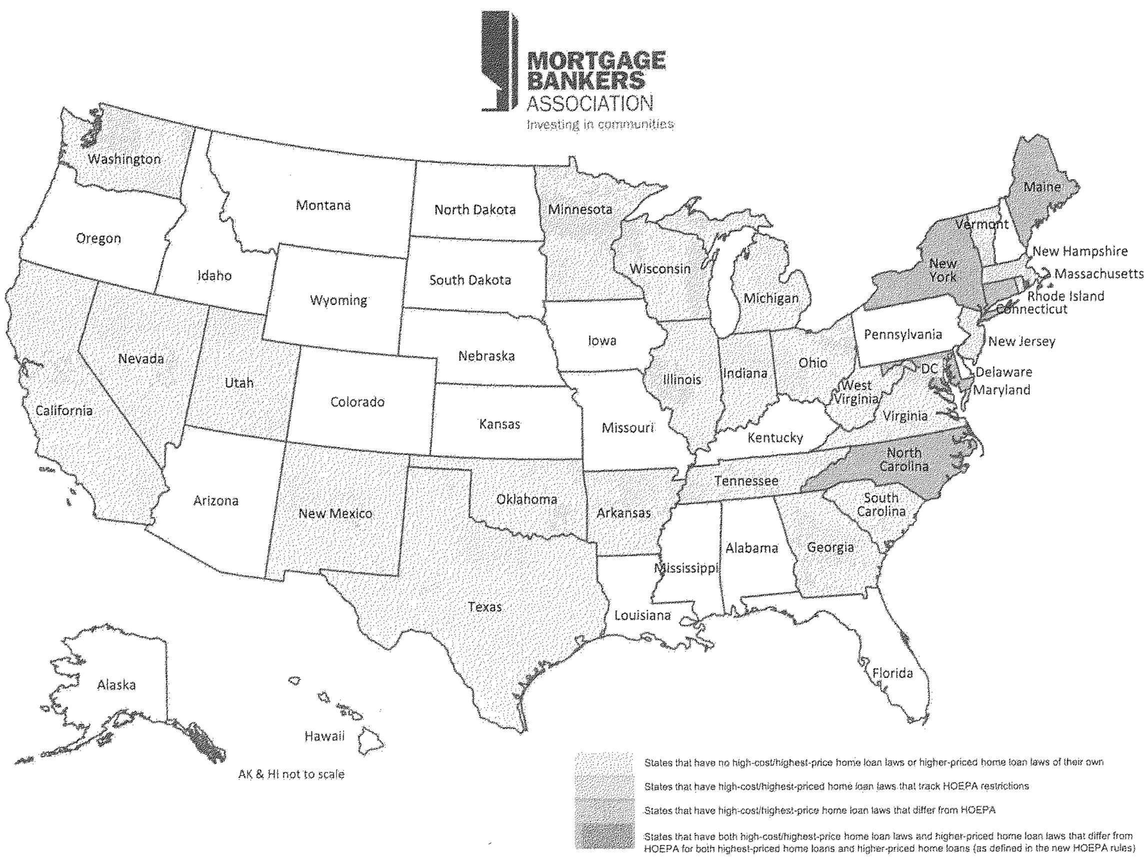
   1. Require HUD and the Federal Reserve Board to work together on a single set of uniform disclosures and accompanying borrower information for all mortgage transactions nationwide and for HUD to withdraw its pending rule until such a single set of disclosures can be issued;

   2. Make borrower remedies compatible without establishing a new right of rescission under RESPA; and

   3. Preempt state disclosures of the same information covered by RESPA and TILA.

C. Amends TILA to provide that all settlement charges other than government charges must be included in the computation of the finance charge and the Annual Percentage Rate (APR) for the loan. The current APR is not a useful shopping tool since major settlement costs are not included in its calculation. An all-in APR would make the APR much more useful to borrowers for such purpose.

D. Maintains the current preemption for federally regulated financial institutions.


MORTGAGE
BANKERS
ASSOCIATION
Investing in communities
Washington
Oregon
California
Idaho
Nevada
Montana
Wyoming
Utah
Arizona
Colorado
New Mexico
North Dakota
South Dakota
Nebraska
Kansas
Oklahoma
Texas
Minnesota
Iowa
Missouri
Arkansas
Louisiana
Wisconsin
Illinois
Michigan
Indiana
Ohio
Kentucky
Tennessee
Mississippi
Alabama
Georgia
Florida
South Carolina
North Carolina
Virginia
West Virginia
DC
Pennsylvania
New York
Vermont
Maine
New Hampshire
Massachusetts
Rhode Island
Connecticut
New Jersey
Delaware
Maryland
Alaska
Hawaii
AK & HI not to scale
States that have no high-cost/highest-price home loan laws or higher-priced home loan laws of their own
States that have high-cost/highest-priced home loan laws that track HOEPA restrictions
States that have high-cost/highest-price home loan laws that differ from HOEPA
States that have both high-cost/highest-price home loan laws and higher-priced home loan laws that differ from HOEPA for both highest-priced home loans and higher-priced home loans (as defined in the new HOEPA rules)

NAFCU
National Association of Federal Credit Unions
3138 10th Street North • Arlington, Virginia • 22201-2149
703-522-4770 • 800-336-4644 • 703-522-0594

B. Dan Berger
Executive Vice President
Government Affairs

September 29, 2009

The Honorable Barney Frank
Chairman
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Spencer Bachus
Ranking Member
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Dear Chairman Frank and Ranking Member Bachus:

I am writing on behalf of the National Association of Federal Credit Unions (NAFCU), the only trade organization exclusively representing the interests of our nation's federal credit unions, regarding tomorrow's Financial Services Committee hearing, entitled "Perspectives on the Consumer Financial Protection Agency Act."

NAFCU appreciates the modest improvements that were made to H.R. 3126, the *Consumer Financial Protection Agency Act of 2009* in the Discussion Draft released by Chairman Frank on September 25th, 2009. We believe that these changes represent progress and take important steps forward in addressing credit union concerns. We appreciate your efforts in seeking to deal with the financial regulatory problems that contributed to the economic crisis, while still taking our views into account.

In spite of the changes to the CFPA Act proposed by Chairman Frank's Discussion Draft, NAFCU maintains several important concerns about this legislation. While we continue to support the creation of a Consumer Financial Protection Agency (CFPA) for those who have been previously unregulated, we do not believe that its authority should extend to regulated, depository institutions, such as credit unions. As credit unions would be the only not-for-profits subject to the full oversight of the CFPA, we could also support an exemption for all not-for-profit organizations that operate in the financial services marketplace. As you are aware, credit unions were not the cause of the current economic crisis and made very few subprime loans. Credit unions are more heavily regulated than other financial institutions, and there are many consumer protections already built into the Federal Credit Union Act (such as a usury ceiling and a prohibition on pre-payment penalties). Furthermore, giving the new agency authority to regulate and examine credit unions that are already regulated by the NCUA would add an unnecessary regulatory layer and increase compliance costs for credit unions. These additional burdens will surely lead to diminished services to credit union members. We are also concerned about the lack of federal preemption in the draft legislation. With strengthened federal consumer protection, we believe that some level of federal preemption is necessary.

E-mail: dberger@nafcu.org • **Web site:** www.nafcu.org

The Honorable Barney Frank
The Honorable Spencer Bachus
September 29, 2009
Page 2 of 2

At the same time, we recognize that more should be done to help consumers and we have offered an alternative approach that we could support. We would propose that, rather than extending broad CFPA authority to federally-insured depository institutions such as credit unions, each functional regulator of federally-insured depository institutions have a new or strengthened office on consumer affairs established. Such an office should report directly to the Presidential appointees at the regulator and be responsible for making sure that the regulator is looking out for consumer concerns in writing rules, supervising and examining institutions compliance, and administratively enforcing violations. Consumer protection offices at the functional regulators could consult with the CFPA and work to tailor model regulations proposed by the CFPA to their institutions. Such an approach will ensure that those regulating the consumer issues at financial institutions have knowledge of the institutions they are examining. This is particularly important to credit unions, as they are regulated and structured differently than others in financial services, and we believe that it is important that any regulator examining credit unions understand their unique nature. We believe that such an approach would strengthen consumer protection while not adding unnecessary regulatory burdens on our nation's financial institutions.

We are also concerned that the Discussion Draft continues to include language granting the CFPA the authority to regulate mortgage, title and credit insurance. Additionally, the draft language provides the new agency with broad authority to determine what does and does not constitute "the business of insurance." Any financial activity the agency determines is not part of the "business of insurance" would fall under its jurisdiction. We believe that the CFPA should be narrowly focused on traditional financial products and should not be tasked with also regulating insurance products. We would note that insurance is not an extension of credit, but rather protects against risk of loss. The fact that some insurance protection covers risks surrounding a credit transaction does not alter the essence of the insurance product. Given this distinction, we believe that mortgage, title and credit insurance should not be included within the CFPA mandate.

We thank you for the opportunity to share our thoughts on this important issue. We look forward to continue working with you and the Committee on the issue of regulatory reform so that the best possible legislative solution can be achieved.

If we can answer any questions or provide you with further information on this matter, please do not hesitate to contact myself or NAFCU's Director of Legislative Affairs, Brad Thaler, at 703-522-4770.

Sincerely,

B. Dan Berger
Executive Vice President, Government Affairs

cc: Members of the House Financial Services Committee

NETWORK BRANDED
PREPAID CARD ASSOCIATION

110 Chestnut Ridge Rd.
Suite 111
Montvale, NJ 07645-1706
Ph: 201.746.0725
Fax: 888.845.8594
www.nbpca.org

September 29, 2009

The Honorable Luis Gutierrez
Chairman
Subcommittee on Financial Institutions and Consumer Credit
House Financial Services Committee
2129 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Gutierrez:

I want to thank you for taking the time last week to visit with members of the Network Branded Prepaid Card Association ("NBPCA"),[1] during our meeting in the Capitol Visitor's Center. Having the opportunity to engage in an informal dialogue with members of Congress has proven to be invaluable for us as we work to educate them about our industry and the consumers we serve. At that time, we expressed to you our concerns with certain provisions of H.R. 3126, the Consumer Financial Protection Agency Act of 2009 ("CPFA Act") that threatens the viability of prepaid card products and could eliminate a key tool of financial inclusion for the more than 40 million U.S. consumers who don't have access to the mainstream banking system and rely on prepaid cards.

Specifically, Section 101(12) of the CFPA Act, which defines deposit-taking activity, provides:

> "[f]or the purposes of this title, the Agency may determine that the **term 'deposit-taking activity' includes** the receipt of money or its equivalent in connection with **the sale or issuance of any payment instrument or stored value product** or service." (Emphasis added.)

---

[1] **About the NBPCA**
The Network Branded Prepaid Card Association (NBPCA) is a nonprofit, inter-industry trade association that supports the growth and success of network branded prepaid cards and represents the common interests of the many players in this new and rapidly growing payment category. The NBPCA's members include financial institutions, card organizations, processors, program managers, marketing and incentive companies, card distributors and law firms. The NBPCA's Working Groups drive the activities of the Association for its more than 42 members. For additional information, visit www.NBPCA.org.

Currently, there are approximately 200,000 non-bank locations across the United States where consumers can either purchase a prepaid card or load funds to the card. If the Consumer Financial Protection Agency ("CFPA") deems selling/issuing prepaid cards as "deposit taking," this will mean that only banks or bank branches can sell or load such products, inevitably decreasing or eliminating access to these important products for those that need them most. By effectively prohibiting the sale or loading of prepaid cards at non-bank and retail locations, this new law would create a serious impediment to financial inclusion for the millions of unbanked consumers who have come to rely upon prepaid cards for carrying out their day-to-day transactions.

Over 100 million network branded prepaid cards have been used by consumers, whether in the form of a gift card, government benefit card, rebate/incentive card, payroll card, general purpose reloadable card or other prepaid product. These products offer a convenient, secure option for millions of consumers. In some applications, these cards are an alternative for consumers who may not have a checking account, debit or credit card, but like the rest of us, need a mechanism for daily living transactions in this increasingly card-based economy. These consumers rely on network branded prepaid cards which they access conveniently through their local grocery stores, drug stores, convenience stores, employers or schools.

For many consumers, prepaid products in their many and varied forms have become a necessary part of day-to-day life in the United States. They offer convenience, security and empowerment, while promoting financial responsibility. This is especially true among the young, just learning to manage their funds responsibly, and the underbanked/financially underserved segments of society that do not qualify for a traditional bank account or payment product or are not comfortable in a banking environment.

The detrimental impact of this language to the millions of consumers who rely on these products is so severe that we are strongly urging you to prevent such an unintended consequence and clarify in the legislation that the sale/issuance of prepaid cards does *not* constitute deposit-taking. We suggest that the proposed language shown above be deleted and replaced with the following:

> "[f]or the purposes of this title, the Agency **shall confirm** that the term 'deposit-taking activity' **would exclude** the receipt of money or its equivalent in connection with the sale or issuance of any payment instrument or stored value product or service." (Emphasis added.)

By doing this, Congress will ensure that banks can continue to distribute and load prepaid card products through non-bank locations, and can avoid creating a serious impediment to financial inclusion for millions of U.S. consumers.

The NBPCA appreciates your leadership as you work through very difficult issues related to regulatory reform of the financial services industry. The NBPCA and its members stand ready to work with you and your staff as you move forward through this process.

Sincerely,

Kirsten Trusko
President & Executive Director
Network Branded Prepaid Card Association

Professors of Consumer Law and Banking Law

A Communication From Academic Faculty
Who Teach Courses Related to Consumer Law and Banking Law
at American Law Schools

September 29, 2009

The Honorable Christopher J. Dodd
Chairman
Committee on Banking, Housing and Urban Affairs
United States Senate

The Honorable Barney Frank
Chairman
Financial Services Committee
United States House of Representatives

The Honorable Richard C. Shelby
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Spencer Bachus
Ranking Member
Financial Services Committee
United States House of Representatives

Via Facsimile

Dear Senators Dodd and Shelby
and Representatives Frank and Bachus,

Statement in Support of Legislation Creating a
Consumer Financial Protection Agency

As teachers and scholars in the fields related to consumer law and banking law who currently teach at American law schools in such states as Alabama, Arizona, California, Connecticut, Florida, Georgia, Illinois, Indiana, Iowa, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Ohio, Oregon, Nebraska, North Carolina, Nevada, New Jersey, New York, Pennsylvania, South Carolina, Tennessee, Texas, Utah, Washington, Wisconsin, and Wyoming as well as Washington D.C., we strongly support legislation to create an independent Consumer Financial Protection Agency ("CFPA"). Our review of the regulatory approaches at the existing agencies, whose jurisdiction includes but does not focus on consumer financial products, leads us to conclude that on balance they place a higher value on protecting the interest of financial product vendors who promote complex debt instruments using aggressive sales practices, than they do on protecting the interests of consumers in transparent, safe, and fair financial products.[1] An independent agency with consolidated authority and a consumer-oriented mission such as the one being considered by your committees is likely to improve public confidence in the safety and efficiency of the vast consumer financial products marketplace—a marketplace that includes complex and nonstandard mortgage instruments, promissory notes, installment sales agreements, credit cards, debit cards, Internet payment devices, and other devices, products, and services in the consumer financial system. It is a system vitally important to public welfare and economic recovery.[2]

The desirable improvements and consolidations proposed to be accomplished by this legislation include (1) a single place to concentrate federal rulemaking authority over consumer financial transactions joined with primary enforcement authority over them; (2) the power to restore banking federalism so as to better accommodate consumer interests;

[1] Scholarly literature that is critical of regulatory rulemaking and decisional outcomes in the area of consumer financial products includes: Peter A. Alces & Jason M. Hopkins, Carrying a Good Joke Too Far, 83 Chi.-Kent L. Rev. 879 (2008); Oren Bar-Gill and Elizabeth Warren, Making Credit Safer, 157 Penn. L. Rev. 1 (2008); Mark E. Budnitz, Commentary, Technology as the Driver of Payment System Rules: Will Consumers Be Provided Seatbelts and Air Bags?, 83 Chi.-Kent L. Rev. 909 (2008); Michael Barr, Banking the Poor, 21 Yale J. On Reg. 121 (2004); Steven F. Davidoff, Paradigm Shift: Federal Securities Regulation In The New Millennium, 2 Brook. J. Corp. Fin. & Com. L. 339 (2008); Diane Ellis, The Effect of Consumer Interest Rate Deregulation on Credit Card Volumes, Charge-Offs, and in the Personal Bankruptcy Rate, Bank Trends 98-05 (FDIC, Mar 1998); Kathleen C. Engel and Patricia A. McCoy, Turning A Blind Eye: Wall Street Finance of Predatory Lending, 75 Fordham L. Rev. 2039 (2007); William N. Eskridge, Jr., One Hundred Years of Ineptitude: The Need for Mortgage Rules Consonant with the Economic and Psychological Dynamics of the Home Sale and Loan Transaction, 70 Va. L. Rev. 1083 (1984); David A. Friedman, Reinventing Consumer Protection, 57 DePaul L.Rev. 45 (2007); Julia Patterson Forrester, Mortgaging the American Dream: A Critical Evaluation of the Federal Government's Promotion of Home Equity Financing, 69 Tul. L. Rev. 373 (1994); John Kiff & Paul Mills, Money for Nothing and Checks for Free: Recent Developments in U.S. Subprime Mortgage Markets, IMF Working Paper No 07/188 (2007); Adam Levitin, Hydraulic Regulation: Regulating Credit Markets Upstream, 26 Yale J. on Reg. 143 (2009); Cathy Lesser Mansfield, The Road to Subprime "HEL" Was Paved with Good Congressional Intentions: Usury Deregulation and the Subprime Home Equity Market, 51 S.C. L. Rev. 473, 555 (2000); Patricia McCoy, The Middle-Class Crunch: Rethinking Disclosure In A World Of Risk-Based Pricing, 44 Harv. J. On Legis. 123 (2007); Saule T. Omarova and Adam Feibelman, Risks, Rules, and Institutions: A Process for Reforming Financial Regulation, 39 U. Mem. L. Rev. 881 (2009); Christopher Lewis Peterson, Preemption, Agency Cost Theory, and Predatory Lending by Banking Agents: Are Federal Regulators Biting Off More Than They Can Chew?, 56 Am. U. L. Rev. 515 (2007); Christopher Lewis Peterson, Federalism and Predatory Lending: Unmasking the Deregulatory Agenda, 78 Temple L. Rev. 1 (2005); Elizabeth Renuart and Diane E. Thompson, The Truth, the Whole Truth, and Nothing But the Truth: Fulfilling the Promise of Truth in Lending, 25 Yale J. on Reg. 181 (2008); Ralph J. Rohner and Thomas A. Durkin, TILA "Finance" and "Other" Charges in Open-End Credit: The Cost-of-Credit Principle Applied to Charges for Optional Products or Services, 17 Loyola Consumer L Rep 137 (2005); Elizabeth R. Schlitz, The Amazing, Elastic, Ever-Expanding Exportation Doctrine and Its Effect on Predatory Lending Regulation, 88 Minn. L. Rev. 518 (2004); 31 Fordham Urb. L.J. 413, 471 (2004); Paul M. Schwartz, Where Do We Go From Here? The Battle Against Predatory Subprime Lending, 3 Brook. J. Corp. Fin. & Com. L. 213 (2008); Elizabeth Warren, Unsafe at Any Rate, 5 Democracy: A Journal of Ideas (Summer 2007).

[2] The proposed legislation excludes securities, see H. 3126, Sec. 122(f)(2).

(3) the authority to improve opportunities for consumers to enforce their rights; and (4) the ability to establish standards for fairness and honesty in agreements for financial products and services. These improvements intrinsically cannot be accomplished through the existing agency structures, or practically are not achievable through them. Several difficulties presented by the existing regime and which are addressed through the proposed changes are documented in the scholarly literature, which is illustrated below.

1. ***Exclusive rulemaking authority and primary enforcement authority.***[3] At critical moments of consumer confusion and vulnerability, regulators of financial institutions, including the Federal Reserve Bank, the Office of Thrift Supervision, and the Office of the Comptroller, have demonstrated unwillingness to expend resources to develop appropriate rules and guidelines and to police mortgage and credit instruments. The two-decades-long delay in effectively regulating credit card practices, despite many warnings from consumer groups, responsible lenders, and scholars, for example, is a well-documented and catastrophic lapse that continues to inflict serious financial injury.[4] Similarly, the Federal Reserve Board waited fourteen years to use the power Congress conferred upon it in 1994 to prohibit unfair or deceptive practices in mortgage lending;[5] had the Fed acted timely, the subprime crisis might have been less severe. As the sub-prime mortgage market exploded with unfamiliar and dangerous instruments, federal bank regulators failed to act decisively to improve the situation, under pressure from vendor constituencies that encouraged non-regulation. When regulators belatedly got

---

[3] Sec. 122 (d) and (e) of H. 3126 if enacted would provide: (d) EXCLUSIVE RULEMAKING AND EXAMINATION AUTHORITY- Notwithstanding any other provision of Federal law other than subsection (f), to the extent that a Federal law authorizes the Agency and another Federal agency to prescribe regulations, issue guidance, conduct examinations, or require reports under that law for purposes of assuring compliance with this title, any enumerated consumer law, the laws for which authorities were transferred under subtitles F and H, and any regulations prescribed under this title or pursuant to any such authority, the Agency shall have the exclusive authority to prescribe regulations, issue guidance, conduct examinations, require reports, or issue exemptions with regard to any person subject to that law. (e) (1) THE AGENCY TO HAVE PRIMARY ENFORCEMENT AUTHORITY- To the extent that a Federal law authorizes the Agency and another Federal agency to enforce that law, the Agency shall have primary authority to enforce that Federal law with respect to any person in accordance with this subsection.

[4] See, e.g., Rossman v. Fleet Bank Nat'l Ass'n, 280 F.3d 384 (2002); Norman I. Silber, Late Charges, Regular Billing, And Reasonable Consumers: A Rationale For A Late Payment Act, 83 Chi.-Kent L. Rev. 855 (2008); Oren Bar-Gill, Seduction by Plastic, 98 Nw. U L Rev 1373, 1420-21 (2004).

[5] See 15 U.S.C. § 1639(l)(2), enacted as part of HOEPA in 1994, which provides:

> The Board, by regulation or order, shall prohibit acts or practices in connection with--
>
> (A) mortgage loans that the Board finds to be unfair, deceptive, or designed to evade the provisions of this section; and
>
> (B) refinancing of mortgage loans that the Board finds to be associated with abusive lending practices, or that are otherwise not in the interest of the borrower

together in October 2006 to try to respond to widespread consumer difficulties in understanding nontraditional, hybrid mortgage products, the different agencies provided limited guidance but they could not jointly address hybrid instruments "because of the difficulty agreeing among themselves, and these instruments remained unregulated."[6] By the time bank regulators did get around to hybrid products, "it was too late to prevent the subprime crisis which had already begun."[7] Reports that regulators view consumer protection as a backwater are particularly troubling and emphasize that the important goal of consumer protection will not receive adequate attention under the current regulatory structure.[8]

2. *The authority to restore banking federalism to accommodate consumer interests.*[9] The traditional police power of states to regulate commercial practices in the interest of their citizens has been undermined by federal banking regulators, whose assertion of preemption has worked to the advantage of financial institutions at the expense of effective consumer protection by states and localities. Two developments are illustrative. In 1978, the Supreme Court upheld regulations of the Comptroller of the Currency that helped to deregulate the credit card business by interpreting the National Bank Act as preempting states from enforcement of their own usury laws.[10] Almost twenty years later, in the 1996 decision *Smiley v. Citibank, S.D.*, N.A., the Court unanimously upheld the interpretation of the Comptroller of Currency that late payment fees were deemed "interest" for the purposes of preempting state regulation of late fee amounts.[11] Both opinions interpreted the National Bank Act of 1864, 12 U.S.C. § 85, and both deferred to the Comptroller's analysis of that Civil War statute - ambiguous at best - to block state regulation. Subsequent federal decisions have accepted the principle of deference to the

[6] WookBai Kim, Challenging The Roots Of The Subprime Mortgage Crisis: The OCC's Operating Subsidiaries Regulations and Watters v. Wachovia Bank, 21 Loy. Consumer L. Rev. 278, 289 (citing Interagency Guidance on Nontraditional Mortgage Product Risks, 71 Fed. Reg. 58,609 (Oct. 4, 2006); Statement on Subprime Mortgage Lending, 72 Fed. Reg. 37,569 (July 10, 2007); see also Laurie S. Goodman, Shumin Li, Douglas J. Lucas, Thomas A. Zimmerman & Frank J. Fabozzi, Subprime Mortgage Credit Derivatives (2008) (arguing that the October 2006 Guidance should have regulated the hybrid 2/28).

[7] Kim, id. n. 57 (citing Interagency Guidance on Nontraditional Mortgage Product Risks, 71 Fed. Reg. 58,609 (Oct. 4, 2006)).

[8] See Editorial, Reforming the Financial System, N. Y. Times, Sept. 14, 2009; Edmund Andrews, Busted: Life Inside the Mortgage Meltdown 79 (2009).

[9] Section 143 of H. 3126, STATE LAW PREEMPTION STANDARDS FOR NATIONAL BANKS AND SUBSIDIARIES CLARIFIED, if enacted would provide for an amendment to the Bank Act, 12 U.S.C. 21 et. seq., stating in its key language that "a State consumer law is not inconsistent with Federal law if the protection the State consumer law affords consumers is greater than the protection provided under Federal law as determined by the Agency." H. 3126, Sec. 143(a).

[10] See Marquette National Bank v. First of Omaha Service Corp, 439 U.S. 299 (1978).

[11] 517 U.S. 735, 745-47 (1996).

Comptroller's interpretation of the scope of nationalized banking regulation.[12] The importance of a more balanced federalism is widely endorsed in the scholarship. [13]

In our view, whatever merit arguments in favor of preemption have are outweighed by the value of having states operate as laboratories, trying different approaches to lending problems, particularly in dealing with the relatively young problems of predatory lending.[14] It is important that Congress not take a simplistic approach favoring only federal development of consumer protection laws in financial products and services; and that Congress not limit the role of the states to enforcement of state and federal law. State legislatures and courts need to be able to continue to develop consumer protection law. Many of the types of non-bank financial products that will be within the jurisdiction of the CFPA have been regulated up until now only by the states, and their good work should not be undermined. In addition, problems are much more likely to grow larger if they can be addressed only at the federal level and not also by states where they first appear.

3. ***The authority to improve the way consumer rights are enforced.***[15] During the past decades, when an increasing proportion of consumer credit agreements have forced consumers into binding arbitration and have severely limited the opportunities to

---

[12] See, e.g., Am. Bankers Ass'n v. Lockyer, 239 F. Supp. 2d 1000 (E.D. Cal. 2002).

[13]See Nicholas Bagley, Note, The Unwarranted Regulatory Preemption of Predatory Lending Laws, 79 N.Y.U. L Rev 2274 (2004); Arthur E. Wilmarth, Jr., The OCC's Preemption Rules Exceed the Agency's Authority and Present a Serious Threat to the Dual Banking System and Consumer Protection, 23 Ann. Rev. Banking & Fin. L. 225 (2004); Keith R. Fisher, Toward a Basal Tenth Amendment: A Riposte to National Bank Preemption of State Consumer Protection Laws, 29 Harv. J.L. & Pub. Pol'y 981 (2006). Christopher L. Peterson, Federalism and Predatory Lending, Unmasking the Deregulatory Agenda, 78 Temple L. Rev. 1 (2005); see also American Bankers Association v Lockyer, 239 F Supp 2d 1000 (ED Cal 2002) (California Credit Card Payment Warning Act, Cal Civ. Code § 1748.13, requiring credit card bills to disclose the length of time consumers have to pay off their balances by paying the minimum, declared unconstitutional because preempted by federal law); Household Credit Services, Inc v. Pfennig, 541 US 232 (2004) (holding that Regulation Z's exclusion of overlimit fees from the term "finance charge" is in no way contrary to § 1605 of TILA). Regarding the more general importance of the states, see Herbert Wechsler, The Political Safeguards of Federalism: The Role of the States in the Composition and Selection of the National Government, 54 Colum L Rev 543(1954) ; Larry D. Kramer, Putting the Politics Back into the Political Safeguards of Federalism, 100 Colum L Rev 215 (2000); Frank S. Alexander Federal Intervention In Real Estate Finance: Preemption And Federal Common Law, 71 N.C. L. Rev. 293 (1993).

[14] See Baher Azmy, Squaring the Predatory Lending Circle: A Case for States as Laboratories of Experimentation, 57 Fla. L. Rev. 295, 301-02 (2005).

[15] Section 125 of H. 3126 if enacted would provide: AUTHORITY TO RESTRICT MANDATORY PRE-DISPUTE ARBITRATION. The Agency, by regulation, may prohibit or impose conditions or limitations on the use of agreements between a covered person and a consumer that require the consumer to arbitrate any future dispute between the parties arising under this title or any enumerated consumer law if the Agency finds that such prohibition, imposition of conditions, or limitations are in the public interest and for the protection of consumers.

challenge oppressive terms and unfair dealing, existing agencies have not acted effectively to promote the availability, impartiality and quality of arbitration tribunals.[16] The result, in too many cases, has been the demonstrable frustration of consumers seeking to vindicate their contractual rights. In fact, according to a recent Congressional Report, less than 1/10th of 1% of arbitrations are brought by consumers.[17] The literature concerning the difficulties with binding consumer arbitration for consumers is extensive.[18] Studies have found the arbitrators find for companies against consumers 94 to 96% of the time,[19] suggesting that arbitration providers are responding to the incentive to find for those who select them: the companies that insert their names in their form contracts. The recent case brought by the Minnesota Attorney General, charging the National Arbitration Forum with deceptive trade practices and false advertising, which terminated in a consent decree under which the NAF agreed to stop accepting new consumer arbitration cases, only emphasizes the importance of regulating predispute consumer arbitration.[20] The CFPA would have the ability to regulate consumer arbitration to insure that it is conducted fairly, or, if that proves impossible, to ban it altogether.

4. ***Standards for fairness, honesty, and information.***[21] It has become increasingly clear that existing disclosures of the costs and terms of many consumer financial products do

---

[16] See Arbitration Abuse: an Examination of Claims Files of the National Arbitration Forum, a Staff Report of the Domestic Policy Subcommittee Majority Staff Oversight and Government Reform Committee, House of Representatives (Dennis J. Kucinich, Chairman), , July 21, 2009, at http://www.clarksvilleonline.com/wp-content/uploads/2009/07/Report-on-National-Arbitration-Forum.pdf.

[17] "The only available data indicates that more than 99% of "consumer arbitrations" are debt collection claims filed by businesses, usually credit card companies or collection companies, against consumers, seeking to collect past due balances under arbitration "agreements" that were unilaterally imposed by the businesses." See Arbitration Abuse Arbitration Abuse: An Examination of Claims Files of the National Arbitration Forum, a Staff Report of the Domestic Policy Subcommittee Majority Staff Oversight and Government Reform Committee, House of Representatives (Dennis J. Kucinich, Chairman), July 21, 2009, at http://www.clarksvilleonline.com/wp-content/uploads/2009/07/Report-on-National-Arbitration-Forum.pdf.

[18] See, e.g., Mark Budnitz, Mandatory Arbitration: The High Cost of Mandatory Consumer Arbitration, 67 Law & Contemp. Prob. 133 (2004); Jean Sternlight, Panacea or Corporate Tool?: Debunking the Supreme Court's Preference for Binding Arbitration, 74 Wash U L Q 637 (1996); Jean Sternlight, Creeping Mandatory Arbitration: Is it Just?, 57 Stan L Rev 1631 (2005); Jack Wilson, "No-Class-Action Arbitration Clauses," State-Law Unconscionability, and the Federal Arbitration Act: A Case for Federal Judicial Restraint and Congressional Action, 23 Quinnipiac L Rev 737, 773 (2004).

[19] Public Citizen Report: The Arbitration Trap: How Credit Card Companies Ensnare Consumers (Sept. 2007) available at http://www.citizen.org/publications/release.cfm?ID=7545 (in the more than 19,000 cases in which an NAF-appointed arbitrator was involved, 94 percent of decisions were for business.); Simone Baribeau, Consumer Advocates Slam Credit-Card Arbitration, Christian Science Monitor, July 16, 2007, available at http://www.csmonitor.com/2007/0716/p13s01-wmgn.html ("arbitrators awarded in favor of creditors and debt buyers in more than 96 percent of the cases.").

[20] The complaint may be found at http://pubcit.typepad.com/files/2009-07-14-signed-complaint-with-exhibits.pdf and the consent decree at http://pubcit.typepad.com/files/nafconsentdecree.pdf.

not adequately inform consumers about the actual costs. For example, a 2007 Federal Trade Commission study found that many borrowers were not able to determine mortgage loan terms or costs from the disclosures in use at the time of the study.[22] If disclosures alone were adequate to enable consumers to obtain appropriate loans, it would not be possible for mortgage originators to "steer" borrowers who could qualify for prime loans to more expensive subprime loans, and yet such steering has been alleged repeatedly.[23] Disclosure approaches alone cannot solve problems that are caused by overly complex terms that consumers cannot readily comprehend;[24] or counteract terms

[21] Section 136 of H. 3126 if enacted would provide: STANDARD CONSUMER FINANCIAL PRODUCTS OR SERVICES. (a) Characteristics of Standard Consumer Financial Products or Services-Subject to regulations prescribed by the Agency under this section, a standard consumer financial product or service is a consumer financial product or service that-- (1) is or can be readily offered by covered persons that offer or seek to offer alternative consumer financial products or services; (2) is transparent to consumers in its terms and features; (3) poses lower risks to consumers; (4) facilitates comparisons with and assessment of the benefits and costs of alternative consumer financial products or services; and (5) contains the features or terms defined by the Agency for the product or service.

[22] James M. Lacko & Janis K. Pappalardo, IMPROVING CONSUMER MORTGAGE DISCLOSURES: AN EMPIRICAL ASSESSMENT OF CURRENT AND PROTOTYPE MORTGAGE DISCLOSURE FORMS ES-6, 11-12 (2007)

[23] See Marsha J. Courchane, Brian J. Surette, & Peter M. Zorn, Subprime Borrowers: Mortgage Transitions and Outcomes, 29 J. Real Estate Fin. & Econ. 365, 381 (2004) ("Our results suggest that borrowers may inappropriately receive subprime mortgages . . ."); Illinois Department of Financial and Professional Regulation, Findings from the HB 4050 Predatory Lending Database Pilot Program 5 (2007) (study of Chicago borrowers finds that many of the borrowers could have qualified for a "more affordable loan had they been better informed about what was available to them"); Michael S. Barr, Credit Where It Counts: the Community Reinvestment Act and Its Critics, 80 N.Y.U.L.Rev. 513, 556 (2005); Gretchen Morgenson, Inside the Countrywide Lending Spree, N.Y. Times, Aug. 26, 2007 (Countrywide's "incentive system also encouraged brokers and sales representatives to move borrowers into the subprime category, even if their financial position meant that they belonged higher up the loan spectrum."); Affidavit of Ton Paschal in City of Baltimore v. Wells Fargo ("I . . . regularly saw minority customers who had good credit scores and credit characteristics in subprime loans who should have qualified for prime or [Fair Housing Act] loans.").

[24] See generally Alan M. White & Cathy Lesser Mansfield, Literacy & Contract, 13 Stan. L. & Pol'y Rev. 233 (2002); President George W. Bush, White House Press Conference, Aug. 9, 2007, available at www.whitehouse.gov/news/releases/2007 ("We've had a lot of really hardworking Americans sign up for loans, and the truth of the matter is they probably didn't fully understand what they were signing up for."); Federal Reserve Board, Truth in Lending, 73 Fed. Reg. 44,522, 44,525-26 (July 30, 2008) ("Consumers who do not fully understand such terms and features, however, are less able to appreciate their risks . . . [f]or example, the payment may increase sharply and a prepayment penalty may hinder the consumer from refinancing to avoid the payment increase. Thus, consumers may unwittingly accept loans that they will have difficulty repaying."); Statement of Peter Orszag, CBO Budget Director, State of the US Economy and Implications for the Federal Budget: Hearing Before the H. Comm. on the Budget, 110th Cong., 6 (Dec. 5, 2007) ("some borrowers lacked a complete understanding of the complex terms of their mortgages and assumed mortgages that they would have trouble repaying."); Michael S. Barr, Sendhil Mullainathan, & Eldar Shafir, Behaviorally Informed Financial Services Regulation 8 (2008) ("a central problem [of the Mortgage Crisis] was that many borrowers took out loans that they did not understand and could not afford."); Elizabeth Renuart and Diane E. Thompson, The Truth, The Whole Truth, and Nothing But the Truth: Fulfilling the Promise of Truth in Lending, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1021318 ("The lender-created complexity of mortgage loans now exceeds what . . . even highly educated consumers are capable of comprehending."); Todd J. Zywicki, The Law and Economics of Subprime Lending, --- Colo. L. Rev. --- (forthcoming), available at

that are inherently unfair; or cure substantive defects in products whose individual attractiveness may be high for particular groups, but whose social impact is "toxic" on a large scale. Thus, so-called "exploding ARMs" may be appropriate for those who reasonably expect a substantial increase in income by the time the payments leap, such as medical residents, but are not suitable for those whose income is more stable and who are unlikely to find substantial payment increases affordable.[25] The literature encouraging a standard-setting approach, and reporting on its effective use in other nations, supports the case for its adoption here. [26]

http://ssrn.com/abstract_id=1106907 ("Having gone through the experience once, second-time homebuyers rarely even closely examine their loan documents. Nor is it likely that even if they did take the time to examine their documents, . . . most borrowers would be unable to comprehend most of their terms."); Norman I. Silber, "Thriving on Adversity: Corporate Treatment and Mistreatment of Consumers in the Wake of Hurricane Katrina, ---Loyola Consumer L.Rev. --- (forthcoming)(many hurricane victims deferred payments without appreciating that greater interest would accrue as a result); Allen J. Fishbein & Patrick Woodall, Exotic or Toxic? An Examination of the Non-Traditional Mortgage Market for Consumers and Lenders 2 (Consumer Federation of America 2006) ("more vulnerable consumers—first time homebuyers, unsophisticated financial consumers, and consumers traditionally underserved by the mortgage market, especially lower-income and minority consumers . . . .are less likely to understand . . . the complexity of the mortgage vehicles they are offered . . . ."); Kathleen C. Engel and Patricia A. McCoy A Tale of Three Markets: The Law and Economics of Predatory Lending, 80 Tex. L. Rev. 1255, 1286 (2002) ("the victims of predatory lenders sign documents without having a clear sense of the terms of the contracts, how much they borrowed, what they purchased, the terms of repayment, or the risks they assumed."); Statement of Ken Logan, Chairman-Elect, National Home Equity Mortgage Association, at the Federal Reserve Board Public Hearing, Building Sustainable Homeownership: Responsible Lending and Informed Consumer Choice 92 (July 11, 2006) ("few borrowers fully understand the residential transaction or the disclosures.").

[25] According to the Center for Responsible Lending, terms that increase the risk of foreclosure include "adjustable interest rates, balloon payments, prepayment penalties, and loans with limited documentation of borrowers' loan qualifications." Ellen Schloemer, Wei Li, Keith Ernst, & Kathleen Keest, Center for Responsible Lending, Losing Ground: Foreclosures in the Subprime Market and Their Cost to Homeowners 5 (2006)

[26] See, e.g., Jean Braucher, Delayed Disclosure in Consumer E-Commerce as an Unfair and Deceptive Practice, 46 Wayne L. Rev. 1805 (2000); Richard B. Cappalli, Arbitration of Consumer Claims: The Sad Case of Two-Time Victim Terry Johnson or Where Have You Gone Learned Hand?, 10 BU Pub Int. L. J. 366, 400-01 (2001); Jon D. Hanson and Douglas A. Kysar, Taking Behavioralism Seriously: The Problem of Market Manipulation, 74 NYU L Rev 630, 654-66, 722 (2002); Samuel Issacharoff & Erin F. Delaney, Credit Card Accountability, 73 U. Chi. L. Rev. 157, 168-75 (2006); Norman I. Silber, Observing Reasonable Consumers: Cognitive Psychology, Consumer Behavior and Consumer Law, 2 Loy. Consumer L. Rev. 69, 74 (1990); Norman I. Silber, Late Charges, Regular Billing, and Reasonable Consumers: A Rationale for a Late Payment Act (2008); Jeff Sovern, Towards a New Model of Consumer Protection: The Problem of Inflated Transaction Costs, 47 Wm and Mary L. Rev. 1635 (2006); Cass R. Sunstein, Boundedly Rational Borrowing, 73 U Chi L Rev 249, 268 (2006); Lauren E. Willis, Decisionmaking and the Limits of Disclosure: The Problem of Predatory Lending: Price, 65 Md. L. Rev. 707 (2006).

Conclusion

We urge Congress to take swift action to pass legislation that contains the tools needed to move forward past the mistakes that have undermined our economic stability and toward a better future for consumers and the nation.

For further information, please send an email to Professor Norman I. Silber at Norman.I.Silber@hofstra.edu or to Professor Jeff Sovern at sovernj@stjohns.edu.

Respectfully,[27]

Richard M. Alderman
Associate Dean
Director, Consumer Law Center
Dwight Olds Chair in Law
University of Houston Law Center

Peter Alexander
Professor of Law
Southern Illinois University School of Law

Ian Ayres
William K. Townsend Professor
Yale Law School

Professor Laura Boeckman
Consumer Law Clinic
Florida Coastal School of Law

Jean Braucher
Roger C. Henderson Professor of Law
University of Arizona James E. Rogers College of Law

Raymond H. Brescia
Assistant Professor of Law
Albany Law School

Mark E. Budnitz
Bobby Lee Cook Professor of Law
Georgia State University College of Law

[27] Affiliations provided for identification only.

J. Scott Colesanti
Assistant Professor of Legal Writing and Research
Hofstra University Law School

Prentiss Cox
Associate Professor of Clinical Law
University of Minnesota Law School

Marianne B. Culhane
Professor of Law
Creighton University School of Law

Gina Calabrese
Professor of Clinical Education and Associate Director
Elder Law Clinic
St. John's University School of Law

A. Mechele Dickerson
Arthur L. Moller Chair in Bankruptcy Law and Practice and
Associate Dean for Academic Affairs
The University of Texas at Austin School of Law

Vincent DiLorenzo
Professor of Law
St. John's University School of Law

Kurt Eggert
Professor of Law and Director of Clinical Legal Education
Chapman University School of Law

Kathleen C. Engel
Professor of Law
Suffolk University Law School

Linda E. Fisher
Professor of Law
Seton Hall Law School

Michael D. Floyd
Professor of Law and Director of International Studies
Samford University, Cumberland School of Law

Julie P. Forrester
Professor of Law
SMU Dedman School of Law

Monroe H. Freedman
Professor of Law
Hofstra University School of Law

David A. Friedman
Assistant Professor of Law
Willamette University College of Law

Anna Gelpern
Associate Professor of Law
American University Washington College of Law

S. Elizabeth Gibson
Burton Craige Professor of Law
University of North Carolina at Chapel Hill

Dwight Golann
Professor of Law, Suffolk University Law School
Former Chair, Consumer Advisory Council to the Governors of the Federal Reserve
Former Chair, Consumer Financial Services Committee, American Bar Association

Ann Goldweber
Professor of Clinical Education
Director of Clinical Education
St. John's University School of Law

Michael M. Greenfield
George Alexander Madill Professor of Contracts and Commercial Law
Washington University in St. Louis

Daniel J.H. Greenwood
Professor of Law
Hofstra University School of Law

John Hennigan
Professor of Law
St. John's University School of Law

Max Huffman
Associate Professor of Law
Indiana University School of Law—Indianapolis

Melissa B. Jacoby
George R. Professor of Law,
University of North Carolina at Chapel Hill.

Creola Johnson
Professor of Law
Ohio State Univ.
Moritz College of Law

Jason Kilborn
Associate Professor of Law
John Marshall Law School

Adam J. Levitin
Associate Professor of Law
Georgetown University Law Center

Jonathan C. Lipson
Peter J. Liacouras Professor of Law
Temple University--Beasley School of Law

Cathy Lesser Mansfield
Professor of Law
Drake University Law School

Jennifer S. Martin
Visiting Associate Professor of Law
University of Oregon School of Law

Stewart Macaulay
Malcolm Pitman Sharp Hilldale Professor Emeritus
University of Wisconsin-Madison

Patricia A. McCoy
Director, Insurance Law Center
and George J. & Helen M. England Professor of Law
University of Connecticut School of Law

Stephen Meili
Professor of Clinical Law
University of Minnesota Law School

Ralph James Mooney
Kaapcke Professor of Law
University of Oregon

James P. Nehf
Associate Dean for Graduate Studies
Professor of Law and Cleon H. Foust Fellow
Indiana University School of Law—Indianapolis

Scott Norberg
Professor of Law
Florida International University College of Law

David G. Oedel
Professor of Law
Mercer University Law School

Rafael I. Pardo
Associate Professor of Law
Seattle University School of Law

Christopher L. Peterson
Professor of Law
Associate Dean for Academic Affairs
University of Utah, S.J. Quinney College of Law

Gary Pieples
Visiting Assistant Professor, Clinic Director
Securities Arbitration and Consumer Clinic
Syracuse University, Office of Clinical Legal Education

Lydie Nadia Cabrera Pierre-Louis
Assistant Professor of Law
St. Thomas University School of Law

Katherine M. Porter
Visiting Associate Professor of Law
University of California at Berkeley
Associate Professor of Law
University of Iowa College of Law

John A. E. Pottow,
Professor of Law
University of Michigan Law School

Burnele V. Powell
Miles & Ann Loadholt Professor of Law
University of South Carolina School of Law

Dee Pridgen
Associate Dean and
Carl M. Williams Professor of Law and Social Responsibility
University of Wyoming College of Law

Nancy B. Rapoport
Gordon Silver Professor of Law
William S. Boyd School of Law
University of Nevada—Las Vegas

David Reiss
Professor of Law
Brooklyn Law School

Janet Leach Richards
Cecil C. Humphreys Professor of Law
University of Memphis Cecil C. Humphreys School of Law

Arnold S. Rosenberg
Assistant Dean
Thomas Jefferson School of Law

Edward L. Rubin
University Professor of Law and Political Science
FedEx Research Professor
Vanderbilt University Law School

Elizabeth Renuart
Assistant Professor of Law
Albany Law School

Heidi Mandanis Schooner
Professor of Law
Columbus School of Law
The Catholic University of America

Teresa M. Schwartz
J.B. & Maurice C. Shapiro Professor (Emeritus) of Public Service Law
George Washington University Law School

Charles B. Shafer,
Professor of Law
University of Baltimore School of Law

Norman I. Silber
Professor of Law,
Hofstra University School of Law

Ronald H. Silverman
Peter S. Kalikow Distinguished Professor of Real Estate Law
Hofstra University School of Law

Jeff Sovern
Professor of Law
St. John's University School of Law

John A. Spanogle
William Wallace Kirkpatrick Professor of Law
George Washington University Law School

Jean R. Sternlight
Saltman Professor
Boyd School of Law
University of Nevada, Las Vegas

Charles J. Tabb
Alice Curtis Campbell Professor
University of Illinois College of Law

Gerald J. Thain
Professor of Law
Chair-holder, Consumer Law Professorship
University of Wisconsin Law School

Gregory M. Travalio
Professor of Law Emeritus
Michael E. Moritz College of Law
The Ohio State University

G. Ray Warner
Professor of Law & Associate Dean for Bankruptcy Studies
St. John's University School of Law

Alan M. White
Assistant Professor of Law
Valparaiso University School of Law

William C. Whitford
Emeritus Professor of Law
Wisconsin Law School

Mary Jo Wiggins
Associate Dean & Professor of Law
Class of 1975 Endowed Professor
The University of San Diego School of Law

Arthur E. Wilmarth, Jr.

Professor of Law
George Washington University Law School

Lauren Willis
Professor of Law
Loyola Law School Los Angeles

Jane K. Winn
Charles I Stone Professor and Director, Law, Technology & Arts Group
University of Washington School of Law

William J. Woodward, Jr.
Professor of Law
Temple University James Beasley School of Law

Eric W. Wright
Professor of Law
Santa Clara University School of Law

SEIU®
Stronger Together

ANDREW L. STERN
International President

ANNA BURGER
International Secretary-Treasurer

MITCH ACKERMAN
Executive Vice President

MARY KAY HENRY
Executive Vice President

GERRY HUDSON
Executive Vice President

ELISEO MEDINA
Executive Vice President

BRUCE RAYNOR
Executive Vice President

DAVE REGAN
Executive Vice President

TOM WOODRUFF
Executive Vice President

SERVICE EMPLOYEES
INTERNATIONAL UNION
CTW, CLC

1800 Massachusetts Ave NW
Washington, DC 20036

202.730.7000
TDD 202 730 7481
www.SEIU.org

October 5, 2009

The Honorable Barney Frank
Chairman, Committee on Financial Services
U.S. House of Representatives
2129 Rayburn House Office Building
Washington, D.C. 20515

Re: Submission of additional information as requested by Representative Patrick T. McHenry

Dear Mr. Chairman:

Thank you for the opportunity to participate in the Committee on Financial Services' hearing on "Perspectives on the Consumer Financial Protection Agency" on Wednesday, September 30, 2009.

As requested by Representative Patrick T. McHenry during the hearing, here is the additional financial information for the record regarding the Service Employees International Union's (SEIU) payments to ACORN.

	2008	2009
Contributions (including General Support and ACORN Projects like Voter Registration)	190,000	25,000
Contracted Services (including services such as the Organizing Apprenticeship Program and Childcare Worker Organizing Campaigns)	1.4 million	220,000

While SEIU has contracted with ACORN for voter registration, community mobilization efforts, and organizing work, we have suspended all active work with ACORN while former Massachusetts Attorney General Scott Harshbarger conducts his review of the organization.

Sincerely,

Anna Burger
International Secretary-Treasurer

AB:ST:gmb

opeiu#2
afl-cio, clc

Protecting consumers requires protecting front-line bank employees

SEIU Stronger Together

Bank employees including tellers, personal bankers, credit card call center workers and managers have told SEIU how their banks target vulnerable consumers with deceptive practices that drive up banks' fee income. Employees report that banks are targeting working and immigrant families in particular to meet sales goals, generate more overdraft fees, and raise credit card interest rates.

Low base salaries and fear of losing their jobs force bank workers to meet high sales goals and push debt onto customers.

> "You want to do what is best for the customer but you can't if you want to reach your goals If you don't hit your goal, you're fired."
>
> **Bank of America platform worker,** *Boston*

First, bank employees want protections that will allow them to blow the whistle on bank practices that hurt their customers and the American economy. Second, they want a voice in the rebuilding of the financial sector and—especially important in an industry where tellers are earning on average $11.32 an hour—the ability to negotiate sensible compensation policies that reward service and sound banking over short-term sales.

> "I often leave my job feeling as if I may not have a job to return to with the constant warnings, threatening e-mails, sales goals... The sales tactics and goals we must often meet sometimes force us to put the consumer—young and old alike—into products that they really can't afford, or are not suitable for their financial needs."
>
> **SunTrust personal banker and teller,** *Washington, D.C.*

Piling on fees

- Encouraging Overdrafts. Bank of America customers who track their spending online do not see all of their checking account activity. Customers do not see 'holds' and changes in the order of their transactions, creating confusion about account balances and allowing the bank to assess more overdraft penalties. The bank encourages customers concerned about overdraft fees to rely on the bank's online system to avoid fees. This practice and some of the bank's overdraft fee practices generally are the subject of a lawsuit in California state court—Clossen v. Bank of America—that is now being settled for $35 million.

> "My job is to create irresponsible debt. It should be helping families build wealth; counseling them about using debt responsibly. But that's not what the bank rewards."
>
> **Bank of America branch manager,** *Washington, D.C.*

- Refunds refused. Bank of America employees report the bank's automated system makes full refunds of overdraft fees for customers who deserve refunds nearly impossible. Washington, D.C., employees, for example, report that they are penalized by the bank if they override the system and award refunds to customers. In June 2009, Bank of America raised from five to 10 the maximum number of overdraft fees Bank of America can apply each day. The new daily limit is as much as $350.

Targeting vulnerable customers

- Interfering with customers' accounts. Bank of America managers tell employees to sign customers up for online banking using customers' confidential information obtained from servicing other accounts.

> "I know many employees who have been pressured so hard to increase their sales quotas that they are going home at night and logging on to people's accounts to make up more transactions ... and when you live the day to day here, it's easy to understand why. If you push back, you're going to get pushed out."
>
> **Bank of America branch manager,** *Washington, D.C.*

- Targeting students, seniors, and non-native English speakers. Employees report that customers are unknowingly signed up for credit cards and bank accounts. In Washington, D.C., there is fierce competition among branches to canvass in the Mexican and Salvadoran embassies, and personal bankers sell accounts in high schools. In Los Angeles, employees report customers attempting to cash federal tax return checks are told instead they should instead deposit them in seven-day CD accounts.

Unethical credit card practices

- Denying active duty military the rate they are entitled to under law. All active duty soldiers are entitled to a 6 percent maximum interest rate on their credit cards, but the bank's employees were not trained to inform members of the armed forces of that benefit. Instead, call center employees report that in the past they have not been allowed to offer that rate unless the customer recalls the entire name of the legislation authorizing the rate.

> "The more money I sold you and the higher the rate, the more money I made. That's what the bank rewards—sales, not service."
>
> **Former Bank of America call center worker,** *Maine*

- Recognizing charge-offs. Credit card collectors routinely use a variety of questionable and aggressive practices such as accepting floating checks that do not have funds to cover them in order to hold onto delinquent accounts for more than 180 days. In this way, the bank can still claim the value of the debt as an asset on its books and in its regulatory filings. Nonperforming debt is a basic measure of a bank's health.
- Delivering threats, spreading rumors. Collectors at Bank of America credit card centers report being given a script that instructed collectors to leave answering machine messages that threatened property liens or lawsuits.
- Failing to disclose. Bank of America credit card call center employees report that they were instructed to use special cell phones—as opposed to recordable landlines—for aggressive collection calls. Bank vice presidents also sent handwritten postcards to customers that do not identify the bank or offer a toll-free number for customers to call.

Undermining employees

- Refusing to pay overtime. Bank of America personal bankers and tellers report they regularly work six days a week, are required to work hours off the clock nearly every week, and receive little to no pay for the regular and repeated overtime work. This is the subject of a pending class action lawsuit in Kansas, the allegations of which appear to mirror what we have heard from employees at Bank of America branches.

> "I am a personal banker in Cambridge, Mass. My coworkers and I have many stories of abuse of customers and bad sales tactics. If we complain to our managers, they just shut us down. We have many concerns about low pay, but worse is having to force bad products on customers."
>
> **Bank of America platform worker,** *Cambridge, Mass.*

- No whistleblower protections. Bank employees who want to blow the whistle on illegal or inappropriate bank practices have no special protections under federal law. Bank of America workers with complaints are told to call a bank-operated hotline. Four Los Angeles-area employees who showed interest in forming a union used the hotline in May 2009 to complain about branch management. One of the four was fired the following week.
- Workers pressured not to organize. They were reprimanded, and one of the four was fired. Bank managers in Philadelphia, Boston, Washington, D.C., and Los Angeles report that bank policy prohibits employees from talking with union organizers at any time—whether at home or at work.

The Trillion Dollar Bank Job

How Wall Street and the Big Banks Are Holding Up America's Economic Recovery

September 2009

Executive Summary

It's been a year since the Lehman Brothers collapse set off a flurry of bank failures and near-failures, threatening the very foundations of the global financial system and bringing our national economy to the brink of a second Great Depression. Taxpayers stepped in and bailed out the ailing banks in order to resuscitate the larger economy and get money flowing to Main Street again. A year later we wonder what we have gotten for that investment. While ordinary Americans are still struggling to stay afloat, the bankers are back to business as usual, paying out billions in bonuses, making profits on the backs of the very taxpayers who bailed them out, and throwing up roadblocks to meaningful regulatory reform that would prevent a repeat of the crisis.

What did we get over the last year?

1. Taxpayer Bailout. Taxpayers have committed **$4.7 trillion** to the financial sector over the last year, only $700 billion of which was through TARP. Even banks like Goldman Sachs that returned their TARP funds earlier this year continue to benefit from other bailout programs, such as the $12.9 billion that Goldman received as an AIG counterparty that it will never have to pay back. Once all crisis-related programs are factored in, taxpayers could be on the hook for a grand total of up to **$17.8 trillion** for this economic rescue.

2. Trillions of Dollars in Lost Wealth for Ordinary Americans. The bank-induced economic crisis has cost Americans trillions of dollars already, on top of the trillions more we have committed through the bailouts.

- American families lost **$11 trillion** in wealth in 2008, nearly 18% of their net worth.
- Americans have lost **$6.1 trillion** in homeowner wealth since June 2006.
- Banks have generally refused to modify mortgages to help prevent foreclosures because it is more profitable for them to collect fees as a family loses its home than it is to save the home.
- Over **5.3 million** Americans have lost their jobs since last September, and the national unemployment rate is at its highest in 26 years.
- Personal bankruptcies are soaring, and are expected to reach levels not seen since a 2005 law made it more difficult to file bankruptcy.
- Between October 2007 and December 2008, the top 1,000 US pension funds lost **$1.75 trillion**, or 23.3% of their value, the worst losses in 30 years.
- Declining property values and personal income have taken their tolls on state and local budgets, leading to cuts in essential services like public health programs, childhood education, and programs for the elderly and disabled.

3. Back to Greed & Business as Usual. While taxpayers are still suffering, the big banks are back to business as usual, paying out tens of billions in bonuses, making tens of billions in profits on the backs of American consumers, and returning to the same kinds of practices that caused the crisis in the first place.

- The nation's top six banks paid out **$31.2 billion** in 2008 bonuses this past winter, and in the first half of 2009 alone, they set aside another **$74.4 billion** for bonuses and compensation for their employees.
- The top six banks posted **$29.6 billion** in profits in the first half of 2009, just months after accepting $160 billion in direct TARP infusions.
- The banks made these handsome profits by embracing the same kind of excessive risk-taking that caused the crisis in the first place: by trading highly-complex derivatives, by repackaging mortgage-backed securities, and by making predatory loans to low-income, high-risk consumers who typically cannot afford to pay them back.
- Rising fees also contributed to the banks' bottom line. Americans will pay more than **$38 billion** in overdraft fees alone in 2009, more than $125 for every man, woman, and child in the United States.
- Banks also raised credit card interest rates on American consumers in an effort to boost their profits before the new credit card reforms take effect next year.
- Even as they continue lending to large corporations and private equity firms, the banks have drastically reduced their small business lending. Lending through the SBA's main program **decreased 42%** over the previous year in the first seven months following the bailout.

4. Banks Standing in the Way of Reform. Despite taking trillions in bailouts, the banks are now using our money to lobby against reforms that would protect us from their abuses. In the nine months following the bailout, companies in the financial, insurance, and real estate sector spent **$321 million** lobbying against federal reforms such as the creation of the Consumer Financial Protection Agency, limits on bonuses, overdraft fee regulation, credit card reform, loan modification proposals that could help keep millions of Americans in their homes, and a ban on payday lending.

This is not what we signed up for!

It's Time for a Real Economic Recovery. As Wall Street celebrates 'green shoots' in the economy and points to signs of recovery, it feel like déjà vu. The market was celebrating signs of recovery last year too, just months before the Lehman Brothers collapse. Meanwhile, Main Street is still hurting. We don't need bankers trying to convince us that happy days are here again. We need real regulatory reform now so that we can have a real economic recovery on Main Street.

It is time for the banks to start aiding in America's economic recovery. The banks need to:

1. Stop foreclosures and save Americans' homes and state and local budgets;
2. Provide the same affordable loans to state and local governments that banks receive from the federal government;
3. Restore small business lending to save jobs and tax revenue; and
4. Lower interest rates on consumer credit cards and stop charging abusive overdraft fees that take billions out of consumers' pockets.

A year ago, Lehman Brothers' collapse shook Wall Street to its core and set off an economic crisis that threatened the foundations of the entire global financial system. In the flurry of bank failures and near-failures that followed, household names like Merrill Lynch, Washington Mutual, and Wachovia either disappeared or got swallowed up by competitors. Within a week, there were no more big, independent investment banks on Wall Street.[1]

As bankers across the country were fighting for their lives, taxpayers threw them a lifeline. We stepped in and bailed out Wall Street to the tune of trillions of dollars because we were told it was necessary to resuscitate the economy. The Treasury Department told us that banks would use taxpayer dollars to modify mortgages to help working families stay in their homes and resume lending to small businesses in order to stem rising unemployment rates and stimulate the economy.

One year later, what have the bailouts gotten us? While top bankers are continuing to make billions of dollars in bonuses, none of the promises made to the American people have been honored. Families continue to face rising foreclosures, rising unemployment, higher credit card interest rates, higher overdraft fees, and roadblocks to real financial reform that would protect us from a repeat of the same crisis in the future. Our pension funds are in freefall, unemployment is skyrocketing, and personal bankruptcies are on pace to set a record for the years after the passage of the new bankruptcy law in 2005.

Some of the big banks claim that they are profitable again. They are raking in tens of billions in profits and paying out tens of billions in bonuses. However, they returned to profitability through the same old tricks—by taking on even more risk with *our* money, by raising the fees and interest rates that they charge *us*, by continuing to foreclose on *our* homes, and cutting lending to small businesses in *our* communities. Furthermore, they are on a lobbying spree, using our money to lobby against the sensible reform that Americans want. They have fought tooth and nail against reforms such as the Consumer Protection Agency that would protect us from their abuses.

Despite taking our money, the banks have done little to help revitalize the economy. **The bailout was supposed to rescue the larger economy, not turn into a handout to Wall Street.** The banks, through their risky behavior, robbed average Americans of trillions of dollars of our wealth. They have taken trillions in bailouts and backstops and have done nothing to fix the overall economy that they crashed.

It is time for the banks to start aiding in America's economic recovery. The banks need to:

1. **Stop foreclosures and save Americans' homes and state and local budgets;**
2. **Provide the same affordable loans to state and local governments that banks receive from the federal government;**
3. **Restore small business lending to save jobs and tax revenue; and**
4. **Lower interest rates on consumer credit cards and stop charging abusive overdraft fees that take billions out of consumers' pockets.**

The Bailout: A Year in Review

A year ago, as the banks fell apart, the federal government moved in with a variety of programs to bail them out and prevent them from taking the entire economy into a freefall.

Although the $700 billion Troubled Assets Relief Program (TARP) is the best-known, in reality, the federal government set up a variety of programs to backstop, guarantee, infuse, and hold up the banks. Taxpayers have already committed $4.7 trillion to the financial sector over the last year through an alphabet soup of programs like TLGP, TALF, and HAMP.[2] Moreover, while banks like Goldman Sachs, Morgan Stanley, and JPMorgan Chase can now brag about getting approval for and, in some cases, actually returning TARP funds, they will continue to benefit from this plethora of other taxpayer handouts,[3] such as the $12.9 billion that Goldman Sachs received as a counterparty to AIG that it will never have to pay back.[4]

The Federal Reserve has set up emergency lending facilities that give banks access to cheap money to get them to start lending again. The FDIC has unveiled guarantee programs to protect the banks against losses. The Treasury has pledged $200 billion to support Fannie Mae and Freddie Mac. HUD has put $300 billion into the Hope for Homeowners Program. Once all of the crisis-related programs are factored in, including the stimulus package and the auto bailout, the total taxpayers could be on the hook for up to $17.8 trillion.[5]

These programs have saved the banks from their risky bets on toxic securities. However, banks now claim they are back to profitability and doing well despite their continued reliance on these taxpayer-funded programs.

Trillions of Dollars in Lost Wealth

One year later, the American families who funded the bailout are not doing so well. The fallout from this bank-induced economic crisis has hit Americans hard. American families lost $11 trillion in wealth in 2008 alone, nearly 18% of their net worth.[6] Millions of us have lost our jobs or been thrown out of our homes. Personal bankruptcies have shot through the roof. Our life savings and retirement funds have been decimated. And because of billions in budget shortfalls, our state and local governments are being forced to cut back on services like public health programs and childhood education. This is all above and beyond the trillions in bailouts and backstops that we have had to fork over to the banks.

Rising Foreclosures

Our communities have been devastated by the foreclosure crisis. American families have lost $6.1 trillion in homeowner wealth since 2006.[7] The average homeowner has lost almost $110,000 in equity.[8] In a vicious cycle, foreclosures cause property values of neighboring homes to decline, making it more difficult for neighboring homeowners to refinance their loans, in turn causing them to fall into foreclosure as well. Every thirteen seconds another American home goes into foreclosure.[9]

According to the *New York* Times, a recent survey by the Mortgage Bankers Association found that "six million loans were either past due or in foreclosure in the second quarter of 2009, the highest level ever recorded by the group."[10] By 2011, nearly half of all Americans will be underwater on their mortgages.[11] In parts of California, Nevada, and Florida, the number will be over 90%.[12] For most Americans, our home is a major source of wealth for our families. This is a staggering loss of wealth that most of our families will likely never recover.

Unfortunately, banks are not doing their part to help fix the problem. A study by the Federal Reserve Bank of Boston shows that banks are not modifying loans to help homeowners avoid foreclosure because "Loan modification is not profitable for lenders." According to the *Boston Globe*, the study found that "only 3 percent of seriously delinquent borrowers—those more than 60 days behind—had their loans modified to lower monthly payments."[13]

Industry insiders say that the reason banks are reluctant to modify loans is that delinquent loans allow the banks that service the loans to collect fees from the homeowner—late fees, fees for insurance, appraisals, title searches, and legal services.[14] Because mortgages are typically sold off to third-party investors who absorb the losses when a house goes into foreclosure, the banks that service the loans often do not have a vested interest in avoiding foreclosure.[15] Therefore they are able to maximize their profits by charging fees as homeowners fall behind on their payments and slowly slip into foreclosure.

According to an attorney at the National Consumer Law Center quoted in the *New York Times*, "Servicers thus have an incentive to push homeowners into late payments and keep them there: if the loan pays late, the servicer is more likely to profit."[16]

According to the Treasury Department's first monthly report on loan modifications in August, Bank of America and Wells Fargo were the worst performers among the big banks when it came to loan modifications.[17] Despite the fact that the two banks have taken $70 billion in direct TARP funds and posted over $13 billion in profits in the first half of this year,[18] they still are not doing their part to help the very taxpayers who bailed them out to stay in their homes.

Rising Unemployment

Over 5.3 million Americans have lost their jobs since last September,[19] and the national unemployment rate has climbed 56%, from 6.2% in September to 9.7% in August,[20] its highest in 26 years.[21] Additionally, another 291,000 Americans have been added to the ranks of "discouraged workers" who are no longer included in unemployment figures because they have stopped looking for work. The number of discouraged workers is up 62% since last September.[22] Altogether, there are 25.8 million unemployed, underemployed, or discouraged workers in the US, 16.8% of the national workforce.[23]

Rising unemployment has taken a toll on our families, as for the first time ever, the number of Americans receiving food stamps topped 34 million, or roughly one in nine Americans.[24] Because unemployment reduces disposable income, it leads to decreased consumer spending, which serves to deepen the recession, possibly leading to even more layoffs and unemployment.

Rising Personal Bankruptcies

Personal bankruptcy filings have surged over the last year during the economic downturn. 1.25 million people filed for personal bankruptcy in the year ending in June, up 34% from the previous year.[25] Experts predict filings this year will be reach levels not seen since 2005, when 2.04 million people rushed to file before a new law went into effect making it more difficult to file for bankruptcy.[26] In July already, more than 126,000 people filed, the highest monthly figure since the 2005 law went into effect.[27]

Lost Retirement Security

The turmoil in the stock markets caused by Wall Street's missteps has had profound ramifications for Main Street. American workers' pensions have taken a serious hit during the crisis, putting millions of hard working Americans' retirement security at risk. In the twelve months between October 2007 and September 2008, the top 1,000 pension funds in the country lost $1 trillion in value. In the three months following the Lehman Brothers collapse, the losses accelerated rapidly, and by December 2008, they had lost an additional $754 billion. The funds lost 23.3% of their value ($1.75 trillion) in just fifteen months, the worst losses in 30 years.[28]

Cuts to Services

Falling home values and rising unemployment have taken a toll on our state and local tax revenues. The $6.1 trillion in homeowner wealth that has been lost in the last three years has led to a $58 billion reduction in annual property tax revenues.[29] The decline in tax receipts has contributed to budget crises all over the country. In a National League of Cities survey, 67% of cities reported hiring freezes or layoffs and 62% reported having to delay or cancel capital projects because of deterioration in the economy.[30] According to the Center for Budget and Policy Priorities, "At least 48 states have addressed or still face shortfalls in their budgets for fiscal year 2010 totaling $165 billion or 24 percent of state budgets," and 34 states are already anticipating holes in their 2011 budgets totaling at least $180 billion.[31]

As a result, states have been forced to make drastic cuts:[32]

- 21 states have made cuts to public health programs.
- 22 states have made cuts to services for the elderly and disabled.
- 24 states have made cuts in K-12 education.
- 32 states have made cuts in higher education.
- 40 states have made cuts in their government workforce, often through layoffs.

Back to Business as Usual

While taxpayers suffer under the crushing burden of the economic crisis and are on the hook for the Wall Street bailouts, the big banks are back to business as usual. They are ignoring their commitments to taxpayers and are helping themselves instead, setting aside tens of billions for bonuses, returning to the same risky behavior that caused the crisis in the first place, and making tens of billions in profits on the backs of American consumers.

Billions in Bonuses

Wall Street's bonus structure incentivized short-term profits over long-term stability. Bankers were awarded bonuses based on how their trades performed in the short run. If their bets went bad a couple of years down the road, they got to keep the money anyway. This encouraged excessive risk-raking, since the bankers' trades only had to perform well until they were paid their bonuses. This perverse compensation structure has been identified as a culprit in the economic crisis.[33]

In his report on Wall Street bonuses, New York State Attorney General Andrew Cuomo wrote of Wall Street's "heads I win, tails you lose"[34] bonus system:

> [T]here is no clear rhyme or reason to the way banks compensate and reward their employees...[I]n these challenging economic times, compensation for bank employees has become unmoored from the banks' financial performance.
>
> Thus, when the banks did well, their employees were paid well. When the banks did poorly, their employees were paid well. And when the banks did very poorly, they were bailed out by taxpayers and their employees were still paid well...[35]

Yet, despite this recognition that excessive and perverse compensation structures helped fuel the economic crisis, the big banks are continuing to pay their executives astronomical salaries and bonuses. This past winter, the nation's top six banks (Bank of America, Citigroup, Goldman Sachs, JPMorgan Chase, Morgan Stanley, and Wells Fargo) paid out $31.2 billion in 2008 bonuses to reward their bankers for posting $84.6 billion in losses last year and wreaking havoc on the global economy.[36]

In the first half of 2009, these six big banks set aside $74.4 billion in bonuses and compensation for their employees.[37] At this rate, total 2009 compensation at these banks could top $148 billion, almost as much as the $160 billion in direct TARP infusions that these six banks took last fall. This would be even higher than the banks paid out any year during the subprime boom.[38]

Even more outrageous, the two most heavily bailed-out banks, Bank of America and Citigroup, are increasing employees' base salaries to get around limits on bonuses for TARP recipients.[39] Citigroup will hike salaries by as much as 50%, so that most employees' compensation will not come down from last year's levels.[40] Bank of America is also offering signing packages to its new Merrill Lynch hires that are even richer than what Merrill paid out at the peak of the economic boom in 2006 and 2007.[41]

Billions in Profits

The same banks that were on life support a year ago posted billions in profits just months later. In the first half of 2009, the top six big banks alone brought in $29.6 billion in profits.[42] Goldman Sachs posted the biggest quarterly profit in its 140-year history this past June, bringing in $50 million a day.[43]

The banks did it by resorting to the same old tricks as before—increasing risk, hiking up bank fees and credit card interest rates, cutting small business lending, and by refusing to modify mortgages to prevent foreclosures so that they can collect fees instead as mentioned earlier.

Increasing Risk

The banks are once again embracing the same kind of excessive risk-taking that caused the crisis in the first place:

- Goldman Sachs turned a record profit in the second quarter by making even riskier bets than it was making before the crisis hit. The bank actually increased its risk profile after getting taxpayer bailout funds, making its record profits by gambling with our money.[44]
- Bank of America, Chase, and Citigroup are all linking corporate credit lines to credit default swaps, the same complex derivatives that caused AIG to collapse.[45]
- Morgan Stanley, Smith Barney, and UBS are now selling "structured notes", which are essentially highly risky and complex derivatives for small businesses.[46]
- In recent months, investment banks have started repackaging old mortgage-backed securities and selling them again as new products. These were the same toxic securities that helped cause the crisis in the first place, and banks are again repackaging and marketing them as super-safe AAA-rated investments.[47]
- Banks like Wells Fargo, US Bank, and Fifth Third are starting up or expanding usurious payday loan programs that charge interest rates as high as 400% to low-income, high-risk consumers who typically cannot afford to pay back the loans.[48]

Hiking Bank Account Fees

Banks are also boosting their bottom lines by raising fees on consumers to offset their losses on risky loans and toxic securities.[49] American consumers will pay more than $38 billion in overdraft fees this year,[50] more than the annual revenues of most Fortune 500 firms including Apple, Google, and Nike.[51] That is $125 for every man, woman, and child in the United States.[52] The national median overdraft fee rose 4% this year, to $26, the first time the fee has gone up during a recession.[53] Earlier this year, Bank of America more than doubled its daily overdraft fee limit from $160 to $350.[54]

But the fee increases are not limited to overdrafts. Bank of America also increased its monthly maintenance fee for its MyAccess Checking Accounts by 50% this year.[55] Meanwhile, Wells Fargo, JPMorgan Chase, and US Bank are passing increased costs for deposit insurance onto customers.[56] As the *New York Times* put it, the result is that "Americans are paying more to save and spend their money."[57]

Raising Credit Card Rates

Banks are also running up interest rates and fees on credit card rates in an effort to boost profits before the new credit card reforms take effect next year.[58] This year, Citigroup has raised interest rates on 13-15 million credit cardholders, by an average 24%, or nearly three percentage points.[59] Bank of America, JPMorgan Chase, and Capital One also hiked up interest rates on many of their cardholders that had never missed a payment.[60] Bank of America had already been arbitrarily raising interest rates on at least one million play-by-the-rules, pay-on-time customers even before the bailout.[61] Bank of America, Chase, and Discover have all raised transaction fees for balance transfers on credit cards by at least 20%.[62]

Cutting Small Business Loans

Even though bailout funds were intended to get banks to start lending again, the banks have drastically reduced their small business lending. When small businesses like Republic Windows and Doors in Chicago lose their financing, they often have to shutter their doors, leading to mass layoffs. 56% of small businesses that have problems finding credit reported having to lay off employees as a result in a National Small Business Association survey.[63] Between October 2008 and April 2009, small business lending through the Small Business Administration's main program decreased 42% over the previous year.[64] Meanwhile, the national unemployment rate skyrocketed, from 6.2% in September 2008 to 9.7% in August 2009.[65]

But at the same time that banks are cutting small business loans, they are continuing to lend to large corporations and private equity firms. For example, Bank of America, JPMorgan Chase, Citigroup, Goldman Sachs, and Morgan Stanley all helped finance the $68 billion Pfizer-Wyeth merger, which will likely result in thousands of layoffs.[66] Bank of America, JPMorgan Chase, Citigroup, and Morgan Stanley are all among the banks providing $3.1 billion in financing to help private equity-owned Warner Chilcott buy Procter and Gamble's drug business.[67]

Standing in the Way of Reform

After crashing the economy and taking trillions of dollars in bailouts and backstops, the banks are now using our own money against us. They are spending millions of dollars of our money to lobby against reforms that would protect us from their abuses in the future. In the nine months following the bailout, companies in the financial, insurance, and real estate sector (which includes banks and other bailed-out companies like AIG), spent $321 million on lobbying.[68] The top six banks alone spent $28.4 million lobbying during this time.[69]

Many banks lobbied against policies that would help protect Americans, both as taxpayers and consumers. They fought against:

- The formation of a Consumer Financial Protection Agency to protect consumers' interests;[70]
- Limits on executive compensation and bonuses to ensure banks don't use taxpayer dollars to pay out bonuses;[71]
- The regulation of overdraft fees to protect American consumers from misleading and potentially predatory bank policies;[72]
- Credit card reform, including caps on interest rates and a ban on anytime-for-any-reason rate hikes;[73]
- Loan modification proposals to help keep millions of Americans in their homes;[74] and
- A ban on payday lending.[75]

The big banks' predatory and abusive business practices cost us trillions of dollars in lost wealth and brought the economy to the brink of collapse. Now they are fighting an all out war to preserve the ability to do it all over again, and they are using our money as the ammunition.

A Real Economic Recovery

Now that the big banks are back to profitability, their promoters would have us believe that the worst is behind us. Wall Street celebrates 'green shoots' in the economy and points to signs of an economic recovery, but Main Street is still hurting.

This feels like déjà vu. The market was celebrating signs of recovery last year too, just months before the Lehman Brothers collapse.

In July 2008, according to the *Los Angeles Times*, President George Bush tried to calm the markets by saying, "We will come through this challenge stronger than ever before. Our economy has continued growing, consumers are spending, businesses are investing, exports continue increasing, and American productivity remains strong."[76] A month later in late August, the new GDP report showed US economic growth to be "much stronger than previously believed."[77] And finally, two weeks later, on September 15th, the morning that Lehman collapsed, Senator John McCain asserted forcefully that "the fundamentals of our economy are strong."[78]

Similarly, this year, we've seen repeated efforts to sound the trumpets and declare victory prematurely. For example, even though the market has celebrated big banks profits so far this year, the *Huffington Post* reported that "The percent of banks that lost money [in the second] quarter set an all-time high."[79] In fact, the percentage of banks that were unprofitable in the first half of 2009 is up 59% from last year. 2008 was the industry's worst year for profitability, and 2009 is currently on pace to beat it.[80]

This has been going on all summer. First in May, even before the results of the Treasury Department's "stress tests" of the largest financial institutions came out, the *New York Times* reported that the Obama administration "seems prepared to argue that...the broad financial system is healthier than many investors fear."[81] The stress tests showed that the biggest financial institutions needed to raise an additional $75 billion.[82] It was later revealed that the number had actually been revised downwards at the behest of the banks, and that the Federal Reserve's initial findings had put the number even higher.[83]

Then in June, *Dow Jones* reported that a decline in credit card delinquencies in the previous month was "igniting hope of a turnaround among investors of plastic," even though the same article also noted that actual credit card losses had continued to climb.[84] A month and a half later, the government celebrated that "the overall economy contracted at an annual rate of only 1 percent in the spring quarter..."[85] To Wall Street, that may be a reason to rejoice. To the average American, it means things continued to get worse.

In early August, the *New York Times* reported that "The most heartening employment report since last summer suggested on Friday that a recovery was under way..."[86] This "heartening" report actually showed an additional quarter million job losses in the month of July, and while the seasonally-adjusted unemployment rate declined a tenth of a percentage point, it was "mainly because so many people dropped out of the hunt for work, ceasing to list themselves as unemployed."[87] Once again, the market was not celebrating things better, but that they were getting worse more slowly.

Then towards the end of August, another *New York Times* article reported that Standard & Poor's Case-Shiller Home Price Index was showing improvements in major cities across the country, "[i]n a convincing sign that the worst housing slump of modern times is coming to an end..."[88] But at the end of the same article, there was a brief mention of the fact that "with unemployment nearing 10 percent, there are probably more foreclosures to come...," which could push prices back down,[89] making that "convincing" sign of a reversal of fortunes seem a little less convincing.

That same week, Federal Reserve officials started pushing out the message that taxpayers had actually made multibillion dollar profits off of the banks that had repaid their TARP funds.[90] But as *Rolling Stone* writer Matt Taibbi pointed out in his blog, "This is sort of like calculating the returns on a mutual fund by only counting the stocks in the fund that have gone up," since only the healthiest banks have repaid their TARP funds so far.[91] A recent study actually found that TARP was $148 billion in the red as of June.[92]

All the chatter about economic recovery and the end of the recession is no more credible now that it was a year ago. In fact, as financial stocks tumbled at the start of September, even *CNNMoney* reported about "worries that market gains have raced ahead of any economic recovery."[93] Wall Street's eternal optimism when it comes to the economy is just a distraction to keep us from demanding real regulatory reform so that the big banks can carry on with business as usual, robbing us of trillions of dollars for decades to come.

We need a real economic recovery. The banks broke the economy, made us pay for repairs that benefitted bankers but have had little effect on the rest of us, and now are readying to break it again at our expense. It is time for them to fix what they broke and to get the economy back on track in a way that works for us, the taxpayers who bailed them out when their backs were against the wall.

Endnotes

[1] Andrew Ross Sorkin and Vikas Bajaj, "Shift for Goldman and Morgan Marks the End of an Era," New York Times, 22 Sep 2008, http://www.nytimes.com/2008/09/22/business/22bank.html.
[2] Jim Kuhnhenn, "US financial market bailout tab hits $4.7 trillion," Associated Press, 20 Jul 2009, http://www.google.com/hostednews/ap/article/ALeqM5heUXausbmwbNjC7_DaF4ZnJ3dYhgD99IEBJG4.
[3] Matt Taibbi, "The Great American Bubble Machine," Rolling Stone, 13 Jul 2009, http://www.rollingstone.com/politics/story/29127316/the_great_american_bubble_machine; Andrew Bary, "How Do You Spell Sweet Deal? For Banks, It's TLGP," Barron's, 18 Apr 2009, http://online.barrons.com/article/SB124001886675331247.html.
[4] "Payments to AIG Securities Lending Counterparties," AIG, http://msnbcmedia.msn.com/i/CNBC/Sections/News_And_Analysis/_News/__EDIT%20London/AIG_Counterparties_List.pdf.
[5] Treasury Department documents from the Federal Reserve Bank Board of Governors, Federal Reserve Bank of New York, FDIC, SIGTARP, and FinancialStability.gov.
[6] S. Mitra Kalita, "Americans See 18% of Wealth Vanish," Wall Street Journal, 13 Mar 2009, http://online.wsj.com/article/SB123687371369308675.html.
[7] "Americans Lose $1.4 Trillion in Home Values in Q4; More Than was Lost in All of 2007," Reuters, 03 Feb 2009, http://www.reuters.com/article/pressRelease/idUS153982+03-Feb-2009+PRN20090203.
[8] "Loss of home equity is the crux of crisis," NOR Marketplace, 24 Dec 2008, http://marketplace.publicradio.org/display/web/2008/11/24/dean_baker_commentary/?refid=0#.
[9] Kent Anderson, "A New Foreclosure Every Thirteen Seconds," Mortgage Law Network," 23 Feb 2009, http://www.mortgagelawnetwork.com/a-new-foreclosure-every-thirteen-seconds/.
[10] http://www.nytimes.com/2009/08/28/opinion/28fri1.html
[11] Al Yoon, "About half of US mortgages seen underwater by 2011," Reuters, 05 Aug 2009, http://news.yahoo.com/s/nm/20090805/bs_nm/us_usa_housing_deutschebank.
[12] Al Yoon, "About half of US mortgages seen underwater by 2011," Reuters, 05 Aug 2009, http://news.yahoo.com/s/nm/20090805/bs_nm/us_usa_housing_deutschebank.
[13] "Lenders avoid redoing loans, Fed concludes," Boston Globe, 07 Jul 2009, http://www.boston.com/business/articles/2009/07/07/lenders_avoid_redoing_loans_fed_concludes/?page=full.
[14] Peter S. Goodman, "Lucrative Fees May Deter Efforts to Alter Loans," New York Times, 30 Jul 2009, http://www.nytimes.com/2009/07/30/business/30services.html?_r=2&scp=1&sq=late%20fee%20profits&st=cse.
[15] Peter S. Goodman, "Lucrative Fees May Deter Efforts to Alter Loans," New York Times, 30 Jul 2009, http://www.nytimes.com/2009/07/30/business/30services.html?_r=2&scp=1&sq=late%20fee%20profits&st=cse.
[16] Peter S. Goodman, "Lucrative Fees May Deter Efforts to Alter Loans," New York Times, 30 Jul 2009, http://www.nytimes.com/2009/07/30/business/30services.html?_r=2&scp=1&sq=late%20fee%20profits&st=cse.
[17] Dawn Kopecki, "Bank of America Among Worst for Loan Modifications," Bloomberg, 04 Aug 2009, http://www.bloomberg.com/apps/news?pid=washingtonstory&sid=aaiRx.lyFD4I#.
[18] Andrew M. Cuomo, "No Rhyme or Reason: The 'Heads I Win, Tails You Lose' Bank Bonus Culture," Jul 2009, Appendix C, pages 14-21, http://www.oag.state.ny.us/media_center/2009/july/pdfs/Bonus%20Report%20Final%207.30.09.pdf.
[19] Bureau of Labor Statistics Monthly Employment Data.
[20] Bureau of Labor Statistics Monthly Employment Data.
[21] "US food stamp list tops 34 million for first time," Reuters, 06 Aug 2009, http://www.forbes.com/feeds/reuters/2009/08/06/2009-08-06T152646Z_01_N06328040_RTRIDST_0_FOODSTAMPS-USA.html.
[22] Bureau of Labor Statistics Monthly Employment Data.
[23] Arthur Delaney, "Unemployment Rate Hits 9.7 Percent As Economy Sheds 216,000 Jobs in August," Huffington Post, 04 Sep 2009, http://www.huffingtonpost.com/2009/09/04/unemployment-hits-97-as-e_n_277218.html.
[24] "US food stamp list tops 34 million for first time," Reuters, 06 Aug 2009, http://www.forbes.com/feeds/reuters/2009/08/06/2009-08-06T152646Z_01_N06328040_RTRIDST_0_FOODSTAMPS-USA.html.

[25] Nancy Trejos, "Personal Bankruptcy Surges 34 Percent," Washington Post, 14 Aug 2009, http://www.washingtonpost.com/wp-dyn/content/article/2009/08/13/AR2009081303399.html.
[26] Nancy Trejos, "Personal Bankruptcy Surges 34 Percent," Washington Post, 14 Aug 2009, http://www.washingtonpost.com/wp-dyn/content/article/2009/08/13/AR2009081303399.html.
[27] Nancy Trejos, "Personal Bankruptcy Surges 34 Percent," Washington Post, 14 Aug 2009, http://www.washingtonpost.com/wp-dyn/content/article/2009/08/13/AR2009081303399.html.
[28] Christine Williamson, "Top 1,000 funds drop close to $1 trillion," Pensions & Investments, 26 Jan 2009, http://www.pionline.com/apps/pbcs.dll/article?AID=/20090126/PRINTSUB/301269981/-1/PENSIONFUNDDIRECTORY&template=printart&AssignSessionID=273361946539658.
[29] Calculation is $6.1 trillion x 0.95%, the median effective property tax rate for U.S. owner-occupied housing, according to the Tax Foundation: http://www.taxfoundation.org/files/proptax_owner-occ_bystate2004-2007-20080923.xls.
[30] Christopher W. Hoene and Michael A. Pagano, "City Fiscal Conditions in 2009," National League of Cities, Sep 2009, page 6, http://www.nlc.org/ASSETS/E0A769A03B464963A81410F40A0529BF/CityFiscalConditions_09%20%282%29.pdf.
[31] Elizabeth McNichol and Iris J. Lav, "New Fiscal Year Brings No Relief From Unprecedented State Budget Problems," Center for Budget and Policy Priorities, 12 Aug 2009, page 1, http://www.cbpp.org/9-8-08sfp.htm.
[32] Nicholas Johnson, Phil Oliff, and Jeremy Koulish, "An Update on State Budget Cuts," Center for Budget and Policy Priorities, 29 Jun 2009, pages 5-11, http://www.cbpp.org/files/3-13-08sfp.pdf.
[33] Stephen Labaton, "Treasury to Set Executives' Pay at 7 Ailing Firms," New York Times, 11 Jun 2009, http://www.nytimes.com/2009/06/11/business/11pay.html.
[34] Andrew M. Cuomo, "No Rhyme or Reason: The 'Heads I Win, Tails You Lose' Bank Bonus Culture," Jul 2009, page 3, http://www.oag.state.ny.us/media_center/2009/july/pdfs/Bonus%20Report%20Final%207.30.09.pdf.
[35] Andrew M. Cuomo, "No Rhyme or Reason: The 'Heads I Win, Tails You Lose' Bank Bonus Culture," Jul 2009, page 1, http://www.oag.state.ny.us/media_center/2009/july/pdfs/Bonus%20Report%20Final%207.30.09.pdf.
[36] Andrew M. Cuomo, "No Rhyme or Reason: The 'Heads I Win, Tails You Lose' Bank Bonus Culture," Jul 2009, Appendix A, page 5, http://www.oag.state.ny.us/media_center/2009/july/pdfs/Bonus%20Report%20Final%207.30.09.pdf.
[37] Andrew M. Cuomo, "No Rhyme or Reason: The 'Heads I Win, Tails You Lose' Bank Bonus Culture," Jul 2009, Appendix C, pages 14-21, http://www.oag.state.ny.us/media_center/2009/july/pdfs/Bonus%20Report%20Final%207.30.09.pdf.
[38] Andrew M. Cuomo, "No Rhyme or Reason: The 'Heads I Win, Tails You Lose' Bank Bonus Culture," Jul 2009, Appendix C, pages 14-21, http://www.oag.state.ny.us/media_center/2009/july/pdfs/Bonus%20Report%20Final%207.30.09.pdf.
[39] Patrick Jenkins, "Wall St pay soars in bid to halt talent exodus," Financial Times, 22 Jun 2009, http://www.ft.com/cms/s/0/7475d4ce-5ec5-11de-91ad-00144feabdc0.html.
[40] Eric Dash, "Citigroup Has a Plan to Fatten Salaries," New York Times, 24 Jun 2009, http://www.nytimes.com/2009/06/24/business/24citigroup.html.
[41] Greg Farrell, "Merrill in aggressive hiring push," Financial Times, 14 Aug 2009, http://www.ft.com/cms/s/0/d9fabc32-8874-11de-82e4-00144feabdc0.html.
[42] Andrew M. Cuomo, "No Rhyme or Reason: The 'Heads I Win, Tails You Lose' Bank Bonus Culture," Jul 2009, Appendix C, pages 14-21, http://www.oag.state.ny.us/media_center/2009/july/pdfs/Bonus%20Report%20Final%207.30.09.pdf.
[43] Joe Bel Bruno, "Goldman Winning Streak: $50 Million a Day," Wall Street Journal, 06 Aug 2009, http://online.wsj.com/article/SB124948551533308045.html.
[44] Nomi Prins, "How You Finance Goldman Sachs' Profits," Mother Jones, 28 Jul 2009, http://www.motherjones.com/politics/2009/07/how-you-finance-goldman-sachs%E2%80%99-profits.
[45] Jessica Silver-Greenberg, Theo Francis, and Ben Levisohn, "Old Banks, New Lending Tricks," Business Week, 05 Aug 2009, http://www.businessweek.com/magazine/content/09_33/b4143020536818.htm.
[46] Jessica Silver-Greenberg, Theo Francis, and Ben Levisohn, "Old Banks, New Lending Tricks," Business Week, 05 Aug 2009, http://www.businessweek.com/magazine/content/09_33/b4143020536818.htm.

[47] "Up to Old Tricks, Wall Street Repackages Bad Mortgages," Associated Press, 24 Aug 2009, http://www.huffingtonpost.com/2009/08/24/up-to-old-tricks-wall-str_n_267066.html.
[48] Jessica Silver-Greenberg, Theo Francis, and Ben Levisohn, "Old Banks, New Lending Tricks," Business Week, 05 Aug 2009, http://www.businessweek.com/magazine/content/09_33/b4143020536818.htm.
[49] Marshall Eckblad, "In Banks' Profit Push, 'Era of Low Fees Is Over,'" Wall Street Journal, 31 Jul 2009, http://online.wsj.com/article/SB124899068710295093.html.
[50] "Debit Card Trap," New York Times Editorial, 20 Aug 2009, http://www.nytimes.com/2009/08/20/opinion/20thu1.html?_r=1.
[51] Jeff Ostrowski, "Banks feast on billions in overdraft fees," Palm Beach Post, 23 Aug 2009, http://www.palmbeachpost.com/news/content/business/epaper/2009/08/23/a1b_bankfees_0824.html.
[52] $38 billion divided by the US population, per US Census: http://www.census.gov/.
[53] Eric Dash, "Bank Fees Rise as Lenders Try to Offset Losses," New York Times, 02 Jul 2009, http://www.nytimes.com/2009/07/02/business/02fees.html?_r=1.
[54] California Reinvestment Coalition Overdraft Guide, Nov 2007, http://www.calreinvest.org/system/assets/99.pdf; Bank of America Personal Schedule of Fees, effective 05 Jun 2009, https://www3.bankofamerica.com/efulfillment/documents/91-11-3000ED.20090605.htm; Jane J. Kim, "Bank Suspends Overdraft Fee Increase," Wall Street Journal, 13 Apr 2009, http://online.wsj.com/article/SB123967277269015845.html.
[55] Marshall Eckblad, "In Banks' Profit Push, 'Era of Low Fees Is Over,'" Wall Street Journal, 31 Jul 2009, http://online.wsj.com/article/SB124899068710295093.html.
[56] Eric Dash, "Bank Fees Rise as Lenders Try to Offset Losses," New York Times, 02 Jul 2009, http://www.nytimes.com/2009/07/02/business/02fees.html?_r=1.
[57] Eric Dash, "Bank Fees Rise as Lenders Try to Offset Losses," New York Times, 02 Jul 2009, http://www.nytimes.com/2009/07/02/business/02fees.html?_r=1.
[58] Nancy Trejos, "Credit Card Issuers Raising Rates Ahead of New Law," Washington Post, 02 Jul 2009, http://www.washingtonpost.com/wp-dyn/content/article/2009/07/01/AR2009070103868.html.
[59] Franceso Guerrera, Saskia Scholtes, and Tom Braithwaite, "Citi raises card rates on millions," Financial Times, 30 Jun 2009, http://www.ft.com/cms/s/0/e1d0c610-65c7-11de-8e34-00144feabdc0.html?nclick_check=1.
[60] Lore Croghan, "Credit card hike fright: Banks raising rates, even if you've paid on time," New York Daily News, 16 Mar 2009, http://www.nydailynews.com/money/2009/03/16/2009-03-16_credit_card_hike_fright_banks_raising_ra.html.
[61] "Credit-card users get rate shock," Baltimore Sun, 19 Feb 2008, http://www.baltimoresun.com/business/bal-bz.cardrates19feb19,0,2452533.story.
[62] Nancy Trejos, "Credit Card Issuers Raising Rates Ahead of New Law," Washington Post, 02 Jul 2009, http://www.washingtonpost.com/wp-dyn/content/article/2009/07/01/AR2009070103868.html.
[63] National Small Business Association 2009 Small Business Credit Card Survey, page 9, http://www.nsba.biz/docs/09CCSurvey.pdf.
[64] "Small Business Lending at Bank of America," SEIU, 22 Jul 2009, page 3, http://www.seiu.org/change-that-works/bank-of-america/bofa-smbiz-final.pdf.
[65] BLS Monthly Employment Data.
[66] "Bank bailout recipients' link to Pfizer deal," TradingMarkets.com, 27 Jan 2009, http://www.tradingmarkets.com/.site/news/Stock%20News/2145293/.
[67] Felix Salmon, "Private equity releverages with a vengeance," Reuters Blog, 25 Aug 2009, http://blogs.reuters.com/felix-salmon/2009/08/25/private-equity-releverages-with-a-vengeance/.
[68] "TARP Recipients Paid Out $114 Million for Politicking Last Year," Capital Eye Blog, OpenSecrets.org, 04 Feb 2009, http://www.opensecrets.org/news/2009/02/tarp-recipients-paid-out-114-m.html; Elizabeth Williamson, T.W. Farnam, and Brody Mullins, "Finance Lobby Cut Spending as Feds Targeted Wall Street," Wall Street Journal, 01 Jul 2009, http://online.wsj.com/article/SB124640640747376775.html.
[69] Lobbying Disclosure Act Database, http://soprweb.senate.gov/index.cfm?event=selectfields.
[70] Edmund L. Andrews, "Banks Balk at Agency Meant to Aid Consumers," New York Times, 01 Jul 2009, http://www.nytimes.com/2009/07/01/business/economy/01regulate.html?_r=1.

[71] Jane Hamsher, "Bailout Recipients Spent $13 Million Lobbying Against Consumers, For Their Own Bonuses in 1Q 2009," FireDogLake.com, 06 May 2009, http://firedoglake.com/2009/05/06/tarp-recipients-spent-taxpayer-dollars-lobbying-against-consumers-for-their-own-bonuses-in-1q-2009/.
[72] American Bankers Association Policy Position on Unfair and Deceptive Acts and Practices, http://www.aba.com/Issues/Issues_UnfairDeceptive.htm.
[73] Lobbying Disclosure Act Database, http://soprweb.senate.gov/index.cfm?event=selectfields.
[74] Ryan Grim, "Cramdown Vote: Banks Bought Senators On The Cheap," Huffington Post, 01 May 2009, http://www.huffingtonpost.com/2009/04/30/cramdown-vote-banks-bough_n_193674.html.
[75] Lobbying Disclosure Act Database, http://soprweb.senate.gov/index.cfm?event=selectfields.
[76] Maura Reynolds and Walter Hamilton, "Economic indicators point to more distress," Los Angeles Times, 16 Jul 2008, http://articles.latimes.com/2008/jul/16/business/fi-econ16.
[77] Greg Robb, "Second-quarter growth revised significantly higher," MarketWatch, 28 Aug 2008, http://www.marketwatch.com/story/revised-us-gdp-surges-33-high-water-mark-for-growth?print=true&dist=printMidSection.
[78] "As Wall Street collapses, McCain declares that 'the fundamentals of our economy are strong,'" Think Progress, 15 Sep 2008, http://thinkprogress.org/2008/09/15/as-wall-street-collapses-mccain-declares-that-the-funamentals-of-our-economy-are-strong/.
[79] Shahien Nasiripour, "Percent of Money-Losing Banks Set An All-Time High In Second Quarter," Huffington Post, 31 Aug 2009, http://www.huffingtonpost.com/2009/08/31/percent-of-money-losing-b_n_272893.html.
[80] Shahien Nasiripour, "Percent of Money-Losing Banks Set An All-Time High In Second Quarter," Huffington Post, 31 Aug 2009, http://www.huffingtonpost.com/2009/08/31/percent-of-money-losing-b_n_272893.html.
[81] David Leonhardt, "Tests of Banks May Bring More Hope Than Fear," New York Times, 04 May 2009, http://www.nytimes.com/2009/05/04/us/politics/04stress.html?_r=2&pagewanted=1.
[82] Edmund L. Andrews, "Ailing Banks Need $75 Billion, U.S. Says," New York Times, 08 May 2009, http://www.nytimes.com/2009/05/08/business/08stress.html?_r=1.
[83] David Reich, Dan Fitzpatrick, and Marshall Eckblad, "Banks Won Concessions on Tests," Wall Street Journal, 09 May 2009, http://online.wsj.com/article/SB124182311010302297.html.
[84] Aparajita Saha-Bubna, "Losses Rose On Credit Cards In Mayl Delinquences Fell A Bit," Dow Jones, 16 Jun 2009, http://online.wsj.com/article/BT-CO-20090616-713276.html.
[85] Jack Healy and Louis Uchitelle, Job Losses Slow, Signaling Shift in the Economy," New York Times 08 Aug 2009, http://www.nytimes.com/2009/08/08/business/economy/08jobs.html?_r=3&hp.
[86] Jack Healy and Louis Uchitelle, Job Losses Slow, Signaling Shift in the Economy," New York Times 08 Aug 2009, http://www.nytimes.com/2009/08/08/business/economy/08jobs.html?_r=3&hp.
[87] Jack Healy and Louis Uchitelle, Job Losses Slow, Signaling Shift in the Economy," New York Times 08 Aug 2009, http://www.nytimes.com/2009/08/08/business/economy/08jobs.html?_r=3&hp.
[88] David Streitfeld, "Index Shows an Improvement in Home Prices," New York Times, 26 Aug 2009, http://www.nytimes.com/2009/08/26/business/economy/26econ.html.
[89] David Streitfeld, "Index Shows an Improvement in Home Prices," New York Times, 26 Aug 2009, http://www.nytimes.com/2009/08/26/business/economy/26econ.html.
[90] Zachery Kouwe, "As Banks Repay Bailout Money, U.S. Sees Profit," New York Times, 31 Aug 2009, http://www.nytimes.com/2009/08/31/business/economy/31taxpayer.html?_r=2&hp.
[91] Mat Taibbi, "Bailout Propaganda Begins," True/Slant, 01 Sep 2009, http://trueslant.com/matttaibbi/2009/09/01/bailout-propaganda-begins/.
[92] Mat Taibbi, "Bailout Propaganda Begins," True/Slant, 01 Sep 2009, http://trueslant.com/matttaibbi/2009/09/01/bailout-propaganda-begins/.
[93] Alexandra Twin, "Wall Street stumbles into September," CNNMoney.com, 01 Sep 2009, http://money.cnn.com/2009/09/01/markets/markets_newyork/index.htm?postversion=2009090115.